NORTH AMERICAN GALVANIZING & COATINGS INC
Form 10-Q
April 27, 2006

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

FORM 10-Q

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

For The Quarterly Period Ended March 31, 2006

Commission File No. 1-3920

NORTH AMERICAN GALVANIZING & COATINGS, INC.
(Exact name of the registrant as specified in its charter)

Delaware
(State of Incorporation)

71-0268502
(I.R.S. Employer Identification No.)

5314 S. Yale Avenue, Suite 1000, Tulsa, Oklahoma 74135
(Address of principal executive offices)

Former address of registrant: 2250 East 73rd Street, Tulsa, Oklahoma 74136

(918) 494-0964
(Registrant's telephone number)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, as defined in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer [ ]   Accelerated filer [ ]   Non-accelerated filer [X]

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of March 31, 2006:

Common Stock $ .10 Par Value............ 6,857,821

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NORTH AMERICAN GALVANIZING & COATINGS, INC.
AND SUBSIDIARY

INDEX TO QUARTERLY REPORT ON FORM 10-Q

FORWARD LOOKING STATEMENTS OR INFORMATION

Certain statements in this Form 10-Q, including information set forth under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations", constitute "Forward-Looking Statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such statements are typically punctuated by words or phrases such as "anticipates," "estimate," "should," "may," "management believes," and words or phrases of similar import. The Company cautions investors that such forward-looking statements included in this Form 10-Q, or hereafter included in other publicly available documents filed with the Securities and Exchange Commission, reports to the Company's stockholders and other publicly available statements issued or released by the Company involve significant risks, uncertainties, and other factors which could cause the Company's actual results, performance (financial or operating) or achievements to differ materially from the future results, performance (financial or operating) or achievements expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences could include, but are not limited to, market substitution of other corrosion protection alternatives, such as paint, changes in demand, prices, the raw materials cost of zinc and the cost of natural gas; changes in economic conditions of the various markets the Company serves, as well as the other risks detailed herein and in the Company's reports filed with the Securities and Exchange Commission. The Company believes that the important factors set forth in the Company's cautionary statements at Exhibit 99 to this Form 10-Q could cause such a material difference to occur and investors are referred to Exhibit 99 for such cautionary statements.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS OF
NORTH AMERICAN GALVANIZING & COATINGS, INC.

We have reviewed the accompanying condensed consolidated balance sheet of North American Galvanizing & Coatings, Inc. and subsidiary (the "Company") as of March 31, 2006, and the related condensed consolidated statements of income and of cash flows for the three-month periods ended March 31, 2006 and 2005. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of North American Galvanizing & Coatings, Inc. and subsidiary as of December 31, 2005, and the related consolidated statements of operations and comprehensive income, stockholders' equity and cash flows for the year then ended (not presented herein); and in our report dated February 10, 2006, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2005 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Deloitte & Touche LLP

Tulsa, Oklahoma

April 27, 2006

NORTH AMERICAN GALVANIZING & COATINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share amounts)

ASSETS	Unaudited March 31, 2006	December 31, 2005
CURRENT ASSETS:		
Cash	$ 768	$ 1,367
Trade receivables--less allowances of $144 for 2006 and $124 for 2005	9,462	6,808
Inventories	6,090	6,077
Prepaid expenses and other assets	551	966
Deferred tax asset--net	193	243
Total current assets	17,064	15,461
PROPERTY, PLANT AND EQUIPMENT--AT COSTS:		
Land	2,167	2,167
Galvanizing plants and equipment	35,572	35,330
	37,739	37,497
Less--allowance for depreciation	(16,584)	(15,954)
Construction in progress	213	325
Total property, plant and equipment--net	21,368	21,868
GOODWILL--Net	3,448	3,448
OTHER ASSETS	277	278
TOTAL ASSETS	$ 42,157	$ 41,055

LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Current maturities of long-term obligations	$ 715	$ 715
Current portion of bonds payable	743	731
Subordinated notes payable	1,000	1,000
Trade accounts payable	1,881	1,838

Accrued payroll and employee benefits	1,034	1,222
Accrued taxes	846	591
Other accrued liabilities	2,033	2,338
Total current liabilities	8,252	8,435
DEFERRED TAX LIABILITY--Net	1,054	1,047
LONG-TERM OBLIGATIONS	7,474	7,072
BONDS PAYABLE	4,956	5,203
Total liabilities	21,736	21,757
COMMITMENTS AND CONTINGENCIES (NOTES 6 AND 7)		
STOCKHOLDERS' EQUITY:		
Common stock--$.10 par value:		
Issued--8,209,925 shares in 2006 and 2005	821	821
Additional paid-in capital	17,488	17,391
Retained earnings	7,525	6,543
Common shares in treasury at cost-- 1,352,104 in 2006 and 1,362,977 in 2005	(5,413)	(5,457)
Total stockholders' equity	20,421	19,298
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 42,157	$ 41,055

See notes to condensed consolidated interim financial statements.

NORTH AMERICAN GALVANIZING & COATINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
THREE MONTHS ENDED MARCH 31, 2006 AND 2005
(In thousands, except per share amounts)

	2006	2005
SALES	$15,411	$ 9,280
COSTS AND EXPENSES:		
Cost of sales	10,996	6,842
Selling, general and administrative expenses	1,841	1,448
Depreciation and amortization	647	619

Total costs and expenses	13,484	8,909
OPERATING INCOME	1,927	371
INTEREST EXPENSE	241	225
INCOME FROM OPERATIONS BEFORE INCOME TAXES	1,686	146
INCOME TAX EXPENSE	704	49
NET INCOME	$ 982	$ 97
NET INCOME PER COMMON SHARE:		
Net income		
Basic	$ 0.14	$ 0.01
Diluted	$ 0.13	$ 0.01

See notes to condensed consolidated interim financial statements.

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NORTH AMERICAN GALVANIZING & COATINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
THREE MONTHS ENDED MARCH, 31 2006 AND 2005
(In thousands, except per share amounts)

	2006	2005
OPERATING ACTIVITIES:		
Net income	$ 982	$ 97
Gain on disposal of assets	7	--
Depreciation	647	619
Deferred income taxes	57	383
Non-cash directors' fees	122	52
Non-cash share-based compensation	19	--
Changes in operating assets and liabilities, net of purchase of assets from Gregory Industries, Inc. (Note 2):		

Accounts receivable--net	(2,654)	(811)
Inventories and other assets	403	(508)
Accounts payable, accrued liabilities and other	(195)	371
Cash provided by (used in) operating activities	(612)	203
INVESTING ACTIVITIES:		
Payment for purchase of Gregory Industries' galvanizing operation	--	(4,129)
Capital expenditures	(154)	(393)
Cash used in investing activities	(154)	(4,522)
FINANCING ACTIVITIES:		
Proceeds from long-term obligations	7,191	8,970
Payments on long-term obligations	(6,789)	(4,837)
Payment on bonds	(235)	(168)
Cash provided by financing activities	167	3,965
DECREASE IN CASH AND CASH EQUIVALENTS	(599)	(354)
CASH AND CASH EQUIVALENTS:		
Beginning of year	1,367	634
End of year	$ 768	$ 280
CASH PAID DURING THE YEAR FOR:		
Interest	$ 410	$ 261
Income taxes	$ 277	$ 9

See notes to condensed consolidated interim financial statements.

NORTH AMERICAN GALVANIZING & COATINGS, INC.AND SUBSIDIARY
NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2006 and 2005
UNAUDITED

NOTE 1. BASIS OF PRESENTATION

The condensed consolidated interim financial statements included in this report have been prepared by North American Galvanizing & Coatings, Inc. (the "Company") pursuant to its understanding of the rules and regulations of the Securities and Exchange Commission for interim reporting and include all normal and recurring adjustments which are, in the opinion of management, necessary for a fair presentation. The condensed consolidated interim financial statements include the accounts of the Company and its subsidiary.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations for interim reporting. The Company believes that the disclosures are adequate to make the information presented not misleading. However, these interim financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005. The financial data for the interim periods presented may not necessarily reflect the results to be anticipated for the complete year.

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 and disclosure of contingent assets and liabilities at the balance sheet dates and the reported amounts of revenues and expenses for each of the periods. Actual results will be determined based on the outcome of future events and could differ from the estimates. The Company's sole business is hot dip galvanizing and coatings which is conducted through its wholly owned subsidiary, North American Galvanizing Company ("NAG").

NOTE 2. BUSINESS EXPANSION - PURCHASE OF ASSETS

On February 28, 2005, NAGalv-Ohio, Inc., a subsidiary of North American Galvanizing Company, purchased certain galvanizing assets of Gregory Industries, Inc., located in Canton, Ohio, for a cash purchase price of $3.7 million plus approximately $0.5 million in purchase related expenses. The purchase expands the service area of North American Galvanizing into the northeast region of the United States. The results of the operations of NAGalv-Ohio, Inc. have been included in the consolidated financial statements since February 28, 2005. Goodwill of less than $0.1 million was recognized in the purchase. The net purchase price was allocated as follows:

Current assets	$1.8 million
Net property, plant & equipment	2.3
Goodwill	0.1
Purchase price	$4.2 million

Pro-forma unaudited results of operations of the Company for the three-month period ended March 31, 2005, prepared as if the purchase had taken place on January 1, 2005 would have been as follows:
(Dollars in Thousands, Except per Share Amounts)

Sales	$ 10,383
Net Loss	(23)
Earnings per share:	
Basic and Diluted	$ --

NOTE 3. STOCK OPTIONS

On March 31, 2006 the Company has two share-based compensation plans, which are shareholder-approved, the 2004 Incentive Stock Plan and the Director Stock Unit Plan (Note 7). The Company's 2004 Incentive Stock (the Plan) permits the grant of share options and shares to its employees and directors for up to 1,250,000 shares of common stock. The Company believes that such awards better align the interests of its employees and directors with those of its shareholders. Option awards are granted with an exercise price equal to the market price of the Company's stock at the date of grant; those option awards vest based on 4 years of continuous service and have 10-year contractual terms.

The Company adopted Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment" ("SFAS No. 123(R)") under the modified prospective method on January 1, 2006. Under the "modified prospective" method, compensation cost is recognized in the financial statements beginning with the effective date, based on the requirements of SFAS No. 123(R) for all share-based payments granted after that date, and based on the requirements of Statement of Financial Accounting Standards No.123, "Accounting for Stock Based Compensation" ("SFAS No. 123") for all unvested awards granted prior to the effective date of SFAS No. 123(R).

SFAS No. 123(R) eliminates the intrinsic value measurement method of accounting in APB Opinion 25 and generally requires measuring the cost of the employee services received in exchange for an award of equity instruments based on the fair value of the award on the date of the grant. The standard requires grant date fair value to be estimated using either an option-pricing model which is consistent with the terms of the award or a market observed price, if such a price exists. Such costs must be recognized over the period during which an employee is required to provide service in exchange for the award. The standard also requires estimating the number of instruments that will ultimately be issued, rather than accounting for forfeitures as they occur.

The compensation cost that has been charged against pre-tax income for the Plan was $19,000 for the first quarter of 2006, with an income tax benefit of $7,000. There was no share-based compensation cost capitalized during the first three months of 2006.

In the first quarter of 2005, the Company accounted for its stock option plans in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees", under which no compensation cost was recognized for stock option awards. Had compensation cost for the Company's stock option plans been determined according to the methodology of SFAS No. 123, the Company's pro forma net earnings and basic and diluted earnings per share for the three months ended March 31, 2005 would have been as follows:

(Dollars in Thousands, Except per Share Amounts)	
Net Income, as reported	$ 97
Deduct: Total stock-based employee compensation expense determined under fair value based methods, net of tax	$ (6)
Pro forma net income	$ 91
Earnings per share:	
Basic and Diluted - as reported	$ .01
Basic and Diluted - pro forma	$ .01

The fair value of options granted under the Company's stock option plans was estimated using the Black-Scholes option-pricing model with the following assumptions used:

	Quarter Ended March 31	
	2006	2005
Volatility	55%	54%
Discount Rate	4.7%	4%
Dividend Yield	0%	0%
Fair Value	$1.47	$1.72

In the first quarter of 2006, the Company issued stock options for 157,500 shares at $2.10 per share, and issued stock options for 50,000 shares at $2.50 per share in the first quarter of 2005.

NOTE 4. INCOME PER COMMON SHARE

Basic earnings per common share for the periods presented are computed based upon the weighted average number of shares outstanding, adjusted for stock unit grants. Diluted earnings per common share for the periods presented are based on the weighted average shares outstanding, adjusted for stock unit grants and for the assumed exercise of stock options and warrants using the treasury stock method.

Three Months Ended March 31	Number of Shares	
	2006	2005
Basic	7,022,181	6,909,360
Diluted	7,790,182	7,626,642

The options excluded from the calculation of diluted earnings per share, due to the option price being higher than the share market value, are 295,000 and 296,500 at March 31, 2006 and 2005, respectively.

NOTE 5. LONG-TERM OBLIGATIONS

(Dollars in Thousands)	March 31 2006	December 31 2005
Revolving line of credit	$ 3,944	$ 3,304
Term loan	4,228	4,465
9.5% note due 2015	17	18
	$ 8,189	$ 7,787
Less current portion	(715)	(715)
	$ 7,474	$ 7,072

In February 2006, North American Galvanizing & Coatings, Inc. offered the noteholders of its $1 million subordinated promissory notes the opportunity to extend the maturity date one year to February 17, 2007. All other note terms remained unchanged. The extension, which was offered on a voluntary basis, was 100% subscribed

In February 2005, the Company amended a three-year bank credit agreement that was scheduled to expire in December 2007 and extended its maturity to February 28, 2008. Subject to borrowing base limitations, the amended agreement provides (i) an $8,000,000 maximum revolving credit facility for working capital and general corporate purposes and (ii) a $5,001,000 term loan that combined the outstanding principal balance of the existing term loan with additional financing for the purchase of assets of a galvanizing facility (Note 2).

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Term loan payments are based on a seven-year amortization schedule with equal monthly payments of principal and interest, and a final balloon payment in February 2008. The term loan may be prepaid without penalty. The revolving line of credit may be paid down without penalty, or additional funds may be borrowed up to the maximum line of credit. At March 31, 2006, the Company had unused borrowing capacity of $3,502,000 under the line of credit, based on the underlying borrowing base of accounts receivable and inventory. At March 31, 2006, $3,944,277 was outstanding under the bank credit agreement, and $553,505 was reserved for outstanding irrevocable letters of credit to secure payment of current and future workers' compensation claims.

Substantially all of the Company's accounts receivable, inventories, fixed assets and the common stock of its subsidiary are pledged as collateral under the agreement, and the credit agreement is secured by a full and unconditional guaranty from NAG. Amounts borrowed under the agreement bear interest at the prime rate of JPMorgan Chase Bank or the LIBOR rate, at the option of the Company, subject to a rate margin adjustment determined by the Company's consolidated debt service coverage ratio. The interest rate on these borrowings was 8.00% at March 31, 2006. In the event the Company fails to maintain a consolidated debt service coverage ratio for any fiscal quarter of at least 1.25 to 1.00, the Applicable LIBOR Rate Margin will be increased from 3.0% to 5.75% and the Applicable Prime Rate Margin will be increased from .25% to 3.00%. Thereafter, the increased rate margin will remain in effect until such time as the Company has maintained a consolidated debt service coverage ratio greater than or equal to 1.25 to 1.00 for a subsequent fiscal quarter.

In the event the Company fails to maintain a consolidated EBITDA to capital expenditures plus current maturity of long-term debt ratio for any fiscal quarter of not less than 1.00 to 1.00, the increase in the Applicable LIBOR Rate Margin ranges from 3.75% to 5.75%, and the increase in the Applicable Prime Rate Margin ranges from 1.00% to 3.00%.

The credit agreement requires the Company to maintain compliance with covenant limits for current ratio, debt to tangible net worth ratio, debt service coverage ratio and a capital expenditures ratio. At March 31, 2006, the Company was in compliance with the covenants. The actual financial ratios compared to the required ratios, were as follows: Current Ratio - actual 2.07 versus minimum required of 1.10; Debt to Tangible Net Worth Ratio - actual 1.28 vs. maximum permitted of 2.50; Debt Service Coverage Ratio - actual 2.18 versus minimum permitted of 1.25; Capital Expenditures Coverage Ratio - actual 1.71 versus minimum required of 1.0.

NOTE 6. COMMITMENTS AND CONTINGENCIES

The Company has commitments with domestic and foreign zinc producers and brokers to purchase zinc used in its hot dip galvanizing operations. Commitments for the future delivery of zinc reflect rates then quoted on the London Metals Exchange and are not subject to price adjustment or are based on such quoted prices at the time of delivery. At March 31, 2006 the aggregate commitments for the procurement of zinc at fixed prices were approximately $1.6 million. The Company reviews these fixed price contracts for losses using the same methodology employed to estimate the market value of its zinc inventory. The Company had unpriced commitments for the purchase of approximately one million pounds of zinc at March 31, 2006.

The Company's financial strategy includes evaluating the selective use of derivative financial instruments to manage zinc and interest costs. As part of its inventory management strategy, the Company expects to continue evaluating hedging instruments to minimize the impact of zinc price fluctuations. The Company had no derivative instruments required to be reported at fair value at March 31, 2006 or December 31, 2005, and did not utilize derivatives in the three-month period ended March 31, 2006 or the year ended December 31, 2005, except for the forward purchase agreements described above, which are accounted for as normal purchases.

The Company's total off-balance sheet contractual obligations at March 31, 2006, consist of approximately $2.1 million for long-term operating leases for vehicles, office space, office equipment, galvanizing facilities and galvanizing equipment and approximately $1.6 million for zinc purchase commitments. The various leases for galvanizing facilities, including option renewals, expire from 2006 to 2017. A lease for galvanizing equipment expires in 2007.

On August 30, 2004, the Company was informed by counsel for the Metropolitan Water Reclamation District of Greater Chicago (the "Water District") that the Water District had, on August 25, 2004 filed a Second Amended Complaint in the United States District Court, Northern District of Illinois, Eastern Division, naming North American Galvanizing & Coatings, Inc. (formerly known as Kinark Corporation) as an added defendant. Counsel for the Water District also gave the Company notice of the Water District's intent to file (or amend the Complaint to include) a Citizens Suit under the Resource Compensation and Recovery Act ("RCRA") against North American Galvanizing & Coatings, Inc., pursuant to Section 7002 of RCRA, 42 U.S.C. Section 6972. This Second Amended Complaint seeks enforcement of an August 12, 2004 default judgment in the amount of $1,810,463.34 against Lake River Corporation and Lake River Holding Company, Inc. in connection with the operation of a storage terminal by Lake River Corporation in violation of environmental laws. Lake River Corporation conducted business as a subsidiary of the Company until June 30, 2000, at which time Lake River Corporation was sold to Lake River Holding Company, Inc. and ceased to be a subsidiary of the Company. The Second Amended Complaint asserts that prior to the sale of Lake River Corporation, the Company directly operated the Lake River facility and, accordingly, seeks to have the Court pierce the corporate veil of Lake River Corporation and enforce the default judgment order of August 12, 2004 against the Company. The Company denies the assertions set forth in the Water District's Complaint and on November 13, 2004 filed a partial motion for dismissal of the Second Amended Complaint.

In December 2004, the Water District filed a Third Amended complaint in the litigation, adding two claims: (1) a common law claim for nuisance; and (2) a claim under the federal Resource Conservation and Recovery Act, in which the Water District argues that the Company is responsible for conditions on the plaintiff's property that present an "imminent and substantial endangerment to human health and the environment." In January 2005, the Company filed a partial motion to dismiss the Third Amended Complaint. On April 12, 2005, the Court issued an order denying in part and granting in part the Company's partial motion to dismiss plaintiff's third amended complaint. The Company has filed an appeal with the Seventh Circuit Court of Appeals requesting dismissal of the sole CERCLA claim contained in the Third Amended Complaint that was not dismissed by the United States District Court's April 12, 2005 order. The Water District has also attempted to appeal those rulings contained in the April 12, 2005 that are adverse to the Water District. Meanwhile, litigation in the United States District Court continues.

The Company has denied any liability with respect to this claim and intends to vigorously defend this case. At this time, the Company has not determined the amount of any liability that may result from this matter or whether such liability, if any, would have a material adverse effect on the Company's financial condition, results of operations, or liquidity.

NAG was notified in 1997 by the Illinois Environmental Protection Agency ("IEPA") that it was one of approximately 60 potentially responsible parties ("PRPs") under the Comprehensive Environmental Response, Compensation, and Liability Information System ("CERCLIS") in connection with cleanup of an abandoned site formerly owned by Sandoval Zinc Co. A number of the PRPs have agreed to work together and with IEPA on a voluntary basis. The Company has been and continues to participate in this volunteer group. The group has retained consultants and legal representatives familiar with IEPA regulations. This volunteer group, with its consultants, has cooperated with IEPA in attempting to better define the environmental issues associated with the Sandoval Zinc site. To that extent, this voluntary group

prepared and submitted to IEPA in August 2000 a work plan. The purpose of this work plan is to attempt to define the extent of environmental remediation that might be required, assess risks, and review alternatives to addressing potential remediation. The IEPA has yet to respond to this proposed work plan or suggest any other course of action, and there has been no activity in regards to this issue during 2006. Therefore, the Company has no basis for determining potential exposure and estimated remediation costs at this time.

The Company is committed to complying with all federal, state and local environmental laws and regulations and using its best management practices to anticipate and satisfy future requirements. As is typical in the galvanizing business, the Company will have additional environmental compliance costs associated with past, present and future operations. Management is committed to discovering and eliminating environmental issues as they arise. Because of frequent changes in environmental technology, laws and regulations management cannot reasonably quantify the Company's potential future costs in this area.

North American Galvanizing & Coatings, Inc. and its subsidiary are parties to a number of other lawsuits and environmental matters which are not discussed herein. Management of the Company, based upon their analysis of known facts and circumstances and reports from legal counsel, does not believe that any other such matter will have a material adverse effect on the results of operations, financial conditions or cash flows of the Company.

NOTE 7. DIRECTOR STOCK UNIT PROGRAM

On January 1, 2005, the Company implemented the Director Stock Unit Program (approved by the stockholders at the Annual Meeting held July 21, 2004) under which a Director is required to defer 50% of his or her board fee and may elect to defer up to 100% of his or her board fee, plus a matching contribution by the Company that varies from 25% to 75% depending on the level of deferral. Such deferrals are converted into a stock unit grant, payable to the Director five years following the year of deferral. For 2005 and 2006, all of the Company's Outside Directors elected to defer 100% of the annual board fee and the Company's chief executive officer and Inside Director has elected to defer a corresponding amount of his salary. Outside Directors currently receive an annual fee of $35,000, which includes attendance at board meetings and service on committees of the board. In the first three months of 2005, fees and salary deferred by the Directors represented a total of 26,250 stock unit grants valued at $2.00 per stock unit. In the first three months of 2006, fees and salary deferred by the Directors represented a total of 60,345 stock unit grants valued at $2.03 per stock unit. The value of a stock unit grant is the average of the closing prices for a share of the Company's stock for the 10 trading days before the date the director fees otherwise would have been payable in cash.

NOTE 8. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

A subsidiary of North American Galvanizing Company (NAGalv-Ohio, Inc.) purchased the after-fabrication hot dip galvanizing assets of Gregory Industries, Inc. located in Canton, Ohio on February 28, 2005. Gregory Industries, Inc. is a manufacturer of products for the highway industry. T. Stephen Gregory, appointed a director of North American Galvanizing & Coatings, Inc. on June 22, 2005 is the chairman of the board and a shareholder of Gregory Industries, Inc. Total sales to Gregory Industries, Inc. for the three-month periods ended March 31, 2006 and 2005 were approximately $293,000 and $118,400, respectively. The amount due from Gregory Industries, Inc. included in trade receivables at March 31, 2006 and December 31, 2005 was $215,100 and $254,000, respectively.

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NORTH AMERICAN GALVANIZING & COATINGS, INC. AND SUBSIDIARY

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

North American Galvanizing is a leading provider of corrosion protection for iron and steel components fabricated by its customers. Hot dip galvanizing is the process of applying a zinc coating to fabricated iron or steel material by immersing the material in a bath consisting primarily of molten zinc. Based on the number of its operating plants, the Company is one of the largest merchant market hot dip galvanizing companies in the United States.

During the three-month period ended March 31, 2006, there were no significant changes to the Company's critical accounting policies previously disclosed in Form 10-K for the year ended December 31, 2005.

On February 28, 2005, NAGalv-Ohio, Inc., a subsidiary North American Galvanizing Company, purchased the hot-dip galvanizing assets of a galvanizing facility located in Canton, Ohio. The transaction was structured as an asset purchase, pursuant to an Asset Purchase Agreement dated February 28, 2005 by and between NAGalv-Ohio, Inc., and the privately owned Gregory Industries, Inc. for all of the plant, property and equipment of Gregory Industries' after-fabrication hot dip galvanizing operation. Operating results of the purchased galvanizing business are included in the Company's financial statements commencing from the date of the purchase on February 28, 2005.

The Company's galvanizing plants offer a broad line of services including centrifuge galvanizing for small threaded products, sandblasting, chromate quenching, polymeric coatings, and proprietary INFRASHIELDSM Coating Application Systems for polyurethane protective linings and coatings over galvanized surfaces. The Company's mechanical and chemical engineers provide customized assistance with initial fabrication design, project estimates and steel chemistry selection.

The Company's galvanizing and coating operations are composed of eleven facilities located in Colorado, Kentucky, Missouri, Ohio, Oklahoma, Tennessee and Texas. These facilities operate galvanizing kettles ranging in length from

16 feet to 62 feet, and have lifting capacities ranging from 12,000 pounds to 40,000 pounds.

The Company maintains a sales and service network coupled with its galvanizing plants, supplemented by national account business development at the corporate level. In a typical year, the Company will galvanize in excess of 365,000,000 pounds of steel products for approximately 2,000 customers nationwide.

All of the Company's sales are generated for customers whose end markets are principally in the United States. The Company markets its galvanizing and coating services directly to its customers and does not utilize agents or distributors. Although hot dip galvanizing is considered a mature service industry, the Company is actively engaged in developing new markets through participation in industry trade shows, metals trade associations and presentation of technical seminars by its national marketing service team.

Hot dip galvanizing provides metals corrosion protection for many product applications used in commercial, construction and industrial markets. The Company's galvanizing can be found in almost every major application and industry that requires corrosion protection where iron or steel is used, including the following end user markets:

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- highway and transportation,
- power transmission and distribution,
- wireless and telecommunications,
- utilities,
- petrochemical processing,
- industrial grating,
- infrastructure including buildings, airports, bridges and power generation;
- wastewater treatment,
- fresh water storage and transportation;
- pulp and paper,
- pipe and tube,
- food processing,
- agricultural (irrigation systems),
- recreation (boat trailers, marine docks, stadium scaffolds),
- bridge and pedestrian handrail,
- commercial and residential lighting poles, and
- original equipment manufactured products, including general fabrication.

As a value-added service provider, the Company's revenues are directly influenced by the level of economic activity in the various end markets that it serves. Economic activity in those markets that results in the expansion and/or upgrading of physical facilities (i.e., construction) may involve a time-lag factor of several months before translating into a demand for galvanizing fabricated components. Despite the inherent seasonality associated with large project construction work, the Company maintains a relatively stable revenue stream throughout the year by offering fabricators, large and small, reliable and rapid turn-around service.

The Company records revenues when the galvanizing and coating processes are completed. The Company generates all of its operating cash from such revenues, and utilizes a line of credit secured by the underlying accounts receivable and zinc inventory to facilitate working capital needs.

Each of the Company's galvanizing plants operate in a highly competitive environment underscored by pricing pressures, primarily from other public and privately-owned galvanizers and alternative forms of corrosion protection, such as paint. The Company's long-term response to these challenges has been a sustained strategy focusing on providing a reliable quality of galvanizing to standard industry technical specifications and rapid turn-around time on every project, large and small. Key to the success of this strategy is the Company's continuing commitment and long-term record of reinvesting earnings to upgrade its galvanizing facilities and provide technical innovations to improve production efficiencies; and to construct new facilities when market conditions present opportunities for growth. The Company is addressing long-term opportunities to expand its galvanizing and coatings business through programs to increase industry awareness of the proven, unique benefits of galvanizing for metals corrosion protection. Each of the Company's galvanizing plants is linked to a centralized system involving sales order entry, facility maintenance and operating procedures, quality assurance, purchasing and credit and accounting that enable the plant to focus on providing galvanizing and coating services in the most cost-effective manner.

The principal raw materials essential to the Company's galvanizing and coating operations are zinc and various chemicals which are normally available for purchase in the open market.

KEY INDICATORS

Key industries which historically have provided the Company some indication of the potential demand for galvanizing in the near-term, (i.e., primarily within a year) include highway and transportation, power transmission and distribution, telecommunications and the level of quoting activity for regional metal fabricators. In general, growth in the commercial/industrial sectors of the economy generates new construction and capital spending which ultimately impacts the demand for galvanizing.

Key operating measures utilized by the Company include new orders, zinc inventory, tons of steel galvanized, revenue, pounds and labor costs per hour, zinc usage related to tonnage galvanized, and lost-time safety performance. These measures are reported and analyzed on various cycles, including daily, weekly and monthly.

The Company utilizes a number of key financial measures to evaluate the operations at each of its galvanizing plants, to identify trends and variables impacting operating productivity and current and future business results, which include: return on capital employed, sales, gross profit, fixed and variable costs, selling and general administrative expenses, operating cash flows, capital expenditures, interest expense, and a number of ratios such as profit from operations and accounts receivable turnover. These measures are reviewed by the Company's operating and executive management each month, or more frequently, and compared to prior periods, the current business plan and to standard performance criteria, as applicable.

KEY DEVELOPMENTS

During the period of January, 2003 through February 2005, the Company reported a number of developments supporting its strategic program to reposition its galvanizing business in the national market.

On February 28, 2005, NAGalv-Ohio, Inc., a subsidiary of North American Galvanizing Company, purchased the hot-dip galvanizing assets of a galvanizing facility located in Canton, Ohio. The transaction was structured as an asset purchase, pursuant to an Asset Purchase Agreement dated February 28, 2005 by and between NAGalv-Ohio, Inc., and the privately owned Gregory Industries, Inc. for all of the plant, property, and equipment of Gregory Industries' after-fabrication hot dip galvanizing operation. Operating results of the purchased galvanizing business are included in the Company's financial statements commencing from the date of purchase on February 28, 2005.

This strategic expansion provides NAG an important, established customer base of major fabricators serving industrial, OEM, and highway markets as well as residential and commercial markets for lighting poles. Canton's 52 foot long dipping kettle is designed to handle large steel structures, such as bridge beams, utility poles and other steel structural components that require galvanizing for extended-life corrosion protection. The Canton plant also processes small parts used in construction, such as nuts and anchor rods, in a dedicated facility with a smaller 16 foot dipping kettle and a spinner operation.

In January 2003, the Company opened its St. Louis galvanizing plant, replacing a smaller plant at the same location. This larger facility is providing NAG a strategic base for extending its geographic area of service. A 51-foot kettle at this facility provides the largest galvanizing capacity in the St. Louis region. In 2004, production tonnage at St. Louis more than doubled compared to production at the plant it replaced.

In January 2003, the Company expanded services at its Nashville galvanizing plant with the announced installation of a state-of-the-art spinner line to galvanize small products, including bolts and threaded material.

RESULTS OF OPERATIONS

The following table shows the Company's results of operations for the three months ended March 31, 2006 and 2005:

	THREE MONTHS ENDED MARCH 31			
	2006		2005	
(DOLLARS IN THOUSANDS)	AMOUNT	% OF SALES	AMOUNT	% OF SALES
Sales	$ 15,411	100.0%	$ 9,280	100.0%
Cost of sales	10,996	71.4%	6,842	73.7%
Gross profit	4,415	28.6%	2,438	26.3%
Selling, general & administrative expenses	1,841	11.9%	1,448	15.6%
Depreciation and amortization	641	4.2%	619	6.7%
Operating income	1,927	12.5%	371	4.0%
Interest expense	241	1.6%	225	2.4%
Income before income taxes	1,686	10.9%	146	1.6%
Income tax expense	704	4.6%	49	--
Net Income	$ 982	6.4%	$ 97	1.0%

2006 COMPARED TO 2005

Sales. Sales for the first quarter ended March 31, 2006 increased 66% over the prior year. The main reason for the increase was a 55% increase in same plant revenues. The remaining revenue increase is due to the Canton, Ohio galvanizing facility, purchased on February 28, 2005. The first quarter 2006 results include three months for Ohio versus only one month in first quarter 2005. In 2005, North American Galvanizing's same plants started the year with a period of slow demand in the first two months. A general increase in demand from fabricators led to a positive trend continuing throughout the year and into 2006. Most customers provided increased volumes in the first quarter of this year. In addition to a general increase in work, non-routine projects related to highway and electrical distribution contributed to the volume increase in the first three months of 2006. First quarter 2006 volumes are 41% higher than the first quarter of 2005 and 18% higher than the 4th quarter of 2005.

Sales prices have increased in the quarter related to increases in zinc and energy costs. In the three-months ended March 31, 2006, average selling prices for galvanizing and related coating services were 18% higher than the prior year first quarter and 9% higher than 4th quarter 2005.

GROSS PROFIT. The gross profit percentage increased 2.3% for the first quarter of 2006 versus the first quarter of 2005.

Due to higher material and energy costs, general customer pricing was increased during the second half of 2005 and the first quarter of 2006. Higher selling prices contributed 15.2% to the gross profit percentage, compared to the prior year first quarter. With these increases in price for galvanizing, the market could react by using other corrosion protection alternatives, such as paint, or by postponing projects. The Company cannot be assured that continuing zinc price increases will be absorbed by the market.

During the first quarter of 2006, zinc costs rose dramatically. The London Metals Exchange (LME) market price for zinc for the first quarter of 2006 averaged $1.02 per pound, compared to $.59 per pound in the first quarter of 2005. At March 31, 2006, the LME market price for zinc was $1.22 per pound. The Company's zinc forward purchase program resulted in some zinc purchases at lower prices than market. Material cost increases were limited to a negative 8.8% impact on gross profit percentage, compared to the prior year first quarter.

Other cost increases, including natural gas, resulted in a negative 2.5% impact on the gross profit percentage, when comparing the first quarter of 2006 to 2005.

Increased costs in the Canton, Ohio galvanizing facility compared to same plants resulted in a negative 1.6% impact on the gross profit percentage, when comparing the first quarter of 2006 to 2005. The primary difference in costs is higher labor costs at the Ohio plant. As part of the transition program started with the February 28, 2005 purchase, management is focused on improving labor efficiency, measured by pounds-per-man-hour and cost-per-man-hour, at this facility.

SELLING, GENERAL AND ADMINISTRATIVE (SG&A) EXPENSES. SG&A increased $393,000, in the first quarter of 2006 to $1,841,000 compared to $1,448,000 in the first quarter of 2005.

The increases are as follows: $115,000 for legal fees related to the Lake River litigation, $74,000 increase for the Canton, Ohio operation purchased February

28, 2005, $72,000 increase in board of director fees due to an increase of fees and the addition of two directors, $54,000 increase in personnel compensation costs, $35,000 increase in bad debt expense, $31,000 increase in travel and entertainment, $19,000 increase in computer and networking costs, offset by $61,000 decrease in audit and tax fee expense, and $24,000 decrease in group health expenses. Other variances from the prior year first quarter SG&A totaled an increase of $78,000.

Selling, general, and administrative expenses decreased as a percentage of sales from 15.6% in first quarter 2005 to 11.9% in first quarter 2006.

Income Taxes. The Company's effective income tax rates for the first quarter of 2006 and 2005 were 41.7% and 33.5%, respectively. The effective tax rates differ from the federal statutory rate primarily due to state income taxes and, in 2005, minor adjustments to previous tax estimates based on actual tax returns filed.

Net Income. For the first quarter of 2006, the Company reported net income of $982,000 compared to net income of $97,000 for the first quarter of 2005. The increase in net income is primarily due to the increase in volume and average selling price from the first three months of 2005 to the first three months of 2006.

LIQUIDITY AND CAPITAL RESOURCES

The Company's cash flow from operations and borrowings under credit facilities have consistently been adequate to fund its current facilities' working capital and base capital spending requirements. During 2006 and 2005, operating cash flow and borrowings under credit facilities have been the primary sources of liquidity. The Company monitors working capital and planned capital spending to assess liquidity and minimize cyclical cash flow.

Cash flow from operating activities for the first three months of 2006 and 2005 was ($612,000) and $203,000, respectively. The decrease of $815,000 in 2006 cash flow from operations was due to increased working capital needs, primarily an increase in accounts receivable due to the significant growth in revenues.

Cash of $154,000 used in 2006 investing activities through March 31 consisted of capital expenditures for equipment and upgrade of existing galvanizing facilities. Investing activities in the first quarter of 2005 included $4,129,000 to acquire certain assets of Gregory Industries' Inc. and capital expenditures of $393,000 for equipment to maintain galvanizing facilities. The Company expects base capital expenditures for 2006 to approximate $1,450,000.

Total debt (current and long-term obligations) increased $167,000 to $14,888,000 in the first three months of 2006. Financing activities for first quarter of 2006 included: payments of $235,000 to a bond sinking fund, proceeds of $7,191,000 from a bank line of credit, and payments of $6,789,000 on the bank line of credit and term loans.

To preserve liquidity, the Company offered to the subordinated noteholders an opportunity to extend the maturity of the debt one year, to February 17, 2007. One hundred percent of the subordinated noteholders agreed to extend the maturity of their notes . All other terms of the notes remained the same. There were no fees associated with the extension.

In February 2005, the Company amended the three-year bank credit agreement that was scheduled to expire in December 2007 and extended its maturity to February 28, 2008. Subject to borrowing base limitations, the amended agreement provided

(i) an $8,000,000 maximum revolving credit facility for working capital and general corporate purposes and (ii) a $5,001,000 term loan that combined the outstanding principal balance of the existing term loan with additional financing for the purchase of assets of a galvanizing facility (Note 2). Term loan payments are based on a seven-year amortization schedule with equal monthly payments of principal and interest, and a final balloon payment in February 2008. The term loan may be prepaid without penalty. The revolving line of credit may be paid down without penalty, or additional funds may be borrowed up to the maximum line of credit. At March 31, 2006, the Company had unused borrowing capacity of $3,502,000 under the line of credit, based on the underlying borrowing base of accounts receivable and inventory. At March 31, 2006, $3,944,277 was outstanding under the bank credit agreement, and $553,505 was reserved for outstanding irrevocable letters of credit to secure payment of current and future workers' compensation claims.

Substantially all of the Company's accounts receivable, inventories, fixed assets and the common stock of its subsidiary are pledged as collateral under the agreement, and the credit agreement is secured by a full and unconditional guaranty from NAG. Amounts borrowed under the agreement bear interest at the prime rate of JPMorgan Chase Bank or the LIBOR rate, at the option of the Company, subject to a rate margin adjustment determined by the Company's consolidated debt service coverage ratio. The interest rate on these borrowings was 8.00% at March 31, 2006. In the event the Company fails to maintain a consolidated debt service coverage ratio for any fiscal quarter of at least 1.25 to 1.00, the Applicable LIBOR Rate Margin will be increased from 3.0% to 5.75% and the Applicable Prime Rate Margin will be increased from .25% to 3.00%. Thereafter, the increased rate margin will remain in effect until such time as the Company has maintained a consolidated debt service coverage ratio greater than or equal to 1.25 to 1.00 for a subsequent fiscal quarter.

In the event the Company fails to maintain a consolidated EBITDA to capital expenditures plus current maturity of long-term debt ratio for any fiscal quarter of not less than 1.00 to 1.00, the increase in the Applicable LIBOR Rate Margin ranges from 3.75% to 5.75%, and the increase in the Applicable Prime Rate Margin ranges from 1.00% to 3.00%.

The credit agreement requires the Company to maintain compliance with covenant limits for current ratio, debt to tangible net worth ratio, debt service coverage ratio and a capital expenditures ratio. At March 31, 2006, the Company was in compliance with the covenants. The actual financial ratios compared to the required ratios, were as follows: Current Ratio - actual 2.07 versus minimum required of 1.10; Debt to

Tangible Net Worth Ratio - actual 1.28 vs. maximum permitted of 2.50; Debt Service Coverage Ratio - actual 2.18 versus minimum permitted of 1.25; Capital Expenditures Coverage Ratio - actual 1.71 versus minimum required of 1.0.

The Company has various commitments primarily related to long-term debt, industrial revenue bonds, operating lease commitments, zinc purchase commitments and vehicle operating leases. The Company's total off-balance sheet contractual obligations at March 31, 2006, consist of approximately $2.1 million for long-term operating leases for vehicles, office space, office equipment, galvanizing facilities and galvanizing equipment and approximately $1.6 million for zinc purchase commitments. The various leases for galvanizing facilities, including option renewals, expire from 2006 to 2017. A lease for galvanizing equipment expires in 2007. NAG periodically enters into fixed price purchase commitments with domestic and foreign zinc producers to purchase a portion of its requirements for its hot dip galvanizing operations; commitments for the future delivery of zinc can be for up to one year.

ENVIRONMENTAL MATTERS

The Company's facilities are subject to extensive environmental legislation and regulations affecting their operations and the discharge of wastes. The cost of compliance with such regulations in the first three months of 2006 and 2005 was approximately $287,000 and $302,000, respectively, for the disposal and recycling of wastes generated by the galvanizing operations.

On August 30, 2004, the Company was informed by counsel for the Metropolitan Water Reclamation District of Greater Chicago (the "Water District") that the Water District had, on August 25, 2004 filed a Second Amended Complaint in the United States District Court, Northern District of Illinois, Eastern Division, naming North American Galvanizing & Coatings, Inc. (formerly known as Kinark Corporation) as an added defendant. Counsel for the Water District also gave the Company notice of the Water District's intent to file (or amend the Complaint to include) a Citizens Suit under the Resource Compensation and Recovery Act ("RCRA") against North American Galvanizing & Coatings, Inc., pursuant to Section 7002 of RCRA, 42 U.S.C. Section 6972. This Second Amended Complaint seeks enforcement of an August 12, 2004 default judgment in the amount of $1,810,463.34 against Lake River Corporation and Lake River Holding Company, Inc. in connection with the operation of a storage terminal by Lake River Corporation in violation of environmental laws. Lake River Corporation conducted business as a subsidiary of the Company until June 30, 2000, at which time Lake River Corporation was sold to Lake River Holding Company, Inc. and ceased to be a subsidiary of the Company. The Second Amended Complaint asserts that prior to the sale of Lake River Corporation, the Company directly operated the Lake River facility and, accordingly, seeks to have the Court pierce the corporate veil of Lake River Corporation and enforce the default judgment order of August 12, 2004 against the Company. The Company denies the assertions set forth in the Water District's Complaint and on November 13, 2004 filed a partial motion for dismissal of the Second Amended Complaint.

In December 2004, the Water District filed a Third Amended complaint in the litigation, adding two claims: (1) a common law claim for nuisance; and (2) a claim under the federal Resource Conservation and Recovery Act, in which the Water District argues that the Company is responsible for conditions on the plaintiff's property that present an "imminent and substantial endangerment to human health and the environment." In January 2005, the Company filed a partial motion to dismiss the Third Amended Complaint. On April 12, 2005, the Court issued an order denying in part and granting in part the Company's partial motion to dismiss plaintiff's third amended complaint. The Company has filed an appeal with the Seventh Circuit Court of Appeals requesting dismissal of the sole CERCLA claim contained in the Third Amended Complaint that was not dismissed by the United States District Court's April 12, 2005 order. The Water District has also attempted to appeal those rulings contained in the April 12, 2005 that are adverse to the Water District. Meanwhile, litigation in the United States District Court continues.

The Company has denied any liability with respect to this claim and intends to vigorously defend this case. At this time, the Company has not determined the amount of any liability that may result from this matter or whether such liability, if any, would have a material adverse effect on the Company's financial condition, results of operations, or liquidity.

NAG was notified in 1997 by the Illinois Environmental Protection Agency ("IEPA") that it was one of approximately 60 potentially responsible parties ("PRPs") under the Comprehensive Environmental Response, Compensation, and Liability Information System ("CERCLIS") in connection with cleanup of an abandoned site formerly owned by Sandoval Zinc Co. A number of the PRPs have agreed to work together and with IEPA on a voluntary basis. The Company has been and continues to participate in this volunteer group. The group has retained consultants and legal representatives familiar with IEPA regulations. This volunteer group, with its consultants, has cooperated with IEPA in attempting to better define the environmental issues associated with the Sandoval Zinc site. To that extent, this voluntary group prepared and submitted to IEPA in August 2000 a work plan. The purpose of this work plan is to attempt to define the extent of environmental remediation that might be required, assess risks, and review alternatives to addressing potential remediation. The IEPA has yet to respond to this proposed work plan or suggest any other course of action, and there has been no activity in regards to this issue during 2006. Therefore, the Company has no basis for determining potential exposure and estimated remediation costs at this time.

The Company is committed to complying with all federal, state and local environmental laws and regulations and using its best management practices to anticipate and satisfy future requirements. As is typical in the galvanizing business, the Company will have additional environmental compliance costs associated with past, present and future operations. Management is committed to discovering and eliminating environmental issues as they arise. Because of frequent changes in environmental technology, laws and regulations management cannot reasonably quantify the Company's potential future costs in this area.

North American Galvanizing & Coatings, Inc. and its subsidiary are parties to a number of other lawsuits and environmental matters which are not discussed herein. Management of the Company, based upon their analysis of known facts and circumstances and reports from legal counsel, does not believe that any such matter will have a material adverse effect on the results of operations, financial conditions or cash flows of the Company.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's operations include managing market risks related to changes in interest rates and zinc commodity prices.

INTEREST RATE RISK. The Company is exposed to financial market risk related to changes in interest rates. Changing interest rates will affect interest paid on the Company's variable rate debt. At March 31, 2006, the Company's outstanding debt of $14,888,000, consisted of the following: Variable rate debt aggregating $8,172,000 under the bank credit agreement, with an effective rate of 8.0%; variable rate debt of $5,699,000 under the industrial revenue bond agreement, with an effective rate of 3.5%; and, fixed rate debt consisting of $1,000,000 face value of 10% subordinated promissory notes and a 9.5% term note of $17,000. The borrowings under all of the Company's debt obligations at March 31, 2006 are due as follows: $1,091,000 in 2006; $2,483,000 in 2007; $7,730,000 in 2008 and $3,584,000 in years 2009 through 2013. Each increase of 10 basis points in the effective interest rate would result in an annual increase in interest charges on variable rate debt of approximately $13,900 based on March 31, 2006 outstanding borrowings. The actual effect of changes in interest rates is dependent on actual amounts outstanding under the various loan agreements. The Company monitors interest rates and has sufficient flexibility to renegotiate the loan agreement, without penalty, in the event market conditions and interest rates change.

ZINC PRICE RISK. NAG periodically enters into fixed price purchase commitments with domestic and foreign zinc producers to purchase a portion of its zinc requirements for its hot dip galvanizing operations. Commitments for the future delivery of zinc, typically up to one (1) year, reflect rates quoted on the

London Metals Exchange. At March 31, 2006, the aggregate fixed price commitments for the procurement of zinc were approximately $1.6 million (Note 6). With respect to these zinc fixed price purchase commitments, a hypothetical decrease of 10% in the market price of zinc from the March 31, 2006 level represented a potential lost gross margin opportunity of approximately $160,000.

The Company's financial strategy includes evaluating the selective use of derivative financial instruments to manage zinc and interest costs. As part of its inventory management strategy, the Company recognizes that hedging instruments may be effective in minimizing the impact of zinc price fluctuations. The Company's current zinc forward purchase commitments are considered derivatives, but the Company has elected to account for these purchase commitments as normal purchases.

ITEM 4. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, management, including our chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures. Based upon, and as of the date of, the evaluation, our chief executive officer and chief financial officer concluded that the disclosure controls and procedures were effective, in all material respects, to ensure that information required to be disclosed in the reports we file and submit under the Exchange Act is recorded, processed, summarized and reported as and when required.

The Company's certifying officers have indicated that there were no significant changes in internal controls over financial reporting that have occurred during the fiscal quarter ended March 31, 2006 that materially affected, or were reasonably likely to materially affect, internal controls over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

On August 30, 2004, the Company was informed by counsel for the Metropolitan Water Reclamation District of Greater Chicago (the "Water District") that the Water District had, on August 25, 2004 filed a Second Amended Complaint in the United States District Court, Northern District of Illinois, Eastern Division, naming North American Galvanizing & Coatings, Inc. (formerly known as Kinark Corporation) as an added defendant. Counsel for the Water District also gave the Company notice of the Water District's intent to file (or amend the Complaint to include) a Citizens Suit under the Resource Compensation and Recovery Act ("RCRA") against North American Galvanizing & Coatings, Inc., pursuant to Section 7002 of RCRA, 42 U.S.C. Section 6972. This Second Amended Complaint seeks enforcement of an August 12, 2004 default judgment in the amount of $1,810,463.34 against Lake River Corporation and Lake River Holding Company, Inc. in connection with the operation of a storage terminal by Lake River Corporation in violation of environmental laws. Lake River Corporation conducted business as a subsidiary of the Company until June 30, 2000, at which time Lake River Corporation was sold to Lake River Holding Company, Inc. and ceased to be a subsidiary of the Company. The Second Amended Complaint asserts that prior to the sale of Lake River Corporation, the Company directly operated the Lake River facility and, accordingly, seeks to have the Court pierce the corporate veil of Lake River Corporation and enforce the default judgment order of August 12, 2004 against the Company. The Company denies the assertions set forth in the Water District's Complaint and on November 13, 2004 filed a partial motion for dismissal of the Second Amended Complaint.

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North American Galvanizing & Coatings, Inc. and its subsidiary are parties to a number of other lawsuits and environmental matters which are not discussed herein. Management of the Company, based upon their analysis of known facts and circumstances and reports from legal counsel, does not believe that any such matter will have a material adverse effect on the results of operations, financial conditions or cash flows of the Company.

ITEM 1A. RISK FACTORS.

There are no material changes from risk factors as previously disclosed in the Company's Annual Report on Form 10-K filed on February 10, 2006.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS - NOT APPLICABLE.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES - NOT APPLICABLE.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS - NOT APPLICABLE.

ITEM 5. OTHER INFORMATION - NOT APPLICABLE.

ITEM 6. EXHIBITS.

(a) Exhibits

3.1 The Company's Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.1 to the Company's Pre-Effective Amendment No. 1 to Registration Statement on Form S-3 (Reg. No. 333-4937) filed on June 7, 1996).

3.2 The Company's Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q dated March 31, 1996).

10.5 Director Stock Unit Program.

10.6	2004 Incentive Stock Plan
31.1	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of of 2002.
32	Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99	Cautionary Statements by the Company Related to Forward-Looking Statements.

SIGNATURES

Pursuant to the requirements of Section 13 and 15(d) of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized:

NORTH AMERICAN GALVANIZING & COATINGS, INC.
(Registrant)

By: /s/ Beth B. Hood

Vice President and
Chief Financial Officer
(Principal Financial Officer)

Date: April 27, 2006

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