# ALJ REGIONAL HOLDINGS, INC.

**244 Madison Avenue**
**PMB #358**
**New York, New York 10016**

**(212) 883-0083**

**Quarterly Report for the**
**Period Ended**
**December 31, 2012**

# ALJ REGIONAL HOLDINGS, INC.

## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Statements in this report (the "Report") regarding financial and operating performance and other statements that are not historical facts, including, among others, statements regarding the Company's business strategy following its disposition of its former operating subsidiary, KES Acquisition Company, a Delaware corporation ("KES"), its ability to identify and successfully acquire and integrate other operating businesses, and its ability to offset future income against net operating loss carryovers ("NOLs") and use its rights plan to preserve NOLs, constitute forward-looking statements. In general, you can identify forward-looking statements by the presence of words such as "anticipate," "believe," "estimate," "expect, "intend," "may", "plan," "predict," "project," "will," and similar expressions.

Forward-looking statements are based on reasonable expectations and are subject to risks and uncertainties. Actual results will differ, perhaps materially, from those set forth or implied by such forward-looking statements due to a variety of factors, including, among others:

- The Company's lack of operations and limited ability to raise financing;
- Uncertainties related to the Company's intent to invest in or acquire control of one or more operating businesses, including its ability to identify, diligence, negotiate, raise financing for and successfully acquire and integrate any operating businesses;
- The Company's ability to acquire operating businesses before its lack of operations impairs its NOLs or subjects it to additional regulatory requirements;
- Uncertainties related to the industry and particular operating businesses which the Company may eventually acquire;
- The Company's ability to compete successfully against other potential acquirers of operating businesses with more experience and resources;
- Uncertainties related to management's investment of the Company's cash pending any acquisitions or strategic investments;
- Uncertainties related to a downturn in general economic conditions or consumer confidence, including changes in conditions of U.S. or international lending, capital and financing markets;
- Changes in tax laws or regulations regarding the use or preservation of NOLs; and
- Private or governmental liability claims or litigation, or the impact of any adverse outcome of any litigation on the adequacy of the Company's reserves, the availability or adequacy of its insurance coverage, its financial well-being or its business and assets.

The Company is also subject to general business risks, including its success in continuing to settle the Company's outstanding obligations from its prior business activities, results of tax audits, the Company's ability to retain and attract key employees, acts of war or global terrorism, and unexpected natural disasters.

Any forward-looking statements included in this Report are made as of the date hereof and based on information available to the Company as of the date hereof. Subject to applicable law, the Company assumes no obligation to update any forward-looking statements.

## TABLE OF CONTENTS


| | Page |
|---|---|
| ITEM 1. EXACT NAME OF THE ISSUER AND THE ADDRESS OF ITS PRINCIPAL EXECUTIVE OFFICES | 3 |
| ITEM 2. SHARES OUTSTANDING | 3 |
| ITEM 3. INTERIM FINANCIAL STATEMENTS | 4 |
| CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED) | 4 |
| CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED) | 6 |
| CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED) THREE MONTHS ENDED DECEMBER 31, 2012 | 7 |
| CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) | 8 |
| NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) DECEMBER 31, 2012 | 9 |
| ITEM 4. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION | 20 |
| ITEM 5. LEGAL PROCEEDINGS | 27 |
| ITEM 6. DEFAULTS UPON SENIOR SECURITIES | 27 |
| ITEM 7. OTHER INFORMATION | 27 |
| RISK FACTORS | 27 |
| ITEM 8. EXHIBITS | 36 |
| ITEM 9. CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER | 37 |

## ITEM 1. EXACT NAME OF THE ISSUER AND THE ADDRESS OF ITS PRINCIPAL EXECUTIVE OFFICES

ALJ Regional Holdings, Inc. ("ALJ" or the "Company") has its principal offices at:

244 Madison Avenue, PMB 358
New York, NY 10016
Phone: (212) 883-0083
Fax: (606) 929-1261

References to the "Company," "we," "us" and "our" are to the consolidated operations of ALJ, including the operations of its subsidiaries, except to the extent the context is intended to refer only to ALJ. The Company was originally incorporated in the State of Delaware under the name Nuparent, Inc. on June 22, 1999. The Company's name was changed to YouthStream Media Networks, Inc. on June 24, 1999 and that name was used through October 23, 2006. The Company's name was changed to ALJ Regional Holdings, Inc. on October 23, 2006.

The Company maintains a website at www.aljregionalholdings.com.

The Company's investor relations contact is Jess Ravich, the Chairman of the Board. Mr. Ravich can be reached at (213) 244-0045.

The Company's transfer agent is American Stock Transfer & Trust Company, LLC whose address and phone number are:

American Stock Transfer & Trust Company, LLC
Operations Center
6201 15th Avenue
Brooklyn, NY 11219
(718) 921-8293

## ITEM 2. SHARES OUTSTANDING

The Company has only two classes of securities; common stock and preferred stock, the details of which are disclosed in the table below.

| | Common Stock Period End Date | | | Preferred Stock Period End Date | | |
|---|---|---|---|---|---|---|
| | December 31, 2012 | September 30, 2012 | September 30, 2011 | December 31, 2012 | September 30, 2012 | September 30, 2011 |
| **Number of Shares Authorized** | 100,000,000 | 100,000,000 | 100,000,000 | 5,000,000 | 5,000,000 | 5,000,000 |
| **Number of Shares Outstanding** | 57,446,598 | 57,246,598 | 56,934,040 | 0 | 0 | 0 |

Of the 5,000,000 shares of preferred stock authorized, 1,000,000 shares have been designated as Series A Preferred Stock, none of which are currently issued and outstanding and 550,000 shares have been designated as Series B Preferred Stock, none of which are currently issued and outstanding.

As of December 31, 2012, there were 202 holders of record of the Company's common stock.

## ITEM 3. INTERIM FINANCIAL STATEMENTS

## EXPLANATORY NOTE

As described in more detail under Note 16 – "Subsequent Events" – below, effective February 5, 2013, ALJ sold its majority owned subsidiary KES. KES, which owned and operated a steel mini-mill (the "Mill"), represented the only business segment in which the Company operated as of December 31, 2012. Therefore, the interim financial statements set forth below reflect the historical operations of KES. Because ALJ no longer owns KES, KES' operations will not be included in ALJ's consolidated financial statements after February 5, 2013. Following the disposition of KES, ALJ has no or only nominal operations and, other than the cash received from the sale of KES and ALJ's other cash on hand, an immaterial amount of assets.

### ALJ REGIONAL HOLDINGS, INC.
### CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

| | December 31, 2012 | September 30, 2012 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 568,304 | $ 2,823,576 |
| Accounts receivable, less allowance for doubtful accounts of $699,907 at December 31, 2012 and $534,447 at September 30, 2012 | 8,962,676 | 11,548,624 |
| Inventories | 26,222,749 | 24,005,885 |
| Prepaid expenses and other current assets | 957,017 | 1,252,102 |
| Other receivables | 0 | 71,701 |
| Deferred taxes | 6,285,599 | 6,285,599 |
| Total current assets | 42,996,345 | 45,987,487 |
| | | |
| Property, plant and equipment | 5,177,477 | 5,177,477 |
| Less accumulated depreciation and amortization | (2,997,602) | (2,934,624) |
| Property, plant and equipment, net | 2,179,875 | 2,242,853 |
| | | |
| Other assets: | | |
| Deposits | 224,460 | 224,460 |
| Deferred loan costs, net of amortization | 239,899 | 274,494 |
| Investment in Bellator | 90,228 | 90,228 |
| Total other assets | 554,587 | 589,182 |
| Total assets | $ 45,730,807 | $ 48,819,522 |

(continued)

**ALJ REGIONAL HOLDINGS, INC.**
**CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)**

**(continued)**

| | December 31, 2012 | September 30, 2012 |
|---|---|---|
| LIABILITIES AND STOCKHOLDERS' DEFICIENCY | | |
| Current liabilities: | | |
| Accounts payable | $ 9,329,252 | $ 7,619,591 |
| Accrued expenses | 3,143,365 | 4,522,920 |
| Income taxes payable | 46,478 | 50,485 |
| Current portion of term loans | 3,500,000 | 4,000,000 |
| Liabilities related to discontinued operations | 298,466 | 298,466 |
| Total current liabilities | $ 16,317,561 | $ 16,491,462 |
| Non-current liabilities: | | |
| Secured line of credit | 5,727,109 | 7,167,015 |
| 8% subordinated term loans | 18,998,213 | 18,998,213 |
| Series A Preferred stock of subsidiary subject to mandatory redemption; 13% cumulative, non-convertible, redeemable preferred stock, mandatory redemption and liquidation value of $1,000 per share; 5,936 shares issued and outstanding at December 31, 2012 plus cumulative dividends of $6,602,305, 5,936 shares issued and outstanding at September 30, 2012 plus cumulative dividends of $5,867,750 | 11,998,305 | 11,803,750 |
| Deferred tax liability | 403,746 | 403,746 |
| Minority interest – related parties | 7,060,222 | 7,266,179 |
| Total liabilities | $ 60,505,156 | $ 62,130,365 |
| Commitments and contingencies | | |
| Stockholders' deficiency: | | |
| Common stock, $0.01 par value; authorized - 100,000,000 shares; 57,446,598 issued and outstanding at Dec. 31, 2012 and 57,246,598 issued and outstanding at Sep 30, 2012 | 574,466 | 572,466 |
| Additional paid-in capital | 288,470,728 | 288,426,728 |
| Accumulated deficit | (302,915,385) | (301,405,879) |
| Treasury stock – 786,600 shares, at cost | (904,158) | (904,158) |
| Total stockholders' deficiency | (14,774,349) | (13,310,843) |
| Total liabilities and stockholders' deficiency | $ 45,730,807 | $ 48,819,522 |

See accompanying notes to condensed consolidated financial statements.

## ALJ REGIONAL HOLDINGS, INC.
## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

| | Three Months Ended December 31, | |
|---|---|---|
| | **2012** | **2011** |
| NET SALES | $30,620,403 | $38,894,890 |
| COSTS AND EXPENSES | | |
| Cost of sales | 28,553,295 | 33,403,449 |
| Selling | 517,753 | 537,459 |
| General and administrative | 2,491,568 | 1,612,836 |
| Total cost of operations | 31,562,616 | 35,553,744 |
| Income from operations | (942,213) | 3,341,146 |
| OTHER INCOME (EXPENSE) | | |
| Interest income | 7,239 | 11,393 |
| Interest expense | (711,250) | (967,183) |
| Loan fees | (67,095) | (82,648) |
| Gain on retirement of debt | - | 16,054 |
| Other income | 2,254 | - |
| Total other income (expense) | (768,852) | (1,022,384) |
| INCOME (LOSS) BEFORE INCOME TAXES AND MINORITY INTEREST | (1,711,065) | 2,318,762 |
| Income taxes | (4,398) | (285,953) |
| INCOME (LOSS) BEFORE MINORITY INTEREST | (1,715,463) | 2,032,809 |
| MINORITY INTEREST – related parties | 205,957 | (309,043) |
| NET INCOME (LOSS) | ($1,509,506) | $1,723,766 |
| NET INCOME (LOSS) PER COMMON SHARE - | | |
| Basic | ($0.03) | $0.03 |
| Dilutive | ($0.03) | $0.03 |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING | | |
| Basic | 57,346,598 | 56,934,040 |
| Dilutive | 59,546,598 | 58,534,040 |

See accompanying notes to condensed consolidated financial statements.

## ALJ REGIONAL HOLDINGS, INC.
## CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)
## (UNAUDITED)
## THREE MONTHS ENDED DECEMBER 31, 2012

| | Common Stock | | Additional Paid-in | Accumulated | Treasury | |
|---|---|---|---|---|---|---|
| | Shares | Amount | Capital | Deficit | Stock | Total |
| Balances at September 30, 2012 | 57,246,598 | $ 572,466 | $ 288,426,728 | $ (301,405,879) | $ (904,158) | $ (13,310,843) |
| Share-based compensation: | | | | | | |
| Exercise of stock options | 200,000 | 2,000 | 44,000 | | | 46,000 |
| Net income | | | | (1,509,506) | | (1,509,506) |
| Balances at December 31, 2012 | 57,446,598 | $ 574,466 | $ 288,470,728 | $ (302,915,385) | $ (904,158) | $ (14,774,349) |

See accompanying notes to condensed consolidated financial statements

## ALJ REGIONAL HOLDINGS, INC.
## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

| | Three Months Ended December 31, | |
|---|---|---|
| | **2012** | **2011** |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income (loss) | $ (1,509,506) | $ 1,723,766 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 62,978 | 90,167 |
| Stock-based compensation | - | 6,090 |
| Amortization of original issue discount on subordinated term loans | - | - |
| Amortization of deferred loan costs | 34,595 | 25,900 |
| Provision for bad debts | (165,460) | (92,019) |
| Minority interest – related parties | (205,957) | 309,044 |
| Changes in operating assets and liabilities: | | |
| Decrease (increase) in - | | |
| Accounts receivable, net | 2,751,408 | 2,723,866 |
| Inventories | (2,216,864) | (2,972,204) |
| Prepaid expenses and other receivables | 366,786 | 418,122 |
| Increase (decrease) in - | | |
| Accounts payable | 1,709,661 | (749,580) |
| Accrued expenses | (1,185,000) | 876,992 |
| Income taxes payable | (4,007) | (5,929) |
| NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES | (361,366) | 2,354,215 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Exercise of stock options | 46,000 | - |
| Net borrowings (repayments) under equipment capital lease obligation | - | (40,985) |
| Net borrowings (repayments) under 8% term loans | - | 530,595 |
| Accrued dividends (repayments) of Preferred Stock | - | 194,555 |
| Repayments on term loans | (500,000) | (1,035,208) |
| Net repayments under secured line of credit | (1,439,906) | (1,013,363) |
| NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES | (1,893,906) | (1,364,406) |
| NET CASH PROVIDED BY (USED IN) OPERATING, INVESTING AND FINANCING ACTIVITIES | (2,255,272) | 989,809 |
| CASH AND CASH EQUIVALENTS | | |
| Net increase (decrease) | (2,255,272) | 989,809 |
| Balance at beginning of period | 2,823,576 | 1,282,228 |
| Balance at end of period | 568,304 | 2,272,037 |
| SUPPLEMENTAL CASH FLOW INFORMATION | | |
| Cash paid for - | | |
| Interest | 147,510 | 132,828 |
| Income taxes | - | 351,698 |

See accompanying notes to condensed consolidated financial statements.

**ALJ REGIONAL HOLDINGS, INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**
**DECEMBER 31, 2012**

## 1. Organization and Basis of Presentation

### Basis of Presentation

The accompanying consolidated financial statements include the accounts of ALJ Regional Holdings, Inc. ("ALJ" or the "Company"), and its direct and indirect wholly and majority-owned subsidiaries. The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America. All inter-company items and transactions have been eliminated in consolidation.

Commencing March 1, 2005, the Company has included the operations of the Mill owned and operated by its majority owned subsidiary KES in its consolidated financial statements (see Note 2 to Consolidated Financial Statements), which represents the only business segment in which the Company operated as of December 31, 2012.

As described in more detail under Note 16 – "Subsequent Events" – below, effective February 5, 2013, the Company sold KES. Therefore, the interim financial statements and these notes thereto reflect the historical operations of KES. Because the Company no longer owns KES, KES' operations will not be included in the Company's consolidated financial statements after February 5, 2013. Following the disposition of KES, the Company has no or only nominal operations and, other than the cash received from the sale of KES and the Company's other cash on hand, an immaterial amount of assets.

The accompanying condensed consolidated financial statements are unaudited, but in the opinion of Company management, contain all adjustments, which include normal recurring accruals, necessary to present fairly the financial position at December 31, 2012 and September 30, 2012, the results of operations for the three months ended December 31, 2012 and 2011, and the cash flows for the three months ended December 31, 2012 and 2011.

Certain information and footnote disclosures normally included in financial statements that have been prepared in accordance with generally accepted accounting principles have been condensed or omitted, although management of the Company believes that the disclosures contained in these financial statements are adequate to make the information presented therein not misleading.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Given the Company's disposition of KES, the results of operations for the three months ended December 31, 2012 are not indicative of the results of operations to be expected for the full fiscal year ending September 30, 2013.

### Liquidity and Capital Resources

The Company recognized net loss of $1.5 million for the three month period ended December 31, 2012 and generated a negative cash flow from operating activities of $361,366 for the three months ended December 31, 2012. The Company used $1.9 million in financing activities and had an accumulated deficit of $302.9 million and a stockholders' deficiency of $14.8 million at December 31, 2012.

The Company recognized net income of $13.3 million for the year ended September 30, 2012 and generated a positive cash flow from operating activities of $14.7 million for the year ended September 30, 2012. The Company used $13.1 million in financing activities, $70,274 from investing activities and had a

stockholder's deficit of $13.3 million, which was primarily comprised of an accumulated deficit of $301.4 million, partially offset by an increase in additional paid-in-capital of $288.4 million at September 30, 2012.

On February 5, 2013, the Company sold KES to Optima Specialty Steel, Inc. ("Optima") for $112.5 million. After satisfying all of KES's liabilities, the Company was able to increase the cash on its balance sheet to approximately $52 million.

Following the disposition of KES, ALJ believes that its current cash resources will be adequate to fund its operations through December 31, 2013. However, to the extent the Company's estimates are inaccurate or its assumptions are incorrect, the Company may not have sufficient cash resources to fund its operations. In such event, the Company may have to seek additional financing for the business.

The Company plans to use its cash resources for future acquisitions or investments in other companies and businesses or for other strategic options. However, the Company is not required to make any such acquisitions, and at this time no specific acquisition targets have been determined. Further, there can be no assurances that such efforts will ultimately be successful. The Company may finance any acquisitions through a combination of debt and/or the issuance of equity securities.

## 2. Nature of Operations and Summary of Significant Accounting Policies

### Nature of Operations

ALJ is a holding company, whose primary asset is a majority share of the outstanding common stock and 100% of the voting securities of KES, the owner and operator of the Mill, which manufactures and sells steel bar flats.

### Cash and Cash Equivalents

Cash and equivalents include all cash, demand deposits and money market accounts with original maturities of three months or less.

### Accounts Receivable

The Company grants credit to its customers generally in the form of short-term trade accounts receivable. Management evaluates the credit risk of its customers utilizing historical data and estimates of future performance.

Accounts receivable are stated at the amount management expects to collect from outstanding balances. When appropriate, management provides for probable uncollectible amounts through a provision for doubtful accounts and an adjustment to a valuation allowance. Management reviews and adjusts this allowance periodically based on the aging of accounts receivable balances, historical write-off experience, customer concentrations, customer creditworthiness and current industry and economic trends. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

### Inventory

Inventories are comprised of raw materials (consisting of alloys and scrap metal), semi-finished goods (billets) and finished goods. Inventory costs include material, labor and manufacturing overhead. Inventories are valued at the lower of average cost or market. The average cost of the billets and scrap metal is adjusted periodically to reflect current changes in cost inputs. The market value of billet and scrap metal inventories was determined using replacement costs.

**Property, Plant and Equipment**

Property, plant and equipment are recorded at cost. Expenditures for routine maintenance and repairs are charged to expense as incurred. Expenditures for equipment renewals and improvements, which extend the useful life of an asset, are capitalized. Certain equipment held under capital lease is classified as property, plant and equipment, and the related obligation is recorded as a liability. Lease amortization is included in depreciation expense.

Depreciation is provided on the straight-line method over the estimated useful lives of the assets, generally 3 to 20 years for machinery and equipment, and 20 to 40 years for buildings and improvements. Equipment under capital lease is amortized using the straight-line method over the primary lease term.

**Revenue Recognition**

The Company recognizes revenue when there is persuasive evidence that an arrangement exists, delivery of the product has occurred and title has passed, the selling price is both fixed and determinable, and collectability is reasonably assured, all of which generally occur either upon shipment of the Company's product or delivery of the product to the destination specified by the customer.

**Stock-Based Compensation**

The Company recognizes compensation expense for its equity awards on a straight-line basis over the requisite service period of the award based on the estimated portion of the award that is expected to vest and applies estimated forfeiture rates based on analyses of historical data, including termination patterns and other factors. The Company uses the quoted closing market price of its common stock on the grant date to measure the fair value of restricted stock awards and the Black-Scholes option pricing model to measure the fair value of stock option awards. The expected volatility is based on historical volatilities of the Company's common stock over the most recent period commensurate with the estimated expected term of the awards. The expected term of an award is equal to the midpoint between the vesting date and the end of the contractual term of the award. The risk-free interest rate is based on the rate on U.S. Treasury securities with maturities consistent with the estimated expected term of the awards. The Company has not paid dividends and does not anticipate paying a cash dividend in the foreseeable future and, accordingly, uses an expected dividend yield of zero.

## Income Taxes

The Company uses the asset and liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax-credit carry-forwards, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amount of assets and liabilities and their tax bases.

The Company's judgments relative to the current provision for income taxes take into account current tax laws, the Company's interpretation of current tax laws and possible outcomes of current and future audits conducted by tax authorities. The Company files income tax returns in the U.S. federal jurisdictions and various state jurisdictions and is subject to U.S. federal tax and state tax examinations for years ranging from 2008 to 2012. The Company's judgments relative to the value of deferred tax assets and liabilities take into account estimates of the amount of future taxable income. Actual operating results and the underlying amount of income in future years could render the Company's current estimates of recoverable net deferred taxes inaccurate. Any of the judgments mentioned above could cause the Company's actual income tax obligations to differ from its estimates, thus materially impacting the Company's financial position and results of operations.

If the Company takes a recognized tax position or has taken a recognized tax position on a tax return that more likely than not would be sustained upon examination by tax authorities, then the Company will recognize the potential asset or liability in the financial statements. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Management believes that the Company has appropriate support for the income tax positions taken and to be taken on its tax returns and that its accrual for tax liabilities are adequate for all open years on assessment of many factors including past experience and interpretation of tax law applied to the facts of each matter.

## Concentrations

The Company maintains its cash balances with a number of financial institutions. The balances are insured by the Federal Deposit Insurance Corporation (FDIC) up to $250,000. At times these balances are in excess of the FDIC insured balances.

For the three month period ending December 31, 2012, the Company had three suppliers that accounted for approximately 57% of raw materials purchases, of which approximately $3.35 million was included in accounts payable at December 31, 2012. For the three month period ending December 31, 2012, the Company had 3 customers that accounted for approximately 20% of net sales, of which approximately $2.58 million was included in accounts receivable at December 31, 2012.

## Earnings Per Share

Basic net income or loss per share is computed by dividing net income or loss by the weighted average number of common shares outstanding for the period. Nonvested shares of restricted stock are not included in the computation of basic net income per share until vested. Diluted net income per share includes the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. Diluted net income per share also includes the dilutive effect of nonvested shares of restricted stock.

The following table summarizes the basic and diluted weighted average shares for the three months ending December 31, 2012 and 2011:

| | Three Months Ended December 31, | |
|---|---|---|
| | **2012** | **2011** |
| Weighted average shares outstanding, basic | 57,346,598 | 56,934,040 |
| Dilutive effect of: | | |
| Options to purchase common stock | 2,200,000 | 1,600,000 |
| Weighted average shares outstanding, diluted | 59,546,598 | 58,534,040 |

## 3. Acquisition of Steel Mini-Mill

In September 2003, ALJ invested $125,000 to acquire a 1.00% membership interest in KES Holdings, LLC, a Delaware limited liability company, which was formed to acquire certain assets of Kentucky Electric Steel, Inc., a Delaware corporation, consisting of the Mill pursuant to Section 363 of the United States Bankruptcy Code through its subsidiary, KES Acquisition Company, LLC, a Delaware limited liability company and predecessor of KES ("KES Acquisition"). The Mill had ceased production on or about December 16, 2002 and its prior owner had filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code on February 5, 2003. The Mill had been in operation for approximately forty years and was refurbished by KES Acquisition subsequent to its acquisition. The refurbished Mill has been generating revenues since late January 2004. ALJ completed its acquisition of the Mill in March 2005.

## 4. Recent Developments

See Notes 15, Tender Offer, and 16, Subsequent Events.

## 5. Related Party Transactions

See Note 16, Subsequent Events.

## 6. Discontinued Operations

As of December 31, 2012 and September 30, 2012, the Company maintained an estimated accrual of liabilities associated with the discontinued operations of $298,000, remaining from its discontinued businesses. The accrued liabilities consist primarily of severance, lease payments, tax payments and other costs related to the operations of the discontinued businesses.

## 7. Accounts Receivable

Accounts Receivable is summarized as follows at December 31, 2012 and September 30, 2012:

| | December 31, 2012 Unaudited | September 30, 2012 |
|---|---|---|
| Accounts Receivable | $ 9,662,583 | $ 12,083,071 |
| Less: Allowance for doubtful accounts | (699,907) | (534,447) |
| Total | $ 8,962,676 | $ 11,548,624 |

## 8. Inventories

Inventories are comprised of the following at December 31, 2012 and September 30, 2012:

| | December 31, 2012 Unaudited | | September 30, 2012 | |
|---|---|---|---|---|
| Raw materials | $ | 1,768,104 | $ | 2,268,113 |
| Semi-finished goods | | 11,246,463 | | 10,986,267 |
| Finished goods | | 13,208,182 | | 10,751,505 |
| Total | $ | 26,222,749 | $ | 24,005,885 |

Inventories are comprised of raw materials, semi-finished goods and finished goods. Inventory costs include material, labor and manufacturing overhead. Inventories are valued at the lower of average cost or market. The average cost of the billets and scrap metal is adjusted periodically to reflect current changes in cost inputs.

## 9. Property, Plant and Equipment

Property, plant and equipment consisted of the following at December 31, 2012 and September 30, 2012:

| | December 31, 2012 Unaudited | | September 30, 2012 | |
|---|---|---|---|---|
| Land | $ | 142,498 | $ | 142,498 |
| Buildings and improvements | | 572,497 | | 572,497 |
| Vehicle | | 6,450 | | 6,450 |
| Machinery and equipment | | 4,456,032 | | 4,456,032 |
| Total | | 5,177,477 | | 5,177,477 |
| Less: Accumulated depreciation and amortization | | (2,997,602) | | (2,934,624) |
| | | 2,179,875 | | 2,242,853 |

Depreciation and amortization expense for the years ended December 31, 2012 and 2011 was $62,978 and $90,167.

## 10. Long-Term Debt

### Secured Credit Line and Restructure of Debt Obligations

On September 30, 2011, KES entered into the Amended and Restated Revolving Credit, Term Loan and Security Agreement (the “Loan Agreement”) with PNC Bank, National Association. The Loan Agreement provides for an asset-based revolving credit line of $30 million (the “Revolver”) and a term loan of $6 million (the “Term Loan,” and together with the Revolver, the “Credit Facility”), which is an increase from KES’ prior credit line of $23 million and term loan of $4 million. The Term Loan and the Revolver bear interest at variable rates based on LIBOR or the base commercial lending rate of PNC as publicly announced from time to time.

As of December 31, 2012, the outstanding balance on the Term Loan was $3.5 million, with an interest rate of 6.00%, and the outstanding balance on the Revolver was $5.7 million, with an interest rate of 8.00%.

As of September 30, 2012, the Revolver had an outstanding balance of $2,667,015, bearing interest at 6.00% and two 30-Day LIBOR loans outstanding with balances of $2,500,000 and $2,000,000, each bearing interest at 4.50%. The Term Loan bears interest at variable rates based on LIBOR or the base commercial lending rate of PNC as publicly announced from time to time. As of September 30, 2012, the outstanding balance on the Term Loan was $4,000,000 and the interest rate was 6.50%.

The Credit Facility is secured by all of the assets of KES and contains customary covenants, including financial covenants requiring KES to maintain certain fixed charge coverage and leverage ratios and has been presented as a non-current liability in the balance sheet. In addition, the Credit Facility contains an event of default if Jess Ravich is no longer on ALJ's Board of Directors. As of December 31, 2012, KES was in compliance with all specified covenants. In the event that KES is not in compliance with any financial covenants, KES intends to seek a waiver of any default from the lender, and if no such waiver is received, the lender would have the right to accelerate the maturity of the Credit Facility at that time. The Term Loan is to be repaid in equal principal payments of $500,000 per quarter over twelve quarters plus certain mandatory prepayments. However, for the year ended September 30, 2012 and interim December 31, 2012, the entire balance of the term loan is classified as a current liability, since the excess cash flow sweep is greater than $2,000,000. The Revolver expires on September 30, 2014.

Mr. Ravich, together with two related trusts, collectively guaranteed the Term Loan. KES agreed to pay a one-time fee of $200,000 to the guarantors. The agreement with the guarantors provides that in the event that Mr. Ravich is no longer a director of ALJ, other than by voluntary resignation, then a guaranty premium fee of $500,000 will be paid to the guarantors. The terms of the guaranty and guaranty fee were approved by the independent members of each of the ALJ and KES Boards of Directors.

**8% Subordinated Loans**

Subordinated loans (the "Subordinated Loans") consist of a series of loans due from KES under the Subordinated Financing Agreement dated July 20, 2009 by and among KES, the lenders party thereto and Ableco, L.L.C. (the "Subordinated Financing Agreement"), which replaced a series of subordinated secured promissory notes dated February 23, 2007, which were originally issued in March 2005 in connection with ALJ's acquisition of KES. The Subordinated Loans are subordinated to the Credit Facility. The Subordinated Loans bear interest at 8% per annum, with interest payable annually. So long as the Credit Facility remains outstanding, the Company may, at its discretion, capitalize unpaid accrued interest into the outstanding Subordinated Loan principal. Principal on the Subordinated Loans is due and payable upon the earlier to occur of (i) an event of default under the Subordinated Financing Agreement, which includes an event of default under the Credit Facility or (ii) February 22, 2017. At December 31, 2012 and September 30, 2012, the principal balance outstanding on the Subordinated Loans was $19 million. Accrued interest on the Subordinated Loans as of December 31, 2012 and September 30, 2012 was $1.9 million and $1.6 million, respectively. The Subordinated Loans are secured by a second priority security interest in all of KES' assets.

The subordinated lenders include affiliates of Ableco, L.L.C., ALJ and three directors who currently serve on ALJ's Board of Directors. These related parties hold Subordinated Loans with an aggregate principal balance of $9.5 million at both September 30, 2012 and December 31, 2012.

**13% Series A Preferred Stock**

In connection with the acquisition of the mill and pursuant to its articles of incorporation, KES issued 25,000 shares of its 13% Series A Preferred Stock with the following rights, preferences and privileges:

a. Dividend Rights. The holders of the 13% Series A Preferred Stock are entitled to receive cumulative dividends in cash at the rate of 13% per year on the face amount of $1,000 per share payable concurrent with the redemption of the 13% Series A Preferred Stock. The dividends are payable, when and as declared by KES' Board of Directors, out of funds legally available for that purpose, upon a liquidation event or upon redemption of the 13% Series A Preferred Stock.

b. Liquidation and Redemption. The 13% Series A Preferred Stock contains a liquidation preference equal to $1,000 per share, plus accrued but unpaid dividends, and is redeemable out of, and to the extent of, legally available funds, at a redemption price equal to the sum of $1,000 and all accrued but unpaid dividends on the first anniversary of KES' full and complete repayment of the Subordinated Loans. As of December 31, 2012, the balance outstanding on the 13% Series A Preferred Stock was $5.9 million, related accrued dividends payable were $6.1 million and $1.9 million of the preferred

stock was held by related parties. As of September 30, 2012, the balance outstanding on the 13% Series A Preferred Stock was $5.9 million, related accrued dividends payable were $5.9 million and $1.9 million of the preferred stock was held by related parties.

c. Convertibility and Voting Rights. The 13% Series A Preferred Stock is not convertible into any other security of the Company, and the holders thereof have no voting rights except with respect to any proposed changes in the preferences and special rights of such stock or except as granted to holders by law.

Pursuant to SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity," because the 13% Series A Preferred Stock provides for mandatory redemption in cash, it is classified as a long-term liability at the redemption value at December 31, 2012 and September 30, 2012 of $12.0 million and $11.8 million, respectively, including cumulative dividends of $6.1 million and $5.9 million, respectively.

## 11. Commitments and Contingencies

### Operating Commitments

The Mill has been operating under a Management Agreement with Pinnacle Steel, LLC ("Pinnacle") effective through September 30, 2015 (the "Management Agreement") pursuant to which Pinnacle provides, at its expense, employees to serve as the general manager of the Mill and provide oversight and general management of the operations of the Mill. Pursuant to the Management Agreement, Pinnacle receives an annual fee of $700,000, payable monthly, and bonus payments based on 16.6% of defined earnings before interest, taxes, depreciation and amortization ("EBITDA") in excess of $6,000,000 for the fiscal years ending September 30, 2005 and thereafter. In addition, in the event the Management Agreement is terminated following a change of control of KES, an amount equal to two times the prior annual management fee and bonuses payable would be payable to Pinnacle. Total management fee expense was $175,000 and $575,491 for the three months ended December 31, 2012 and 2011, respectively. As of December 31, 2012 and September 30, 2012, the balance of accrued management fee was $1.7 million and $0, respectively.

The Company has various short-term commitments for the purchase of materials, supplies and energy arising in the ordinary course of business which aggregated approximately $2.0 million and $2.8 million at December 31, 2012 and September 30, 2012, respectively.

The Company has a defined contribution pension plan for eligible employees who have completed one month of service and have attained the age of twenty-one. The Company's matching contribution equals 100% of each participant's elective deferral, not to exceed 6% of their eligible compensation. Participants are immediately vested in their deferred compensation and earnings thereon. The participant becomes 100% vested in the Company's matching contributions after one year of credited service. The Company may make other discretionary contributions to be determined on an annual basis. The Company's contributions charged to operations during the quarters ended December 31, 2012 and December 31, 2011 were approximately $133,000 and $110,000, respectively.

## 12. Income Taxes

The Company incurs income tax expense due to taxable income from operations. There were no income tax expenses incurred for the three months ended December 31, 2012, as the company registered a net loss of $1.5 million. The Company recognized federal and state income tax expense related to continuing operations for the three months ended December 31, 2011 of $285,953.

Deferred tax assets and liabilities are included in the financial statements at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

The Company files income tax returns in the U.S. federal jurisdiction and various states. The Company is subject to tax examinations for periods post 2008 by federal, state and local tax authorities for various tax liabilities incurred by the parent entity and its subsidiaries, including any discontinued businesses. The amount of any tax assessments and penalties may be material and may negatively impact the Company's operations. Given the uncertainty in the amount and the difficulty in estimating the probability of the assessments arising from future tax examinations, the Company has not made any accruals for such tax contingencies.

In assessing the realization of deferred tax assets, the Company performed an analysis of the available evidence to determine whether it is more likely than not that some portion or all of the deferred tax assets can be realized. One factor considered is the ability of the Company to generate consistent future taxable income in the periods in which the temporary differences become deductible. The main component of the deferred tax assets is the net operating loss carry-forward. There has been significant positive evidence established by the Company to justify that only a partial valuation allowance is necessary. The Company has shown consistent profitability over the past three years. A valuation allowance of $85.3 million has been established against the net deferred tax asset of $91.2 million as of December 31, 2012 and September 30, 2012.

Effective October 1, 2007, the Company adopted Financial Accounting Standards Board ("FASB") Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN48"). FIN48 requires that a position taken or expected to be taken in a tax return be recognized in the financial statements when it is more likely than not that the position would be sustained upon examination by tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Management believes that the Company has appropriate support for the income tax positions taken and to be taken on its tax returns and that its accrual for tax liabilities are adequate for all open years on assessment of many factors including past experience and interpretation of tax law applied to the facts of each matter.

At December 31, 2012, the Company had a net operating loss carry-forward for federal income tax purposes of approximately $258 million that expires from 2020 through 2028. The use of approximately $36 million of this net operating loss in future years may be restricted under Section 382 of the Internal Revenue Code. The realization of the benefits of the net operating losses is dependent upon sufficient taxable income in future years. Lack of consistent future earnings, a change in ownership of the Company, or the application of the alternative minimum tax rules could adversely affect the Company's ability to utilize these net operating losses.

For taxable periods beginning after February 28, 2005, KES is included in the consolidated federal income tax return filed by ALJ as common parent. KES has entered into a Tax Sharing Agreement with ALJ, pursuant to which it has agreed to pay ALJ an amount equal to 50% of its "separate company tax liability," subject to compliance with the Credit Facility and Subordinated Financing Agreement. The term "separate company tax liability" is defined as the amount, if any, of the federal income tax liability (including, without limitation, liability for any penalty, fine, additions to tax, interest, minimum tax and other items applicable to such subsidiary in connection with the determination of the subsidiary's tax liability), which such subsidiary would have incurred if its federal income tax liability for the periods during which it is includible in a consolidated federal income tax return with ALJ were determined generally in the same manner in which its separate return liability would have been calculated under Section 1552(a)(2) of the Code.

### 13. Share-based Compensation and Stock Options

The Company determines the fair value of all stock-based compensation, including stock options and warrants by using the Black-Scholes option-pricing model. Included in the selling, general and administrative expenses for the three months ended December 31, 2012 and 2011, the Company recognized share-based share compensation expense of $0 and $6,090, respectively.

All share-based payments to employees are recognized in the financial statements as compensation expense based on the fair value on the date of grant. The Black-Scholes model requires input of certain assumptions, including volatility, expected term, risk-free interest rates, and dividend yield. The Company did not issue restricted stock grants or stock options for the twelve months ended September 30, 2012 or the three months ended December 31, 2012. For restricted stock grants issued during the twelve months ended September 30, 2011, the Company computed volatility of 106% and a risk-free interest rate of 0.15%. Volatility was computed over the most recent period commensurate with the expected term of the options and restricted stock. The risk-free interest rate was based on the rate of U.S. Treasury securities with maturities consistent with the expected term of the options and restricted stock. The Company has not paid dividends on its common stock and does not anticipate paying a cash dividend in the foreseeable future and accordingly, uses an expected dividend yield of zero.

The summary of stock option activity for the three months ending December 31, 2012 is as follows:

| | Number of Options | Weighted Average Exercise Price per Share | Weighted Average Contractual Term |
|---|---|---|---|
| Balance outstanding as of September 30, 2012 | 2,400,000 | $0.40 | 5.0 years |
| Exercised | 200,000 | $0.23 | 5.0 years |
| Balance outstanding as of December 31, 2012 | 2,200,000 | $0.38 | 5.0 years |
| Options vested as of December 31, 2011 | 2,200,000 | $0.38 | 5.0 years |

## 14. Sale of KES

On November 18, 2012, ALJ and KES entered into a definitive merger agreement (the "Merger Agreement") for the sale of KES to Optima for $112.5 million in cash (the "Merger"). The Merger was effected as a merger of Optima's wholly owned subsidiary KES Optima Acquisition Inc. with and into KES with KES surviving as a wholly owned subsidiary of Optima. The Merger was unanimously approved by the ALJ Board and was approved by the stockholders of ALJ at the special stockholders meeting held on December 21, 2012. The Merger was conditioned upon, among other customary closing conditions, Optima arranging and closing, no later than February 28, 2013, sufficient financing.

## 15. Tender Offer

On November 19, 2012, ALJ launched a self-tender offer (the "Tender Offer") to use approximately 50% of its expected cash immediately following closing of the Merger to acquire up to approximately 50% of its outstanding common stock. The Tender Offer was structured as a modified "Dutch auction" tender offer for up to 30,000,000 shares of ALJ's common stock at a price per share not greater than $0.86 and not less than $0.84. The Tender Offer was conditioned upon the closing of the Merger.

## 16. Subsequent Events

On February 5, 2013, ALJ completed the sale of KES to Optima for $112.5 million in cash. The carrying amounts of the assets and liabilities of KES as of December 31, 2012 are as follows:

ASSETS

| | |
|---|---|
| Current Assets: | |
| Accounts receivable, net of allowances | $ 8,962,676 |
| Inventory | 26,222,749 |
| Prepaid expenses and other current assets | 876,086 |
| Deferred Tax Asset | 606,444 |
| Total Current Assets | 36,667,955 |

| | | |
|---|---|---|
| Property, Plant and Equipment, net of accumulated depreciation | | 2,179,875 |
| | | |
| Other Assets: | | |
| Deferred loan costs, net of amortization | | 239,899 |
| Deposits | | 224,460 |
| Total other assets | | 464,359 |
| | | |
| Total Assets | | 39,312,189 |
| | | |
| Current Liabilities | | |
| Accounts Payable | | 8,947,011 |
| Accrued Expenses | | 3,112,592 |
| Term notes Payable | | 3,500,000 |
| Total current liabilities | | 15,559,603 |
| | | |
| Line of Credit | | 7,037,725 |
| 8% Subordinated Loans Payable | | 19,242,105 |
| Deferred Tax Liability | | 310,626 |
| Preferred stock, including accrued dividends | | 11,998,305 |
| Total Liabilities | | 54,148,364 |
| | | |
| Common Stock | | 8 |
| Additional Paid in Capital | | (51,383,780) |
| Accumulated Deficit | | 36,547,597 |
| Total Stockholders Deficiency | | (14,836,175) |
| | | |
| Total Liabilities and Stockholders Equity | $ | 39,312,189 |

Revenues from KES for the quarter ended December 31, 2012 and 2011 were $30.6 million and $38.9 million, respectively. Net (loss)/income from KES for the quarter ended December 31, 2012 and 2011 were $(1.3) million and $1.7 million, respectively.

As a result of the sale of KES, ALJ's cash position increased to approximately $52 million. ALJ will also recognize a gain of approximately $52 million, which will be offset by a reduction of $7.3 million in Minority Interest and $5.7 million in the reduction of deferred tax assets.

As a result of the sale of KES, ALJ retired all outstanding loans at KES and sold 100% of the stock in KES. This included $10.9 million related to the Term Loan and Revolver and related accrued interest, $20.8 million related to the 8% Subordinated Loans and related accrued interest (not including proceeds paid to ALJ as a holder of 8% Subordinated Loans), $11.9 million related to the 13% KES Preferred Stock and accrued dividends, and $10.2 million related to the Series B Common Stock of KES (not including proceeds paid to ALJ as a holder of KES Series B Common Stock).

Jess Ravich, who is the Chairman of the Board of the Company and was a director of KES, received as a result of the sale, (i) $3.3 million as payment of principal and accrued interest on the 8% Subordinated Loans, (ii) $1.3 million related to the sale of 1,618 shares of Series B Common Stock of KES, and (iii) $2.4 million related to the retirement of the 13% Preferred Stock of KES, including accrued dividends. Additionally, Libra Securities Holdings, LLC, an affiliate of Mr. Ravich, received as a result of the sale, (i) $3.9 million as payment of principal and accrued interest on the 8% Subordinated Loans, (ii) $2.9 million related to the sale of 3,657 shares of Series B Common Stock of KES, and (iii) $1.4 million related to the retirement of the 13% Preferred Stock of KES, including accrued dividends.

Robert Scott Fritz, a director of the Company, received as a result of the sale, (i) $186,544 as payment of principal and accrued interest on the 8% Subordinated Loans, and (ii) $114,185 related to the sale of 144 shares of Series B Common Stock of KES.

Hal G. Byer, a director of the Company, received as a result of the sale, (i) $166,437 as payment of principal and accrued interest on the 8% Subordinated Loans, and (ii) $62,643 related to the sale of 79 shares of Series B Common Stock of KES.

As a result of the sale of KES, Pinnacle, a company affiliated with John Scheel, ALJ's director, President and CEO, and KES's director, President and CEO, received a termination fee equal to two (2) times the Management Fee and Management Incentive Fee payable for the twelve months immediately preceding the close of the sale, which was computed to be $5.1 million.

Effective as of February 5, 2013, the following agreements between KES, on the one hand, and ALJ, certain officers or directors of ALJ or their affiliates, on the other hand, were terminated: (i) the Management Agreement, (ii) the Amended and Restated Tax Sharing Agreement (the "Tax Sharing Agreement"), dated as of February 23, 2007, by and between KES and ALJ, and (iii) the Fee and Reimbursement Agreement (the "Fee and Reimbursement Agreement"), dated as of September 30, 2011, by and between KES and certain guarantors related to Mr. Ravich.

In connection with the Merger and Tender Offer, ALJ decided to postpone any relisting of its stock on a national exchange until such time when it has substantial operations and the Board determines that the cost of such listing is warranted and beneficial to ALJ stockholders.

The Company used approximately $25.2 million of the unrestricted cash at ALJ following the Merger to purchase 30,000,000 shares of its common stock from its stockholders at $0.84 per share in the Tender Offer. The Tender Offer expired on February 8, 2013 and the Company expects to close the Tender Offer by February 19, 2013. The Company anticipates that its cash position will be reduced by $25.2 million following completion of the Tender Offer. The Company plans to use the remainder of the cash at ALJ following the Merger and Tender Offer for future acquisitions or investments in other companies and businesses or for other strategic options. However, the Company is not required to make any such acquisitions, and at this time no specific acquisition targets have been determined.

## ITEM 4. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

### General Overview

Commencing March 1, 2005, the Company has included the operations of the Mill, which represented the only business segment in which the Company operated, in its consolidated financial statements. The Company completed the acquisition of the Mill on March 9, 2005 (see Note 3 to Consolidated Financial Statements). As discussed in further detail below, on February 5, 2013, the Company completed the disposition of KES (including the Mill).

### Critical Accounting Policies and Estimates

The Company prepared its financial statements in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Management periodically evaluates the estimates and judgments made. Management bases its estimates and judgments on historical experience and on various factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates as a result of different assumptions or conditions.

The Company believes that of its significant accounting policies, which are described in Note 2 to the accompanying consolidated financial statements and in the Company's annual report for the year ended September 30, 2012, the following accounting policies involve a greater degree of judgment and complexity. Accordingly, these are the policies the Company believes are the most critical to aid in fully understanding and evaluating its consolidated financial condition and results of operations.

**Revenue Recognition**

The Company recognizes revenue when there is persuasive evidence that an arrangement exists, delivery of the product has occurred and title has passed, the selling price is both fixed and determinable, and collectability is reasonably assured, all of which generally occur either upon shipment of the Company's product or delivery of the product to the destination specified by the customer.

**Accounts Receivable**

The Company grants credit to its customers generally in the form of short-term trade accounts receivable. Management evaluates the credit risk of its customers utilizing historical data and estimates of future performance. Accounts receivable are stated at the amount management expects to collect from outstanding balances. When appropriate, management provides for probable uncollectible amounts through a provision for doubtful accounts and an adjustment to a valuation allowance. Management reviews and adjusts this allowance periodically based on the aging of accounts receivable balances, historical write-off experience, customer concentrations, customer creditworthiness, and current industry and economic trends. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

**Inventories**

Inventories are comprised of raw materials, semi-finished goods and finished goods. Inventory costs include material, labor and manufacturing overhead. Inventories are valued at the lower of average cost or market. The average cost of the billets, scrap metal, and finished goods is adjusted monthly.

**Income Taxes**

The Company uses the asset and liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax-credit carry-forwards, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amount of assets and liabilities and their tax bases.

The Company's judgments relative to the current provision for income taxes take into account current tax laws, the Company's interpretation of current tax laws and possible outcomes of current and future audits conducted by tax authorities. The Company files income tax returns in the U.S. federal jurisdictions and various state jurisdictions and is subject to U.S. federal tax and state tax examinations for years ranging from 2008 to 2012. The Company's judgments relative to the value of deferred tax assets and liabilities take into account estimates of the amount of future taxable income. Actual operating results and the underlying amount of income in future years could render the Company's current estimates of recoverable net deferred taxes inaccurate. Any of the judgments mentioned above could cause the Company's actual income tax obligations to differ from its estimates, thus materially impacting the Company's financial position and results of operations.

If the Company takes a recognized tax position or has taken a recognized tax position on a tax return that more likely than not would be sustained upon examination by tax authorities, then the Company will recognize the potential asset or liability in the financial statements. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Management believes that the Company has appropriate support for the income tax positions taken and to be taken on its tax returns and that its accrual for tax liabilities are adequate for all

open years based on assessment of many factors, including past experience and interpretation of tax law applied to the facts of each matter.

**Recent Events**

On November 18, 2012, ALJ and KES entered into the Merger Agreement for the sale of KES to Optima for $112.5 million in cash. The transaction was effected as a merger of Optima's wholly owned subsidiary KES Optima Acquisition Inc. with and into KES with KES surviving as a wholly owned subsidiary of Optima. The Merger was unanimously approved by the ALJ Board. The Merger was approved by the stockholders of ALJ at the special stockholders meeting held on December 21, 2012. ALJ's stockholders approved the Merger by a vote of 35,604,591 shares in favor (representing 61.98% of the total outstanding shares), 310 shares abstaining and 73,145 broker non-votes. On February 5, 2013, ALJ completed the sale of KES to Optima for $112.5 million in cash.

As a result of the sale of KES, ALJ's cash position increased to approximately $52 million. ALJ will also recognize a gain of approximately $52 million, which will be offset by a reduction of $7.3 million in Minority Interest and $5.7 million in the reduction of deferred tax assets.

As a result of the sale of KES, ALJ retired all outstanding loans at KES and sold 100% of the stock in KES. This included $20.8 million related to the 8% Subordinated Loans (not including proceeds paid to ALJ as a holder of 8% Subordinated Loans) and related accrued interest, $11.9 million related to the 13% KES Preferred Stock and accrued dividends, and $10.2 million related to the Series B Common Stock of KES (not including proceeds paid to ALJ as a holder of KES Series B Common Stock).

Also as a result of the sale of KES, the following agreements between KES, on the one hand, and ALJ, certain officers or directors of ALJ or their affiliates, on the other hand, were terminated: (i) the Tax Sharing Agreement, (ii) the Management Agreement and (iii) the Fee and Reimbursement Agreement.

The Company used approximately $25.2 million of the unrestricted cash at ALJ following the Merger to purchase 30,000,000 shares of its common stock from its stockholders at $0.84 per share in the Tender Offer. The Tender Offer expired on February 8, 2013 and the Company expects the Tender Offer to close by February 19, 2013. The Company anticipates that its cash position will be reduced by $25.2 million following completion of the Tender Offer. The Company plans to use the remainder of the cash at ALJ following the Merger and Tender Offer for future acquisitions or investments in other companies and businesses or for other strategic options. However, the Company is not required to make any such acquisitions, and at this time no specific acquisition targets have been determined.

Certain of ALJ's directors tendered shares of ALJ Common Stock in the Tender Offer. The table below sets forth beneficial ownership of ALJ's directors and officers immediately prior to, and immediately following, the Tender Offer.

| Name of Director or Officer | Amount and Nature of Beneficial Ownership Immediately Preceding Tender Offer (1) | Percent of Class Immediately Preceding Tender Offer (1) | Amount and Nature of Beneficial Ownership Immediately Following Tender Offer (1) | Percent of Class Immediately Following Tender Offer (1) |
|---|---|---|---|---|
| Robert Scott Fritz, Director | 1,185,099 (2) | 2.06% | 613,040 (2) | 2.23% |
| Hal G. Byer, Director | 516,028 | *% | 115,741 | *% |
| Jess M. Ravich, Chairman of the Board | 13,154,569 (3) | 22.13% | 13,154,569 (3) | 44.67% |
| John Scheel, Chief Executive Officer, President and Director | 738,460 | 1.29% | 738,460 | 2.69% |
| Olimpio Lee Squitieri, Director | 1,275,510 (4) | 2.22% | 1,067,928 (4) | 3.89% |
| T. Robert Christ, Chief Financial Officer | 200,000 (5) | *% | 200,000 (5) | *% |
| All current directors and officers as a group | 17,069,666 (6) | 28.62% | 15,889,738 (6) | 53.60% |

* Less than 1%

(1) Consistent with the regulations of the U.S. Securities and Exchange Commission, shares of ALJ Common Stock issuable upon exercise of derivative securities by their terms exercisable within 60 days are deemed outstanding for the purpose of computing the percentage ownership of the person holding such derivative securities but are not deemed outstanding for computing the percentage ownership of any other person. Unless otherwise indicated below, to the knowledge of the Company, the persons and entities named in this table have sole voting and sole investment power with respect to all shares beneficially owned, subject to community property laws where applicable. Percent of class immediately preceding Tender Offer is based on 57,446,598 shares issued and outstanding as of the expiration of the Tender Offer on February 8, 2013. Percent of class immediately following Tender Offer is based on the Company's expectation that there will be 27,446,598 shares issued and outstanding as of the completion of the Tender Offer on February 19, 2013.

(2) Includes 431,088 shares held by The Ravich Children Permanent Trust, for which Mr. Fritz is the sole trustee.

(3) Includes 5,288,751 shares held by the Exemption Trust under the Ravich Revocable Trust of 1989 and 5,844,632 shares held by Ravich Revocable Trust of 1989, as well as 2,000,000 shares issuable upon exercise of currently vested options.

(4) Includes 202,000 shares held in a custodial account for the benefit of Mr. Squitieri's daughter over which he has dispositive power. Mr. Squitieri disclaims beneficial ownership for these shares.

(5) Includes 200,000 shares issuable upon exercise of currently vested options.

(6) Includes 2,200,000 shares issuable upon exercise of currently vested options.

**Results of Operations for the Three Months Ending December 31, 2012 and 2011**

The following table sets forth selected unaudited consolidated statements of operations data for each of the periods indicated on an actual basis and as a percentage of total revenues for the respective periods.

| | Three Months Ended December 31, | | | |
|---|---|---|---|---|
| | 2012 | | 2011 | |
| Net Sales | $30,620,403 | 100.0% | $38,894,890 | 100.0% |
| Cost of sales | 28,553,295 | 93.2% | 33,403,449 | 85.9% |
| Gross Profit | 2,067,108 | 6.8% | 5,491,441 | 14.1% |
| Selling | 517,753 | 1.7% | 537,459 | 1.4% |
| General and administrative | 2,491,568 | 8.1% | 1,612,836 | 4.1% |
| Income from operations | (942,213) | -3.1% | 3,341,146 | 8.6% |

## For the three months ended December 31, 2012 and 2011

### Net Sales

Net sales for the three months ended December 31, 2012 were $30.6 million, a decrease of $8.3 million, or 21%, over net sales of $38.9 million for the three months ended December 31, 2011. The decrease in net sales was primarily attributable to a decrease in tons invoiced of 4,088 tons, or 11.4%, and a decrease of $121 in the average selling price per ton.

### Cost of Sales

Cost of sales for the three months ended December 31, 2012 were $28.6 million, a decrease of $4.9 million, or 15%, over cost of sales of $33.4 million for the three months ended December 31, 2011. Cost of sales as a percentage of sales for the three months ended December 31, 2012 was 93.2% as compared to cost of sales as a percentage of sales for the three months ended December 31, 2011 of 85.9%. The decrease in cost of sales was primarily due to a decrease of tons shipped.

### Gross Profit

Gross profit for the three months ended December 31, 2012 was $2.1 million, a decrease of $3.4 million, or 62%, over gross profit of $5.5 million for the three months ended December 31, 2011. Gross profit as percentage of sales decreased for the three months ended December 31, 2012 to 6.8% as compared to the gross profit as a percentage of sales of 14.1% for the three months ended December 31, 2011.

### Selling Expenses

Selling expenses for the three months ended December 31, 2012 were $517,753, a decrease of $19,706, or 4% over selling expenses for the three months ended December 31, 2011 of $537,459. Selling expenses as a percentage of sales was relatively comparable for the three months ended December 31, 2012 and December 31, 2011 at 1.7% and 1.4%, respectively. Selling expenses primarily decreased as a result of lower commissions related to lower sales revenue.

### General and Administrative Expenses

General and administrative expenses for the three months ended December 31, 2012 were $2.5 million, an increase of $878,732, or 54% over general and administrative expenses of $1.6 million for the three months ended December 31, 2011. General and administrative expenses as a percentage of sales for the three months ended December 31, 2012 were 8.1% as compared to general and administrative expenses as a

percentage of sales for the three months ended December 31, 2011 of 4.1%. The increase was primarily attributable to an increase in expenses related to the sale of KES.

**Liquidity and Capital Resources – December 31, 2012**

The Company recognized net loss of $1.5 million for the three month period ended December 31, 2012 and generated a negative cash flow from operating activities of $361,366 for the three months then ended. The Company used $1.9 million in financing activities and had an accumulated deficit of $303.0 million and a stockholders' deficiency of $14.8 million at December 31, 2012.

The Company recognized net income of $13.3 million for the year ended September 30, 2012 and generated a positive cash flow from operating activities of $14.7 million for the year ended September 30, 2012. The Company used $13.1 million in financing activities, $70,274 in investing activities and had a stockholder's deficit of $13.3 million, which was primarily comprised of an accumulated deficit of $301.4 million, partially offset by an increase in additional paid-in-capital to $288.4 million at September 30, 2012.

As of December 31, 2012, the balance outstanding on the Credit Facility was $9.2 million ($5.7 million under the Revolver and an aggregate of $3.5 million under the Term Loan).

At December 31, 2012, KES was in compliance with all financial covenants under the Credit Facility based on its financial statements.

The Credit Facility was repaid in full effective February 5, 2013 in connection with the completion of the sale of KES.

Following the disposition of KES, ALJ believes that its cash resources will be adequate to fund its operations through December 31, 2013. However, to the extent that the Company's estimates are inaccurate or its assumptions are incorrect, the Company may not have sufficient cash resources to fund its operations. In such event, the Company may have to seek additional financing for the business.

The Company plans to use its cash resources for future acquisitions or investments in other companies and businesses or for other strategic options. However, the Company is not required to make any such acquisitions, and at this time no specific acquisition targets have been determined. Further, there can be no assurances that such efforts will ultimately be successful. The Company may finance any acquisitions through a combination of debt and/or the issuance of equity securities.

**Operating Activities**

During the three months ended December 31, 2012, the Company used $361,366 from operating activities, primarily attributable to a net loss $1.5 million, an increase in inventory of $2.2 million and accrued expenses of $1.2 million, partially offset by a decrease in accounts receivable of $2.8 million and an increase in accounts payable of $1.2 million.

**Financing Activities**

For the three months ended December 31, 2012, the Company used $1.9 million in financing activities primarily attributable to the partial repayment of $1.4 million against the line of credit and partial repayment of $500,000 against the Term Loan.

### Principal Commitments

At December 31, 2012, the Company's principal commitments consisted of the following obligations:

| | Payments Due by 12 Month Periods Ending December 31, (in thousands) | | | | | |
|---|---|---|---|---|---|---|
| **Contractual cash obligations** | **Total** | **2013** | **2014** | **2015** | **2016** | **Thereafter** |
| 8% Subordinated loans | 18,998 | --- | --- | --- | --- | 18,998 |
| Term loan – PNC | 3,500 | 3,500 | --- | --- | --- | --- |
| Revolver – PNC | 5,727 | --- | 5,727 | --- | --- | --- |
| Operating leases | 1,247 | 680 | 397 | 57 | 57 | 57 |
| Management services agreement | 1,925 | 700 | 700 | 525 | --- | --- |
| 13% Series A Preferred Stock of subsidiary subject to mandatory redemption, including accrued dividends | 11,998 | --- | --- | --- | --- | 11,998 |
| Total contractual cash obligations | $ 43,395 | $ 4,880 | $ 6,824 | $ 582 | $ 57 | $ 31,053 |

At December 31, 2012, the Company did not have any material commitments for capital expenditures.

At December 31, 2012, the Company had various short-term commitments for the purchase of materials, supplies and energy arising in the ordinary course of business which aggregated approximately $2.0 million.

All of the principal commitments set forth in the table above were satisfied and discharged in full effective February 5, 2013 in connection with the completion of the sale of KES.

### Off-Balance Sheet Arrangements

The Company did not have any transactions, obligations or relationships that could be considered off-balance sheet arrangements at December 31, 2012.

## ITEM 5. LEGAL PROCEEDINGS

Historically, the Company has been subject to various lawsuits, claims and other legal actions arising in the ordinary course of business. On December 5, 2012, SWVA, Inc. ("SWVA"), the lessor of KES's ladle metallurgy furnace, filed a civil lawsuit against KES in the Cabell County Circuit Court of West Virginia. The action arises from an alleged breach of the ladle metallurgy furnace lease, as a result of the Merger. Specifically, SWVA alleges that its consent is required to effect the Merger. The complaint seeks, among other remedies, injunctive relief to enjoin the Merger and further use of the ladle metallurgy furnace, and immediate payment of all sums due under the ladle metallurgy furnace lease. On December 13, 2012, SWVA filed a motion for injunctive relief seeking, among other remedies, a preliminary injunction to enjoin the Merger and further use of the ladle metallurgy furnace. On December 20, 2012, the court held a hearing and denied SWVA's motion for injunctive relief. The Company believes it has meritorious defenses to SWVA's allegations and will vigorously defend itself against this lawsuit, however, should SWVA prevail in the litigation, it could result in a loss of use of the ladle metallurgy furnace, as well as the monetary damages. While the Company believes that the ultimate outcome of this matter will not have a material adverse effect on the Company, its outcome is not determinable and a negative outcome may adversely affect the Company's financial position, liquidity, or results of operations.

The Company cannot predict the impact (if any) that the matter described above may have on its business, results of operations, financial position or cash flows. Because of the inherent uncertainty of such matter, including the early stage and lack of specific damage claims, the Company cannot estimate the possible loss from such matter.

As of December 31, 2012, management was not aware of any legal contingencies involving the Company, other than the matter described above. In the opinion of management, any potential matters other than the matter described above, involve such amounts that unfavorable disposition would not have a material adverse effect on the financial position or results of operations of the Company.

Following ALJ's disposition of KES effective as of February 5, 2013, KES is no longer a subsidiary of ALJ and ALJ is no longer subject to any risk in connection with the matter described above.

## ITEM 6. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 7. OTHER INFORMATION

None.

## RISK FACTORS

The following risk factors and other information included in this Report should be carefully considered. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial also may impair our business operations. If any of the following risks actually occur, our business, financial condition and operating results could be significantly harmed.

### Risks Related to Our Existing Business

**We are a company with minimal to no operations and a relatively large cash balance.**

We have approximately $25.8 million of cash on hand following the disposition of KES and the completion of the Tender Offer. We will continue to incur ongoing expenses for employee salaries and certain other expenses while we look to find another business to acquire but will have no operations to produce cash. We cannot assure you how much of our current cash balance, if any, will ultimately be available for future acquisitions.

**Our limited cash resources could materially adversely affect our ability to execute our business strategy.**

We have approximately $25.8 million of cash on hand following the disposition of KES and the completion of the Tender Offer, and we currently have no operations with which to generate additional cash. Demands on our limited cash resources could have a material effect on our ability to execute our business strategy. Specifically, our ability to make acquisitions may be limited because competing bidders for target entities may have greater financial resources at their disposal, and we may be unable to make more than one acquisition given our limited cash resources.

**Our net operating loss carry-forwards could be substantially limited if we experience an "ownership change" as defined in Section 382 of the Internal Revenue Code or do not timely acquire another business that generates taxable income.**

Our ability to utilize NOLs and tax credit carry-forwards to offset our future taxable income and/or to recover previously paid taxes would be limited if we were to undergo an "ownership change" within the meaning of Section 382 of the Code.

Section 382 of the Code contains rules that limit the ability of a company that undergoes an "ownership change," which is generally any change in ownership of more than 50% of its stock over a three-year period, to utilize its NOLs and certain built-in losses recognized in years after the ownership change. These rules generally operate by focusing on ownership changes among stockholders owning directly or indirectly 5% or more of the stock of a company and any change in ownership arising from a new issuance of stock by the company.

If we undergo an ownership change for purposes of Section 382 as a result of future transactions involving our common stock, including purchases or sales of stock between 5% shareholders or equity financings or other equity issuances in connection with future acquisitions, our ability to use our NOLs and to recognize certain built-in losses would be subject to the limitations of Section 382. Depending on the resulting limitation, a significant portion of our NOLs could expire before we would be able to use them. We had approximately $258 million of (pre-tax) NOLs as of December 31, 2012. The NOLs do not begin to expire until 2020 and are available to be used at some level through 2025. Our inability to utilize our NOLs could have a negative impact on our financial position and results of operations.

We do not believe we have experienced an "ownership change" as defined by Section 382 in the last three years. However, whether a change in ownership occurs in the future is largely outside of our control, and there can be no assurance that such a change will not occur.

In May 2009, we announced that our Board adopted a shareholder rights plan designed to preserve stockholder value and the value of certain tax assets primarily associated with NOLs and built in losses under Section 382 of the Code.

We also amended our certificate of incorporation to add certain restrictions on transfers of our stock that may result in an ownership change under Section 382.

Additionally, our ability to utilize our NOLs to offset future tax liabilities may be limited if we do not timely acquire another business which generates taxable income. For example, if it takes us substantially more than one year to acquire another business, we may be treated as having liquidated for U.S. federal income tax purposes, which could prevent us from being able to use our NOLs to offset future income of the new business.

**Our internal controls and procedures may be deficient.**

Our internal controls and procedures may be subject to deficiencies or weaknesses. Any failure of our internal controls or procedures could harm our operating results or cause us to fail to meet our obligation to maintain adequate public information.

**We may have unknown liabilities stemming from YouthStream Media Networks, Inc.'s historical operations.**

There may have been liabilities that stem from YouthStream Media Networks, Inc.'s historical operations of which we are not aware. In the event any such liability becomes known, it may lead to claims against us, including, but not limited to, lawsuits, administrative proceedings, and other claims. Any such liabilities may subject us to increased expenses for attorneys' fees, fines and litigation and expenses associated with any subsequent settlements or judgments. There can be no assurance that such unknown liabilities do not exist. To the extent that such liabilities become known, any such liability-related expenses may materially and adversely affect our profitability, operating results and financial condition.

**We may encounter difficulties in acquiring other companies.**

We currently plan to use our cash for future acquisitions or investments in other companies and businesses or for other strategic options. However, even if we identify suitable candidates, we may not be able to make investments or acquisitions on commercially acceptable terms. Acquisitions may require substantial time and resources and make it difficult to maintain our standards, controls and procedures. We may not be able to retain key employees of the acquired companies or maintain good relations with their clients or suppliers. We may be required to incur debt and to issue equity securities to effect and/or fund acquisitions, which may be dilutive to existing stockholders or impair our ability to utilize our NOLs.

**We cannot assure you that any business acquisitions we make will be successful.**

We cannot assure you that any completed acquisition will be successful and that our investments will yield a favorable return. Our management may not have experience in the industry in which we decide to invest. Until we select a particular industry or business in which to complete an acquisition, there is no current basis for you to ascertain the merits or risks of the industry or business in which we may ultimately operate. Although we will evaluate the risks inherent in a particular target business, we cannot assure you that all of the significant risks present in that target business will be properly assessed. Even if we properly assess those risks, some of them may be outside of our control. Further, we anticipate that acquisitions would be made largely or completely with cash, meaning a substantial portion of our available cash could be used to consummate the acquisitions or we could incur or assume significant amounts of indebtedness. We also may experience significant financial, managerial and operational challenges in the integration of acquired businesses. Also, we are required to account for acquisitions under the purchase method, which would likely result in our recording significant amounts of goodwill or other tangible and intangible assets. The inability of a subsidiary to sustain profitability may result in an impairment loss in the value of long-lived assets, principally goodwill and other tangible and intangible assets, which would adversely affect our financial statements.

**We are dependent upon our officers and directors and their loss could adversely affect our ability to operate.**

Our operations are dependent upon a relatively small group of individuals and, in particular, our officers and directors. We believe that our success depends on the continued service of our officers and directors, at least until we have consummated an acquisition. In addition, our officers and directors are not required to commit any specified amount of time to our affairs and, accordingly, will have conflicts of interest in allocating management time among various business activities, including identifying potential acquisition opportunities and monitoring the related due diligence. The unexpected loss of the services of one or more of our directors or officers could have a detrimental effect on us.

**We cannot assure you that our common stock will become listed on any securities exchange.**

In connection with the Merger and Tender Offer, we have decided to postpone any relisting of our stock on a national exchange until such time when we have substantial operations and we determine that the cost of a listing is warranted and beneficial to our stockholders. Even if we were to determine to pursue a listing, we cannot assure you that we would be able to meet the initial listing standards, including the minimum per share price and minimum capitalization requirements, or that we would be able to maintain a listing of our common stock on either of those or any other trading venue. Until such time as we determine to list and qualify for listing on NASDAQ, the American Stock Exchange or another trading venue, our common stock will continue to be quoted on the Pink Sheets, which may make it more difficult for an investor to dispose of shares or obtain accurate quotations as to the market value of our common stock.

**We may not be able to identify suitable acquisition targets at prices we consider appropriate.**

We intend to invest in or acquire control of one or more operating businesses through merger, capital stock exchange, stock purchase, asset acquisition or other similar investment. However, we are not obligated to do so, and no specific acquisition targets have been designated at this time. There can be no assurances that we will be able to identify suitable acquisition targets. If we do identify an appropriate acquisition target, we may not be able to successfully and satisfactorily negotiate the terms of the acquisition, including a price that we consider acceptable.

**Because of our structure, other companies may have a competitive advantage and we may not be able to consummate an attractive acquisition.**

In pursuing our acquisition strategy, we expect to encounter competition from entities having a business objective similar to ours, including venture capital funds, leveraged buyout funds and operating businesses. Many of these entities are well established and have extensive experience in identifying and effecting acquisitions directly or through affiliates. Many of these competitors possess greater technical, human and other resources than we do and our financial resources will be relatively limited when contrasted with those of many of these competitors. While we believe that there are potential acquisition targets that we could acquire with our current cash resources, our ability to compete in acquiring certain sizable acquisition targets will be limited by our available financial resources. This inherent competitive limitation gives others an advantage in pursuing the acquisition of certain target businesses. In addition, we are limited in our ability to issue common stock due to limitations arising from maintaining our NOLs, and such limitation may impede our ability to structure any acquisition. Any of the foregoing may place us at a competitive disadvantage in successfully negotiating any acquisition.

**Subsequent to any acquisition, we may be required to take or incur write-downs or write-offs, restructuring and impairment or other charges or expenditures that could have a significant negative effect on our financial condition, results of operations and our stock price, which could cause you to lose some or all of your investment.**

Even if we conduct extensive due diligence on an acquisition target that we acquire, we cannot assure you that this diligence will surface all material issues that may be present inside a particular acquisition target, that it would be possible to uncover all material issues through a customary amount of due diligence, or that factors outside of the acquisition target and outside of our control will not later arise. As a result of these factors, we may be forced to later write-down or write-off assets, restructure our operations, or incur impairment or other charges or expenditures that could result in our reporting losses. Even if our due diligence successfully identifies certain risks, unexpected risks may arise and previously known risks may materialize in a manner not consistent with our preliminary risk analysis. Even if these charges are non-cash items and do not have an immediate impact on our liquidity, the fact that we report charges of this nature could contribute to negative market perceptions about us or our securities. In addition, charges of this nature may cause us to violate net worth or other covenants to which we may be subject as a result of assuming pre-existing debt held by an acquisition target or by virtue of our obtaining financing in connection with any such acquisition. Further, unexpected expenses could have a serious impact on our liquidity.

**A significant portion of our cash could be expended in pursuing acquisitions that are not consummated.**

It is anticipated that the investigation of each specific acquisition target and the negotiation, drafting and execution of relevant agreements, disclosure documents and other instruments will require substantial time and attention and substantial costs for accountants, attorneys and others. In addition, we may opt to make down payments or pay exclusivity or similar fees in connection with structuring and negotiating an acquisition. If a decision is made not to complete a specific acquisition, the costs incurred up to that point in connection with the abandoned transaction, potentially including down payments or exclusivity or similar fees, will not be recoverable. Furthermore, even if an agreement is reached relating to a specific acquisition target, we may fail to consummate the transaction for any number of reasons including those beyond our control. Any such event will result in a loss to us of the related costs incurred, which could materially and adversely affect our subsequent attempts to locate and combine with another business.

**We may be unable to obtain equity or debt financing, if required, to complete an acquisition or to fund the operations and growth of an acquisition target.**

We may be required to seek additional financing through the issuance of equity or debt securities or other financing arrangements to complete an acquisition or under an employee incentive plan after consummation of an acquisition. We cannot assure you that such financing will be available on acceptable terms, if at all. We are limited in our ability to issue common stock due to limitations arising from maintaining our NOLs, and such limitation may impede our ability to structure any equity financing. To the extent that financing proves to be unavailable when needed to consummate a particular acquisition, we may be compelled to restructure or abandon that particular acquisition and seek alternative acquisition targets. The presence of a financing contingency will make us less competitive in relation to other bidders in a particular transaction. In addition, if we complete an acquisition, we may require additional financing to fund the operations or growth of the acquisition target. The failure to secure additional financing could have a material adverse effect on the continued development or growth of our combined business or businesses.

**We may only be able to complete one acquisition with the proceeds of the Merger, which will cause us to be solely dependent on a single business which may have a limited number of products or services.**

It is likely we will only be able to complete an acquisition of a single target business given our limited cash resources and need to rely on substantial leverage. By consummating an acquisition with only a single entity, our lack of diversification may subject us to numerous economic, competitive and regulatory developments. Further, we would not be able to diversify our operations or benefit from the possible spreading of risks or offsetting of losses, unlike other entities which may have the resources to complete several acquisitions in different industries or different areas of a single industry. Accordingly, the prospects for our success may be solely dependent upon the performance of a single business, or dependent upon the development or market acceptance of a single or limited number of products, processes or services.

This lack of diversification may subject us to numerous economic, competitive and regulatory developments, any or all of which may have a substantial adverse impact upon the particular industry in which we may operate subsequent to our initial acquisition.

Alternatively, if we acquire more than one business, we could also face additional risks, including additional burdens and costs with respect to possible multiple negotiations and due diligence investigations (if there are multiple sellers) and the additional risks associated with the subsequent assimilation of the operations and services or products of the acquired companies. If we are unable to adequately address these risks, it could negatively impact our profitability and results of operations.

**Since we have not yet selected a particular industry or acquisition target, we are unable to currently ascertain the merits or risks of the industry or business in which we may ultimately operate.**

We may acquire a company in any industry we choose and are not limited to any particular industry or type of business. Accordingly, there is no current basis for you to evaluate the possible merits or risks of the particular industry in which we may ultimately operate or the target business which we may ultimately acquire. To the extent we complete an acquisition with a financially unstable company or an entity in its development stage, we may be affected by numerous risks inherent in the business operations of those entities. If we complete an acquisition with an entity in an industry characterized by a high level of risk, we may be affected by the currently unascertainable risks of that industry. Although our management will endeavor to evaluate the risks inherent in a particular industry or target business, we may not properly ascertain or assess all of the significant risk factors.

**The officers and directors of an acquisition target may resign upon consummation of an acquisition. The loss of an acquisition target's key personnel could negatively impact the operations and profitability of the target after the acquisition.**

The role of an acquisition target's key personnel upon the consummation of an acquisition cannot be ascertained at this time. Although we contemplate that certain members of an acquisition target's management team will remain associated with the acquisition target following an acquisition, it is possible that members of the management of an acquisition target will not wish to remain in place.

**Our management has significant discretion in determining how to use our cash.**

Our management has significant discretion in determining how to use our cash. Our management may decide to invest in or acquire any business in any industry. You may not have a vote on any of our investment or strategic decisions, and you may disagree with our management's investment or strategic decisions. We cannot predict whether our investments or strategic initiatives will yield a favorable return, or even preserve our initial investment.

**We will be exposed to fluctuations in the value of our investment portfolio.**

We intend to invest our cash in investments such as business development companies, money market funds, certificates of deposit, or direct or guaranteed obligations of the U.S. government, or keep them as cash. We cannot predict whether our investments will yield a favorable return, or even preserve principal. Our management has broad discretion in the investment of our cash, and stockholders will be relying on the judgment of our management regarding such investments.

Any significant decline in the market value of our cash, cash equivalents and marketable securities could materially adversely affect our financial condition and operating results. Credit ratings and pricing of investment securities can be negatively affected by liquidity, credit deterioration, financial results, economic risk, political risk, sovereign risk or other factors. As a result, the value and liquidity of our cash, cash equivalents and marketable securities could decline and result in a significant impairment, which could materially adversely affect our financial condition and operating results.

**We may issue additional common or preferred shares to complete an acquisition or under an employee incentive plan after consummation of an acquisition, which would dilute the interest of our stockholders and likely present other risks.**

We may issue a substantial number of additional shares of common or preferred stock in connection with an acquisition or under an employee incentive plan after consummation of an acquisition. The issuance of additional shares of common or preferred stock:

- may significantly dilute the equity interest of holders of common stock;

- may subordinate the rights of holders of common stock if preferred stock is issued with rights senior

to those afforded our common stock;

- could cause a change in control if a substantial number of common stock is issued, which may affect, among other things, our ability to use our NOLs, if any, and could result in the resignation or removal of our present officers and directors; and

- may adversely affect prevailing market prices for our common stock.

**We may be required to register as an "investment company" under the Investment Company Act if we fail to acquire another operating business within one year.**

We are not engaged in the business of investing, reinvesting or trading in securities, and we do not hold ourselves out as being engaged in those activities. However, under the Investment Company Act of 1940, as amended (the "Investment Company Act"), a company may fall within the scope of being an "inadvertent investment company" if the value of its investment securities (as defined in the Investment Company Act) is more than 40% of its total assets (exclusive of government securities and cash and certain cash equivalents). Our investment securities will likely have a value in excess of 40% of the value of our total assets (exclusive of government securities and cash and certain cash equivalents).

There is an exception that would give us a grace period of one year if we become an inadvertent investment company before we would be required to register as an investment company. This exception would allow us one year from the date of becoming an inadvertent investment company to become engaged primarily in businesses other than investing, reinvesting, owning, holding or trading in securities.

In order to cease being an inadvertent investment company, we intend to acquire one or more operating businesses, or at least controlling interests in one or more operating businesses, so that our principal business will be other than that of investing, reinvesting, owning, holding or trading in securities. There can be no assurance that we will be able to complete such acquisitions by the applicable deadline.

In the event that we are required to register as an investment company under the Investment Company Act, we would be forced to comply with substantive requirements including limitations on our ability to borrow, limitations on our capital structure, limitations on the issuance of debt and equity securities, restrictions on acquisitions of interests in partner companies, prohibitions on transactions with affiliates, prohibitions on the issuance of options and other limitations on our ability to compensate key employees, certain governance requirements, restrictions on specific investments and reporting and record-keeping, voting and proxy disclosure requirements. In the event that we are deemed to be an investment company subject to registration as such under the Investment Company Act, compliance costs and burdens upon ALJ may increase and the additional requirements may adversely affect our business, results of operations or financial condition.

**The Tender Offer reduced our "public float," which may result in lower stock prices or reduced liquidity in the trading market for our shares in the future.**

Our purchase of shares pursuant to the Tender Offer reduced the number of shares of common stock that would otherwise be traded publicly. This may reduce the volume of trading in our shares of common stock and may result in lower stock prices and reduced liquidity in the trading of our shares of common stock.

**Risks Related to our Common Stock**

**Our common stock is illiquid and stockholders may be unable to sell their shares.**

Our common stock is currently quoted on the "Pink Sheets" under the symbol "ALJJ.PK." There is currently only a limited market for our common stock, and we can provide no assurance to investors that a more robust market will develop. If a broader market for our common stock does not develop, our stockholders may encounter difficulties selling their common stock from time to time. We do not have the

ability to uplist our stock on NASDAQ, the NYSE or the AMEX exchanges because we do not meet the qualifications for listing on those exchanges at this time.

**Our stock is a penny stock and, as a result, our stockholders are more limited in their ability to sell their stock.**

The SEC has adopted rules that regulate broker-dealer practices in connection with the sale of penny stocks, or low-priced securities other than securities registered on certain exchanges, to persons other than established customers and institutional accredited investors. Because our securities constitute penny stocks within the meaning of the rules, the rules apply to us and our securities. For transactions covered by these rules, prior to effecting a transaction in a penny stock, a broker-dealer must, among other things: (a) make a special suitability determination for the purchaser; (b) deliver a standardized risk disclosure document to the customer; (c) receive written acknowledgement of the receipt of the disclosure statement; (d) provide to customers current bids and offers, including the number of shares to which such bid and offer prices apply; (e) disclose to customers the broker-dealer and sales representation compensation; and (f) receive the purchaser's written consent to the transaction prior to the sale. These suitability requirements and disclosure requirements may have the effect of reducing the trading activity in the secondary market for our stock.

**Volatility in the market price of our common stock.**

The market price of our common stock could fluctuate substantially in the future in response to a number of factors, including the following:

- our quarterly operating results;
- changes in general conditions in the economy or the financial markets; and
- announcements by us of significant acquisitions.

In addition, in recent years the stock market has experienced extreme price and volume fluctuations. This volatility has had a significant effect on the market prices of securities issued by many companies for reasons unrelated to their operating performance. These broad market fluctuations may materially adversely affect our stock price, regardless of our operating results.

**We do not currently plan to pay dividends to holders of our common stock.**

We do not currently anticipate paying cash dividends to the holders of our common stock. Accordingly, holders of our common stock must rely upon price appreciation as the sole method to realize a gain on their investment. There can be no assurances that the price of our common stock will ever appreciate in value.

**The anti-takeover provisions of our stockholders rights plan may have the effect of delaying or preventing beneficial takeover bids by third parties.**

We have a stockholder rights plan designed to preserve the value of certain tax assets primarily associated with our NOLs and built in losses under Section 382. At September 30, 2012, the Company had approximately $258 million in net operating losses and the use of such losses to offset federal income tax would be limited, if the Company experiences an "ownership change" under Section 382. This would occur if stockholders owning (or deemed under Section 382 to own) 5% or more of the Company's stock by value increase their collective ownership of the aggregate amount of the Company's stock by more than 50 percentage points over a defined period of time. The Rights Plan was adopted to reduce the likelihood of an "ownership change" occurring as defined by Section 382.

In connection with the Rights Plan, the Company declared a dividend of one preferred share purchase right for each share of its common stock outstanding as of the close of business on May 21, 2009. Pursuant to the Rights Plan, any stockholder or group that acquires beneficial ownership of 4.9 percent or more of the Company's outstanding stock (an "Acquiring Person") without the approval of the Company's Board

would be subjected to significant dilution of its holdings. Any existing stockholder holding 4.9% or more of the Company's stock will not be considered an Acquiring Person unless such stockholder acquires additional stock of the Company; provided, however, that existing stockholders actually known to the Company to hold 4.9% or more of its stock as of April 30, 2009 are permitted to purchase up to an additional 5% of the Company's stock without triggering the Rights Plan. In addition, in its discretion, the Board may exempt certain persons whose acquisition of securities is determined by the Board not to jeopardize the Company's deferred tax assets and may also exempt certain transactions. The Rights Plan will continue in effect until May 13, 2019, unless it is terminated or redeemed earlier by the Board.

While the Rights Plan is intended to protect our NOLs and built-in losses under Section 382, it may also have the effect of delaying or preventing beneficial takeover bids by third parties.

**ITEM 8. EXHIBITS**

A list of exhibits required to be filed as part of this report is set forth in the Index to Exhibits, which immediately precedes such exhibits, and is incorporated herein by reference.

**EXHIBITS**

| Exhibit No. | Description |
|---|---|
| 1* | First Amendment to Restated Certificate of Incorporation of ALJ Regional Holdings, Inc. as filed with the Secretary of State of the State of Delaware on June 1, 2010. |
| 2 | Restated Certificate of Incorporation of ALJ Regional Holdings, Inc. as filed with the Secretary of State of the State of Delaware on June 16, 2009 (incorporated by reference to Exhibit 1 to the Company's Quarterly Report for the quarter ended June 30, 2009 available at www.pinksheets.com.). |
| 3 | Certificate of Ownership and Merger of YouthStream Media Networks, Inc. as filed with the Secretary of State of the State of Delaware on October 23, 2006. (incorporated by reference to Exhibit 2 to the Company's Annual Report available at www.pinksheets.com posted on January 15, 2007) |
| 4 | Restated Bylaws of ALJ Regional Holdings, Inc. (incorporated by reference to Exhibit 7 to the Company's Quarterly Report for the quarter ended March 31, 2009 available at www.pinksheets.com.) |
| 5 | YouthStream Media Networks, Inc. 2000 Stock Incentive Plan (incorporated by reference to Exhibit 10.28 to YouthStream's Form 10-KSB filed with the SEC for the fiscal year ended June 30, 1999). |
| 6 | Rights Agreement dated May 13, 2009 by and between ALJ Regional Holdings, Inc. and American Stock Transfer and Trust Company, LLC (incorporated by reference to Annex B to ALJ Regional Holdings proxy statement dated May 15, 2009 available at www.pinksheets.com). |
| 7** | Agreement and Plan of Merger dated November 18, 2012 by and among KES Acquisition Company, ALJ Regional Holdings, Inc., Optima Specialty Steel, Inc. and KES Optima Acquisition Inc. |
| 8** | Form of Stockholder Support Agreement. |
| 9** | Form of Voting and Tender Agreement. |

* Filed with the Company's Quarterly Report for the period ended June 30, 2010.

** Filed with the Company's Current Report dated November 18, 2012.

## ITEM 9. CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER

**Certification of the Chief Executive Officer**

I, John Scheel, hereby certify that:

1. I have reviewed this quarterly disclosure statement of ALJ Regional Holdings, Inc. for the fiscal quarter ended December 31, 2012;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements and other financial information included or incorporated by reference in this disclosure statement, fairly present, in all material respects, the financial condition, results of operations and cash flows of ALJ Regional Holdings, Inc., as of, and for, the fiscal quarter ended December 31, 2012.

Date: February 15, 2013

/S/ John Scheel
John Scheel,
Chief Executive Officer

**Certification of the Chief Financial Officer**

I, T. Robert Christ, hereby certify that:

1. I have reviewed this quarterly disclosure statement of ALJ Regional Holdings, Inc. for the fiscal quarter ended December 31, 2012;
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements and other financial information included or incorporated by reference in this disclosure statement, fairly present, in all material respects, the financial condition, results of operations and cash flows of ALJ Regional Holdings, Inc., as of, and for, the fiscal quarter ended December 31, 2012.

Date: February 15, 2013

/S/ T. Robert Christ
T. Robert Christ,
Chief Financial Officer