ADA-ES INC
Form 10KSB/A
July 26, 2006

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB/A
Amendment #1

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

For the fiscal year ended December 31, 2005

Commission File Number: 000-50216

ADA-ES, Inc.
(Name of small business issuer in its charter)

Colorado	84-1457385
(State of incorporation)	(IRS Employer Identification No.)

8100 SouthPark Way, Unit B, Littleton, Colorado 80120-4525
(Address of principal executive offices, including Zip Code)

(Issuer's telephone number, including area code): (303) 734-1727

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

Title of class
Common Stock, no par value

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

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

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. [X]

State issuer's revenues for its most recent fiscal year. $ 11,028,000

State the aggregate market value of the voting and non-voting common equity held by nonaffiliates computed by reference to the price at which the common equity was sold, or the average bid and asked prices of such common equity, as of a specified date within the past 60 days. As of March 24, 2006 was $129,654,000.

Number of shares outstanding of registrant's Common Stock, no par value as of March 24, 2006 - 5,620,040.

DOCUMENTS INCORPORATED BY REFERENCE:
None

Transitional Small Business Disclosure Format: Yes __ No X

PART II

Item 7. Financial Statements.

Our Financial Statements can be found at pages F-1 through F-20 of this report.

Item 8A. Controls and Procedures.

Disclosure Controls and Procedures

We maintain disclosure controls and procedures designed to ensure that the information required to be disclosed by us in the reports we file with the Securities and Exchange Commission (SEC), is recorded, processed, summarized and disclosed within the time periods specified in the rules of the SEC. Based on their evaluation of our disclosure controls and procedures which took place as of December 31, 2005, the end of the period covered by this report, the Chief Executive and Financial Officers believe that these controls and procedures are effective to ensure that (i) we are able to record, process, summarize and disclose the information we are required to disclose in the reports we file with the SEC within the required time periods and (ii) information required to be disclosed by us in such reports is accumulated and communicated to our management, including our principal executive and financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosures.

Internal Control Over Financial Reporting

The Company also maintains a system of internal controls designed to provide reasonable assurance that: transactions are executed in accordance with management's general or specific authorization; transactions are recorded as necessary (1) to permit preparation of financial statements in conformity with generally accepted accounting principles, and (2) to maintain accountability for assets; access to assets is permitted only in accordance with management's general or specific authorization; and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

During the fourth fiscal quarter of 2005, there have been no significant changes in our controls over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, those controls.

Item 13. Exhibits

(a) Exhibits and Index of Exhibits

No.	Description
Index to Exhibits.	
3.1	Amended and Restated Articles of Incorporation of ADA-ES (1)
3.2	Amended and Restated Bylaws of ADA-ES (2)
4.1	Form of Specimen Common Stock Certificate (3)
4.2	Registration Rights Agreement dated October 21, 2005 (4)
4.3	Registration Rights Agreement between ADA-ES, Inc. and Arch Coal, Inc. dated March 19, 2003 (16)

No.	Description
4.4	Standstill and Registration Rights Agreements dated August 3-6, 2004 (6)
10.1	Distribution Agreement dated as of March 17, 2003 between Earth Sciences, Inc. and ADA-ES, Inc. (7)
10.2	2003 ADA-ES, Inc. Stock Option Plan** (16)
10.3	Market Development Agreement between NORIT Americas Inc. and Earth Sciences, Inc. dated June 29, 2001 (5)
10.4	Assignment and Assumption Agreement between NORIT Americas Inc., Earth Sciences, Inc. and ADA-Environmental Solutions LLC dated August 4, 2003 (8)
10.5	Joint Venture and Co-Marketing Agreement by and between Arch Coal Sales Company and ADA- Environmental Solutions LLC as of January 1, 2002 (5)
10.6	Securities Subscription and Investment Agreement between ADA-ES, Inc. and Arch Coal, Inc. dated July 7, 2003 (7)
10.7	U.S. Department of Energy Cooperative Agreement No. DE-FC26-00NT41004 "Field Test Program to Develop Comprehensive Design, Operating, and Cost Data for Mercury Control Systems" (7)
10.8	U.S. Department of Energy Cooperative Agreement No. DE-FC26-00NT40755 "Advanced Flue Gas Conditioning as a Retrofit Upgrade to Enhance PM collection from Coal-Fired Electric Utility Boilers" (7)
10.9	Joint Product Exploitation and Marketing Agreement dated October 2, 2002, by and between ALSTOM Power Inc. and ADA Environmental Solutions LLC (5)
10.10	Tax Sharing Agreement between ADA-ES, Inc. and Earth Sciences, Inc. dated March 17, 2003 (5)
10.11	U.S. Department of Energy Cooperative Agreement No. DE-FC26-02NT41591 "Long-Term Operation of a COHPAC System for Removing Mercury from Coal-Fired Flue Gas" (7)
10.12	Amendment No. 1 to Distribution Agreement by and between ADA-ES, Inc. and Earth Sciences, Inc. dated August 15, 2003 (8)
10.13	2003 Stock Compensation Plan #1** (9)
10.14	2003 Stock Compensation Plan #2** (10)
10.15	U.S. Department of Energy Cooperative Agreement No. DE-FC26-03NT41986 "Evaluation of Sorbent Injection for Mercury Control" (11)
10.16	Purchase Order #4500589101 signed 3/18/04 from We Energies (12)
10.17	Clean Coal Power Initiative Repayment Agreement between the U.S. Department of Energy and ADA-ES, Inc. dated April 6, 2004 (12)
10.18	TOXECON Sorbent Sales Repayment Agreement by and between Norit America Inc. and ADA-ES, Inc. dated February 18, 2004 (12)
10.19	Development and Field Validation Agreement between Thermo

	Environmental Instruments Inc. and ADA-ES, Inc. dated April 16, 2004 (12)
10.20	Distribution Agreement between Thermo Environmental Instruments Inc. and ADA-ES, Inc. dated April 16, 2004 (12)
10.21	ADA-ES, Inc. 2004 Executive Stock Option Plan** (13)
10.22	U.S. Department of Energy Cooperative Agreement No. DE-FC26-05NT42307 "Low-Cost Options for Moderate Levels of Mercury Control" (14)
10.23	Employment Agreement dated May 1, 1997 between C. Jean Bustard and ADA Environmental Solutions, LLC (assigned to ADA-ES, Inc.) ** (14)
10.24	Employment Agreement dated May 1, 1997 between Michael D. Durham and ADA Environmental Solutions, LLC (assigned to ADA-ES, Inc.) ** (14)
10.25	Employment Agreement dated January 2, 2000 between Mark H. McKinnies and ADA Environmental Solutions, LLC (assigned to ADA-ES, Inc.) ** (14)
10.26	Employment Agreement dated January 1, 2000 between Richard J. Schlager and ADA Environmental Solutions, LLC (assigned to ADA-ES, Inc.) ** (14)
10.27	2004 Stock Compensation Plan #2 and model stock option agreements** (13)
10.28	2004 Directors Stock Compensation Plan #1** (15)
10.29	2005 Directors' Compensation Plan**(16)
21.1	Subsidiaries of ADA-ES, Inc. (5)
23.1*	Consent of Hein & Associates LLP
31.1*	Certification of Chief Executive Officer of ADA-ES, Inc. Pursuant to 17 CFR 240.13a-14(a) or 17 CFR 240.15d-14(a)

No.	Description
31.2*	Certification of Chief Financial Officer of ADA-ES, Inc. Pursuant to 17 CFR 240.13a-14(a) or 17 CFR 240.15d-14(a)
32.1*	Certifications Pursuant to 17 CFR 240.13a-14(b) or 17CFR 240.15d-14(b) and18 U.S.C. Section 1350

(*) - filed herewith.
(**) - Management contract or compensatory plan or arrangement.
(1) Incorporated by reference to Exhibit 3.1 to the Form 10-QSB for the quarter ended September 30, 2005 filed on November 10, 2005 (File No. 000-50216).
(2) Incorporated by reference to Exhibit 3.2 to the Form 8-K dated December 1, 2005 filed on December 5, 2005 (File No. 000-50216).
(3) Incorporated by reference to Exhibit 4.1 to the Form 8-K dated October 21, 2005 filed on October 26, 2005 (File No. 000-50216).
(4) Incorporated by reference to Exhibit 10.1 to the Form 8-K dated October 21, 2005 filed on October 26, 2005 (File No. 000-50216).
(5) Intentionally omitted.
(6) Incorporated by reference to Exhibit A to Exhibit 10.1 to the Form S-3 filed on October 18, 2004 (File No. 333-119795).
(7) Incorporated by reference to the same numbered Exhibit to the Form 10-SB/A-3 filed on July 28, 2003 (File No. 000-50216).
(8) Incorporated by reference to the same numbered Exhibit to the Form 10-SB/A-4 filed on August 24, 2003 (File No. 000-50216).
(9) Incorporated by reference to Exhibit 99.2 to the Form S-8 filed on November 14, 2003 (File No. 333-110479).
(10) Incorporated by reference to Exhibit 99.1 to the Form S-8 filed on February 6, 2004 (File No. 333-112587).
(11) Incorporated by reference to the same numbered Exhibit to the Form 10-KSB for the year ended December 31, 2003 filed on March 30, 2004 (File No. 000-50216).
(12) Incorporated by reference to the same numbered Exhibit to the Form 10-QSB for the quarter ended March 31, 2004 filed on May 13, 2004 (File No. 000-50216).

(13) Incorporated by reference to Exhibit 99.3 to the Form S-8 filed on December 14, 2004 (File No. 333-121234).
(14) Incorporated by reference to the same numbered Exhibit to the Form 10-KSB for the year ended December 31, 2004 filed on March 30, 2005 (File No. 000-50216).
(15) Incorporated by reference to Exhibit 99.1 to the Form S-8 filed on April 16, 2004 (File No. 333-114546).
(16) Incorporated by referenced to the same numbered Exhibit to the Form 10-KSB for the year ended December 31,2005 filed on March 30, 2006.

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ADA-ES, Inc.

(Registrant)

By /s/ Mark H. McKinnies	/s/ Michael D. Durham
Mark H. McKinnies, Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	Michael D. Durham President (Chief Executive Officer)
Date: July 25, 2006	July 25, 2006

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

/s/ John W. Eaves	/s/ Rollie J. Peterson
John W. Eaves, Director Director	Rollie J. Peterson Director
July 25, 2006 Date	July 25, 2006 Date
/s/ Jeffrey C. Smith	/s/ Michael D. Durham
Jeffrey C. Smith, Director	Michael D. Durham, Director
July 25, 2006 Date	July 25, 2006 Date
/s/ Mark H. McKinnies	/s/ Ronald B. Johnson
Mark H. McKinnies, Director	Ronald B. Johnson, Director
July 25, 2006 Date	July 25, 2006 Date

ADA-ES, INC. AND SUBSIDIARY
Consolidated Financial Statements
For the Years Ended
December 31, 2005 and 2004

INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
ADA-ES, Inc. and Subsidiary
Littleton, Colorado

We have audited the accompanying consolidated balance sheet of ADA-ES, Inc. and Subsidiary as of December 31, 2005, and the related consolidated statements of income, changes in stockholders' equity and cash flows for the years ended December 31, 2005 and 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of ADA-ES, Inc. and Subsidiary as of December 31, 2005, and the results of their operations and their cash flows for the years ended December 31, 2005 and 2004 in conformity with U.S. generally accepted accounting principles.

HEIN & ASSOCIATES LLP

Denver, Colorado
February 13, 2006

ADA-ES, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEET
DECEMBER 31, 2005

ASSETS

CURRENT ASSETS:	
Cash and cash equivalents	$ 14,026,000
Trade receivables, net of allowance for doubtful accounts of $4,000	3,014,000
Investments in securities	2,515,000
Prepaid expenses and other	283,000
Total current assets	19,838,000
PROPERTY AND EQUIPMENT, at cost	1,663,000
Less accumulated depreciation and amortization	(1,013,000)
Net property and equipment	650,000
GOODWILL, net of $1,556,000 in amortization	2,024,000
INTANGIBLE ASSETS, net of $44,000 in amortization	156,000
INVESTMENTS IN SECURITIES	5,663,000
OTHER ASSETS	385,000
TOTAL ASSETS	$ 28,716,000

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:	
Accounts payable	$ 1,706,000
Accrued payroll and related liabilities	516,000
Accrued expenses	138,000
Deferred revenue and other	460,000
Total current liabilities	2,820,000
LONG-TERM LIABILITIES:	
Deferred compensation and other	40,000
Total liabilities	2,860,000
COMMITMENTS AND CONTINGENCIES (Notes 4 and 6)	
STOCKHOLDERS' EQUITY:	
Preferred stock; 50,000,000 shares authorized, none outstanding	--
Common stock; no par value, 50,000,000 shares authorized, 5,610,267 shares issued and outstanding	26,318,000
Accumulated other comprehensive income	33,000
Accumulated deficit	(495,000)
Total stockholders' equity	25,856,000
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 28,716,000

See accompanying notes to these consolidated financial statements.

ADA-ES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

	FOR THE YEARS ENDE DECEMBER 31,	
	2005	
REVENUE:		
Mercury emission control	$ 8,784,000	$ 5
Flue gas conditioning	1,917,000	2
Combustion aids and others	327,000	
Total net revenues	11,028,000	8
COST OF REVENUES		
Mercury emission control	5,722,000	3
Flue gas conditioning	796,000	
Combustion aids and others	223,000	
Total cost of services	6,741,000	5
GROSS MARGIN	4,287,000	3
OTHER COSTS AND EXPENSES:		
General and administrative	2,502,000	2
Research and development	977,000	
Depreciation and amortization	157,000	
Total expenses	3,636,000	3
OPERATING INCOME	651,000	
OTHER INCOME (EXPENSE):		
Interest and other expense	(9,000)	
Interest and other income	357,000	
Total other income	348,000	
INCOME BEFORE INCOME TAX PROVISION	999,000	
DEFERRED INCOME TAX PROVISION	(336,000)	
NET INCOME	663,000	
UNREALIZED GAINS AND (LOSSES) ON CERTAIN INVESTMENTS IN DEBT AND EQUITY SECURITIES, net of tax	(1,000)	
COMPREHENSIVE INCOME	$ 662,000	$

NET INCOME PER COMMON SHARE - BASIC AND DILUTED	$ .13	$
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	4,966,000	4
WEIGHTED AVERAGE DILUTED COMMON SHARES OUTSTANDING	5,137,000	4

See accompanying notes to these consolidated financial statements.

ADA-ES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' E
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

	COMMON STOCK		ACCUMULATED OTHER COMPREHENSI
	SHARES	AMOUNT	INCOME
BALANCES, January 1, 2004	3,582,230	$ 4,467,000	$ --
Stock issued to employees and directors for expenses	25,716	181,000	--
Issuance of stock for cash, net	1,000,000	7,620,000	--
Issuance of stock on exercise of options	173,265	435,000	--
Issuance of stock on conversion of debt	14,500	36,000	--
Tax benefit of stock transactions	--	395,000	--
Unrealized gains on investments	--	--	34,0
Net income	--	--	--
BALANCES, December 31, 2004	4,795,711	13,134,000	34,0
Stock and stock options issued to consultant and directors for expenses	4,221	75,000	--
Issuance of stock for cash, net	789,089	12,538,000	--
Issuance of stock on exercise of options	40,976	303,000	--
Tax benefit of stock transactions	--	268,000	--
Return of shares from escrow	(19,730)	--	--
Unrealized loss on investments	--	--	(1,0
Net income	--	--	--
BALANCES, December 31, 2005	5,610,267	$ 26,318,000	$ 33,0

See accompanying notes to these consolidated financial

ADA-ES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEA

	DECEMBER
	2005
CASH FLOWS FROM OPERATING ACTIVITIES:	
Net income	$ 663,000
Adjustments to reconcile net income to net cash provided by Operating activities:	
Depreciation and amortization	157,000
Loss on asset dispositions and securities	104,000
Write off of inventory	28,000
Expenses paid with stock and stock options	75,000
Deferred tax expense	336,000
Changes in operating assets and liabilities:	
(Increase) decrease in:	
Receivables	(1,816,000)
Prepaid expenses and other	(103,000)
Increase (decrease) in:	
Accounts payable	1,273,000
Accrued expenses	222,000
Deferred revenue and other	270,000
Net cash provided by operating activities	1,209,000
CASH FLOWS FROM INVESTING ACTIVITIES:	
Capital expenditures for equipment and patents	(374,000)
Investment in securities	(10,753,000)
Proceeds from asset dispositions	--
Proceeds from sale of securities	8,999,000
Net cash used in investing activities	(2,128,000)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Payments on debt and notes payable	(4,000)
Exercise of stock options	303,000
Sale of stock	12,538,000
Net cash provided by financing activities	12,837,000
INCREASE IN CASH AND CASH EQUIVALENTS	11,918,000
CASH AND CASH EQUIVALENTS, beginning of year	2,108,000
CASH AND CASH EQUIVALENTS, end of year	$ 14,026,000
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION:	
Cash payments for interest	$ 2,000
SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:	
Transfer of inventory to property	$ --
Tax effect of stock option exercises	$ 268,000
Stock issued in conversion of debt	$ --

See accompanying notes to these consolidated financial statements

ADA-ES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES:

Nature of Operations - The accompanying consolidated financial statements include the accounts of ADA-ES, Inc. (ADA) and its wholly-owned subsidiary, ADA Environment Solutions, LLC (ADA LLC). ADA's only asset is its investment in its wholly-owned subsidiary, ADA LLC. All significant intercompany transactions have been eliminated. Collectively, ADA and ADA LLC are referred to as the Company.

The Company is principally engaged in providing environmental technologies and specialty chemicals to the coal-burning utility industry. The Company also generates substantial revenue from contracts co-funded by the government and industry. The Company's sales occur principally throughout the United States.

Cash Equivalents - The Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. The Company maintains the majority of its cash in deposit accounts collateralized by U.S. Treasury Securities. The amount on deposit at December 31, 2005 was held in one commercial bank and was in excess of the insurance limits of the Federal Deposit Insurance Corporation.

Receivables and Credit Policies - Trade receivables are uncollateralized customer obligations due under normal trade terms requiring payment within 30 days from the invoice date. Management reviews trade receivables periodically and reduces the carrying amount by a valuation allowance that reflects management's best estimate of the amount that may not be collectible.

Investments- Investments in securities include certificates of deposit and debt securities. All investments in debt securities are classified as available-for-sale securities, and are recorded at fair value in investments in securities, with the change in fair value during the period excluded from earnings and recorded net of tax as a component of other comprehensive income.

Premiums and discounts on investments in debt securities are amortized over the contractual lives of those securities. During the first half of 2005, the Company transferred debt securities totaling approximately $5,532,000 to available-for-sale from the held-to-maturity category because of the trading activity initiated by the debt security managers. The transfer resulted in an increase to other comprehensive income of $20,000. All of the Company's investments in debt and marketable equity securities are classified as available-for-sale at December 31, 2005, as they are held for an indefinite period. Unrealized holding losses on such securities, net of tax, which were reported in other comprehensive income for 2005 were $1,000.

Inventories - Inventories, which are included in prepaid expenses and other, are stated at the lower of cost or market, determined by the first-in, first-out method and consist of supplies.

ADA-ES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Revenue Recognition - ADA follows the percentage of completion method of accounting for all significant contracts excluding government contracts and chemical sales. The percentage of completion method of reporting income takes into account the estimated costs to complete and estimated gross margin for contracts in progress. The Company recognizes revenue on government contracts based on the time and expenses incurred to date. As of December 31, 2005, costs incurred in excess of billings totaled $142,000 and are included in prepaid expenses and other in the accompanying Balance Sheet. Billings in excess of recognized income totaled $135,000 as of December 31, 2005 and are included in deferred revenue and other in the accompanying Balance Sheet.

ADA chemical sales are recognized when products are shipped to customers. A reserve is established for any returns, based on historical trends. Chemical products are shipped FOB shipping point and title passes to the customer when the chemicals are shipped. The Company's sales agreements do not contain a right of inspection or acceptance provision and products are generally received by customers within one day of shipment. The Company has had no significant history of non-acceptance, nor of replacing goods damaged or lost in transit. Consulting revenue is recognized as services are performed and collection is assured.

Property and Equipment - Property and equipment is stated at cost. Depreciation on assets is provided using the straight-line method based on estimated useful lives ranging from 3 to 10 years. Maintenance and repairs are charged to operations as incurred. When assets are retired, or otherwise disposed of, the property accounts are relieved of costs and accumulated depreciation and any resulting gain or loss is credited or charged to income.

Intangible Assets - Intangible assets principally consist of patents. Patents obtained by the Company directly are being amortized over a 17-year life. Amortization of intangible assets for the years ended December 31, 2005 and 2004 was $11,000 and $10,000, respectively. Based on the balance of intangible assets as of December 31, 2005, the Company anticipates amortization expense over the next 5 years to be approximately $11,000 per year.

Intangible assets consist of:

	Cost	Accumulated Amortization	Net
Patents	$ 200,000	$ 44,000	$ 156,000

ADA-ES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Goodwill - Goodwill consists of the excess of the aggregate purchase price over the fair value of net assets of businesses acquired. Goodwill was amortized over a 10-year period through December 31, 2001 and is attributable to the Company's FGC reporting segment. As of January 1, 2002, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets. Under SFAS No. 142, goodwill is no longer amortized, but subject to an impairment evaluation, which is performed in the fourth quarter of each year. As a result of this evaluation, which was performed on the FGC reporting segment, the Company concluded that no impairment of its goodwill was required.

Operating Costs - Operating costs include all labor, fringe benefits, subcontract labor, chemical costs, materials, equipment, supplies and travel costs directly related to the Company's production of revenue.

General and Administrative - General and administrative costs include personnel related fringe benefits, sales and administrative staff labor costs, facility costs and other general costs of conducting business.

Net Income Per Share - Net income per share is presented in accordance with the provisions of SFAS No. 128, Earnings Per Share. Basic EPS is calculated by dividing the income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted EPS is calculated using the same numerator as basic EPS and further reflects the potential dilution that could occur if outstanding stock options were exercised. The effect of such dilutive stock options added 171,000 and 67,000 shares in 2005 and 2004, respectively, to the weighted average number of common shares outstanding used in calculation of diluted EPS.

Impairment of Long-Lived Assets - The Company follows SFAS No. 144, Impairment of Long-Lived Assets. In the event that facts and circumstances indicate that the carrying value of assets or intangible assets may be impaired, an evaluation of recoverability would be performed. Based on the Company's evaluation as of December 31, 2005, no impairment of value existed.

Fair Value of Financial Instruments - The carrying amounts of financial instruments, including cash, cash equivalents, accounts receivable, accounts payable and accrued liabilities approximates fair value due to the short maturity of these instruments. The fair values of investments are estimated based on quoted market prices for those investments.

Income Taxes - The Company accounts for income taxes under the liability method of SFAS No. 109, whereby current and deferred tax assets and liabilities are determined based on tax rates and laws enacted as of the balance sheet date. A valuation allowance is provided when deferred tax assets are not expected to be realized.

Research and Development Costs - Research and development costs are charged to operations in the period incurred.

Stock-Based Compensation - The Company records expense for stock options granted to employees by using APB 25, which requires expense to be recognized only to the extent the exercise price of the stock-based compensation is below the market price on the date of grant. Transactions in equity instruments with non-employees for goods or services are

ADA-ES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

accounted for on the fair value method. Because the Company has elected not to adopt the fair value accounting described in SFAS No. 123 for employees, it is subject only to the disclosure requirements described in SFAS No. 123.

Had compensation cost been determined based on an estimate of the fair value consistent with the method of SFAS No. 123 at the grant dates for awards under those plans, the Company's net income and EPS would have been reduced to the pro forma amounts indicated below.

	Years Ended December 31, 2005	2004
Net income (loss):		
As reported	$ 663,000	$ 336,000
Fair value of stock based compensation, net of tax	(147,000)	(48,000)
Pro forma	$ 516,000	$ 288,000
Net income (loss) per share - basic and diluted:		
As reported	$ .13	$ .08
Fair value of stock based compensation	(.03)	(.01)
Pro forma - basic and diluted	$ .10	$ .07

The options granted in 2004 and 2005 had exercise prices equal to the market price on the date of the grants. Prior to the third quarter of 2005, the Company showed expense related to stock options in the period of grant. The presentation above, including 2004 amounts, shows expense amortized over the estimated service period, as required under SFAS 123. The average fair value of each employee option granted in 2005 and 2004 was approximately $2.18 and $1.38, respectively, and was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Years Ended December 31, 2005	2004
Expected volatility	41%	35%
Risk-free interest rate	2.6%	2.5%
Expected life of options (in years)	4.8	4.4
Expected dividends	0	0

Use of Estimates - The preparation of the Company's consolidated financial statements in conformity with generally accepted accounting principles requires the Company's management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying

ADA-ES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

notes. Actual results could differ from those estimates. The Company makes significant assumptions concerning: 1) the impairment of and the remaining realizability of its intangibles; 2) estimates of certain overhead and other rates on research contracts with the U.S. Government, which are subject to future audits. At this time, the Company does not believe any future government audit will result in material adjustment to previously recorded revenues; 3) the allowance for doubtful accounts, which is based on historical experience; 4) the valuation and classification of investments in available-for-sale securities, which is based on estimated fair market value; and 5) the percentage of completion method of accounting for significant long-term contracts, which is based on estimates of gross margins and of the costs to complete such contracts.

Comprehensive Income - SFAS No. 130 establishes standards for reporting and display of comprehensive income, its components and accumulated balances. Comprehensive income is defined to include all changes in equity except those resulting from investments by owners and distributions to owners. In 2005 and 2004, comprehensive income includes unrealized gains (losses) on investments, net of income tax expense, of ($1,000) and $34,000, respectively.

Segment Information - The Company follows SFAS No. 131, Disclosure About Segments of an Enterprise and Related Information. SFAS No. 131 establishes standards on the way that public companies report financial information about operating segments in annual financial statements and requires reporting of selected information about operating segments in interim financial statements issued to the public. It also establishes standards for disclosures regarding products and services, geographic areas, and major customers. SFAS No. 131 defines operating segments as components of a company about which discrete financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Company has three reportable segments: mercury emission controls (MEC), flue gas conditioning and consulting (FGC), and combustion aids and consulting (CA).

Recently Issued Accounting Pronouncements - In December 2004, the FASB issued SFAS No. 123R, Share-Based Payment. This Statement is a revision of SFAS No. 123, Accounting for Stock-Based Compensation. This Statement supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS No. 123R establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services, or incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments. SFAS No. 123R focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions and requires the Company to measure and recognize costs of share-based payment transactions in the financial statements. The Company must implement SFAS No. 123R as of the beginning of the first quarter of 2006. The Company is evaluating the impact of SFAS No. 123R on its financial statements and believes the impact will be similar to proforma amounts disclosed above.

In November 2005, the FASB issued Staff Position ("FSP") FAS115-1/124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments , which addresses the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. This FSP also

includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The guidance in this FSP amends FASB Statements No. 115, Accounting for Certain Investments in Debt and Equity Securities , and No. 124, Accounting for Certain Investments Held by Not-for-Profit Organizations , and APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock . This FSP is effective for reporting periods beginning after December 15, 2005. Adoption of this FSP is not expected to have a material impact on the Company's financial statements.

In April 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections, requiring retrospective application as the required method for reporting a change in accounting principle, unless impracticable or a pronouncement includes specific transition provisions. This statement also requires that a change in depreciation, amortization, or depletion method for long-lived, non-financial assets be accounted for as a change in accounting estimate effected by a change in accounting principle. This statement carries forward the guidance in APB Opinion No. 20, Accounting Changes, for the reporting of the correction of an error and a change in accounting estimate. This statement is effective for accounting changes and correction of errors made in fiscal years beginning after December 15, 2005 and is not expected to have a material impact on the Company's financial statements.

2. PROPERTY AND EQUIPMENT:

Property and equipment as of December 31, 2005 is summarized as follows:

		Estimated Useful Lives
Machinery and equipment	$ 1,375,000	3-10
Leasehold improvements	210,000	7
Furniture and fixtures	78,000	5
	$ 1,663,000	

Depreciation and amortization of property and equipment for the years ended December 31, 2005 and 2004 was $146,000 and $143,000, respectively.

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3. INVESTMENTS:

Investments in available-for-sale securities are reported at their fair value in investments in securities and are summarized as follows at December 31, 2005: Gross Gross Unrealized Fair Unrealized Gain Loss Value

Certificates of deposit	$ --	$ --	$ 1,200,000
Common stock	$ 142,000	$ (18,000)	$ 1,444,000
Debt securities	$ 4,000	$ (76,000)	$ 5,534,000
Total	$ 146,000	$ (94,000)	$ 8,178,000
Less short-term portion			$(2,515,000)
Long-term portion			$ 5,663,000

Realized gains and losses are determined on the basis of specific identification of the security sold. During 2005, information on securities sold is as follows:

Carrying amount of securities sold	$ 9,031,000
Sale proceeds	$ 8,999,000
Gross realized losses	$ (60,000)
Gross realized gains	$ 28,000

Accumulated other comprehensive income for 2005 and 2004 includes an unrealized holding gain, net of tax, on securities of $33,000 and $34,000, respectively.

Debt securities will mature as follows:

Year(s)	Amount
2006	$ 271,000
2007-2010	1,706,000
2011-2015	2,934,000
Beyond 2015	623,000
Total	$ 5,534,000

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4. GOVERNMENT AND INDUSTRY FUNDED CONTRACTS:

ADA has performed activities under five contracts awarded by the Department of Energy (the "DOE") that contributed a total of $2,348,000 and $2,387,000 to revenues in 2005 and 2004, respectively. These amounts are included in Mercury emission control revenues. ADA typically invoices the DOE monthly for labor and expenditures plus estimated overhead factors, less cost share amounts. The total approved DOE budgets amount to $23.2 million, of which the Company's and industry partners' cost-share portion is $7.4 million. The remaining unearned amount of the contracts was $5.4 million as of December 31, 2005, of which $3.3 million is expected to be recognized by the Company in 2006 (including cash contributions by other industry partners). These contracts are subject to audit and future appropriation of funds by Congress. The Company's historical experience has not resulted in significant adverse adjustments to the Company, however the government audits for years ended 2005, 2004, 2003 and 2002 have not yet been finalized.

5. STOCKHOLDERS' EQUITY:

Shares and Stock Options Issued for Pension Expenses and Directors' and Consultant Compensation - In 2004 the Company issued shares of its common stock for the payments of approximately $146,000 of ADA pension related expenses (see Note 6) and $35,000 of non-management directors' compensation, based upon the per share value of unrestricted common stock of ADA at the time of exchanges. In 2005, the Company issued shares of its common stock for compensation of $58,000 to non-management directors based on the market price of the common stock, and recorded $17,000 of expense related to stock options issued to a consultant.

Sale of Stock, Convertible Debenture and Grant of Option to Arch - In 2003, the Company sold 137,741 shares to Arch Coal for $1 million and sold a convertible debenture for $300,000, both pursuant to an investment agreement. Of the shares sold, 37,741 were originally placed in escrow of which 19,730 shares were returned to the Company during 2005 since the market price of the Company's shares exceeded a minimum of $9.08 for a twenty-day continuous period during the one-year period from the date of their issuance. The Debenture was repaid during 2004. As a part of the share purchase Arch was also granted an option to purchase 50,000 shares for $10.00 per share. The option expires in five years. Under the option, Arch may purchase 16,667 shares after August 2004, another 16,667 shares after August 2005, and the remaining shares after August 2006.

Sale of Stock in 2005 and 2004 - In August 2004 and October 2005, the Company entered into several Subscription and Investment Agreements. Under the August 2004 agreements, the Company privately sold 1 million shares of its common stock to a limited number of institutional investors at a price of $8.00 per share. The net proceeds to the Company from the sales totaled $7,620,000. Under the October 2005 agreements, the Company privately sold 789,089 shares of its common stock to a limited number of institutional investors at a price of $17.00 per share. Net proceeds to the Company totaled $12,538,000.

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Stock Options - During 2003 the Company adopted the 2002 ADA-ES, Inc. Stock Option Plan and reserved 400,000 shares of common stock for issuance under the plan. In general, all options granted under the plan expire ten years from the date of grant unless otherwise specified by the Company's board of directors. The exercise price of an option will be determined by the compensation committee of the board of directors at the time the option is granted and will not be less than 100% of the fair market value of a share of our common stock on the date the option is granted. The compensation committee may provide in the option agreement that an option may be exercised in whole immediately or is exercisable in increments through a vesting schedule. During 2005, 61,900 options were granted under this plan.

During 2004 the Company adopted the 2004 Executive Stock Option Plan. This plan authorized the grant of up to 200,000 options to purchase shares of the Company's Common Stock to executive officers of the Company. The option exercise price of grants under this plan is the market price on the date of the grant. The options are exercisable over a 10-year period based on a vesting schedule that may be accelerated based on performance of the individual recipients as determined by the Board of Directors. During 2004, 200,000 options were granted under this plan. In January 2005 and 2006 the Board of Directors authorized the vesting of 27,080 options and 38,428 options, respectively, under this plan.

During 2004 the Company adopted a plan (the "2004 Plan") for the issuance of shares and the grant of options to purchase shares of the Company's Common Stock to the Company's non-management directors. The 2004 Plan provided for the award of stock of 603 shares per individual non-management director or 4,221 shares in total, and the grant of options of 5,000 per individual non-management director or 35,000 in total, all of which were formally granted and issued in 2005 after approval of the 2004 Plan by the stockholders. The option exercise price of $13.80 per share for the stock options granted on November 4, 2004 was the market price on the date of the grant. The options are exercisable over a period of five years and will vest over a three-year period, one-third each year for continued service on the Board. If such service is terminated, the non-vested portion of the option will be forfeited.

During 2005 the Company adopted the 2005 Directors' Compensation Plan (the "2005 Plan"), which authorized the issuance of shares of Common Stock and the grant of options to purchase shares of the Company's Common Stock to non-management directors. The 2005 Plan provides a portion of the annual compensation to non-management directors of the Company in the form of awards of shares of Common Stock and vesting of options to purchase Common Stock of the Company for services performed for the Company. Under the 2005 Plan, the award of stock is limited to not more than 1,000 shares per individual per year, and the grant of options is limited to 5,000 per individual in total. The aggregate number of shares of Common Stock reserved for issuance under the 2005 Plan totals 90,000 shares (50,000 in the form of stock awards and 40,000 in the form of options). The exercise price will be the market price on the date of grant, the shares of Stock

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underlying the option will vest for exercise at a rate of no more than 1,667 shares per annual period per individual, and any unvested shares of Stock that are outstanding at the date the individual is no longer is a Director will be forfeited. The 2005 Plan, if not terminated earlier by the Board, will terminate ten years after the date of its adoption. In January 2006 the Board of Directors authorized the issuance of 1,000 shares of Common Stock each, or a total of 7,000 shares, to the non-management directors of the Company.

The Company granted options to employees in 2004 and to employees and a consultant in 2005 as additional compensation. The following is a table of options activity during 2004 and 2005:

	Employees Options	Non-Employee Options	Weighted Average Exercise Price
OPTIONS OUTSTANDING, January 1, 2004	187,310	80,000	3.94
Options granted	275,995	--	9.32
Options expired	(7,800)	--	2.80
Options exercised	(157,765)	(30,000)	2.51
OPTIONS OUTSTANDING, December 31, 2004	297,740	50,000	$ 9.01
Options granted	96,900	30,000	15.29
Options expired	(2,181)	--	13.80
Options exercised	(40,976)	--	7.39
OPTIONS OUTSTANDING, December 31, 2005	351,483	80,000	$ 10.99

The weighted average remaining contractual life for all options as of December 31, 2005 was approximately 8.3 years. At December 31, 2005, 107,722 options with a weighted average exercise price of $9.90 were fully vested and exercisable. Of the remaining 323,761 options, 103,877 options with a weighted average exercise price of $12.68 vest in 2006, 42,617 options with a weighted average exercise price of $15.74 vest in 2007, 150,267 options with an exercise price of $8.60 vest at the discretion of the board of directors based on specific achievements of individual employees, with minimum annual vesting of 10,000 and maximum vesting of 20,000. Additionally, 27,000 options with an exercise price of $14.60 vest at the discretion of the board of directors upon achievement of performance objectives.

Following is information related to options outstanding at December 31, 2005:

Range	Shares Outstanding	Weighted Average Exercise Price	Weighted Average Contractual Life (in years)	Number Exercisabl

$2.80	13,425	$ 2.80	7.8	13,425
$8.60 - $10.00	254,960	$ 8.87	8.5	59,218
$13.80 - $18.61	163,098	$14.96	8.1	35,079
	431,483	$10.99	8.3	107,722

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6. COMMITMENTS AND CONTINGENCIES:

Pension Expense and Retirement Plan - The Company assumed a defined contribution and 401(k) plan covering all eligible employees as of January 1, 2003. The Company recognized contribution expense of $206,000 and $161,000 for 2005 and 2004, respectively, based on a percentage of the eligible employees' annual compensation.

Performance Guarantee Activated Carbon Injection Systems - Under contracts to supply activated carbon injection systems, the Company may grant performance guarantees to the owner of the power plants that guarantee the performance of the associated equipment for a specified period and the achievement of a certain level of mercury removal based upon the injection of a specified quantity of activated carbon at a specified rate given other plant operating conditions. In the event the equipment fails to perform as specified, the Company is obligated to correct or replace the equipment. In the event the level of mercury removal is not achieved, the Company has a "make right" obligation within the contract limits.

Office Lease - The Company leases office space under a non-cancellable operating lease. Total rental expense was $153,000 and $158,000 for the years ending December 31, 2005 and 2004, respectively. The total minimum rental commitments at December 31, 2005 was $494,000 for lease payments due in 2006 through 2009 as follows:

Year	Amount
2006	$ 119,000
2007	122,000
2008	125,000
2009	128,000
	$ 494,000

7. MAJOR CUSTOMERS:

Sales to unaffiliated customers which represent 10% or more of the Company's sales for the years ended December 31, 2005 and 2004 were as follows (as a percentage of each entity's sales):

Customer	2005	2004
A (Governmental Contracts)	21%	28%
B	11%	10%
C	13%	-

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At December 31, 2005, approximately 89% of the Company's trade receivables were from five customers.

A significant portion of ADA's revenue is derived from contracts with the DOE and chemical and equipment sales to coal-burning electric power plants.

8. INCOME TAXES:

The following lists the Company's deferred tax assets and liabilities as of December 31, 2005, which are included in Other Assets and Accrued Expenses, respectively, in the accompany Balance Sheet:

Current assets (liabilities):	
Prepaid expenses	$ (39,000)
Unrealized gains - securities held for sale	(19,000)
Deferred revenues, compensation and other	30,000
	(28,000)
Non-current assets (liabilities)	
Deferred compensation, warranty and other	9,000
Property and intangible asset differences	(60,000)
Net loss carryforward	318,000
Tax credits	101,000
	368,000
Net tax assets	$ 340,000

As of December 31, 2005, the Company had approximately $857,000 of tax loss carryforwards. If not utilized to reduce taxable income in future periods, $40,000 will expire in 2023 and the remainder in 2024. Approximately $69,000 of tax loss carryforwards were used to reduce taxable income in 2005. The Company's valuation allowance as of December 31, 2005 and 2004 was $0, as the Company believes that it is more likely than not that its deferred tax assets would be realized in the future.

At December 31, 2005 and 2004, the Company's current tax provision was reduced by $268,000 and $395,000, respectively, attributable to the tax effects of stock option exercises recorded in stockholders' equity.

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The following is a reconciliation of the actual income tax rate - expense (benefit) to the expected combined Federal and State tax rate of approximately 34%:

	2005	2004
Expected income tax rate - expense (benefit)	35%	34%
Permanent differences	(4%)	(4%)
Tax credits	(1%)	(17%)
State income taxes	3%	3%
Other	1%	-
Actual income tax rate	34%	16%

9. RELATED PARTY TRANSACTIONS:

As discussed above in Note 5, the Company executed a Securities Subscription and Investment Agreement with Arch Coal, Inc. in 2003. Pursuant to the investment agreement, Arch purchased a $300,000 convertible debenture from the Company, purchased 137,741 shares of the Company's Common stock and was also granted an option to purchase 50,000 shares. The debenture and accrued interest thereon was repaid in 2004. In addition, the Company co-markets its ADA-249 product and performs certain testing and research projects under agreements with Arch. Under such arrangements, the Company has recorded revenue of $230,000 and $25,000 in 2005 and 2004, respectively. A designee of Arch has been appointed a seat on the Company's Board of Directors and management of the Company has agreed in the future to nominate and to vote all proxies and other shares of stock in the Company which they are entitled to vote in favor of that designee so long as Arch holds no less than 100,000 shares of the Company's common stock.

10. BUSINESS SEGMENT INFORMATION:

The following information relates to the Company's three reportable segments: MEC, FGC, and CA. All assets are located in the U.S. and are not evaluated by management on a segment basis. All significant customers are U.S. companies.

Year Ended December 31, 2005:

	MEC	FGC	CA	Total
Total revenue	$8,784,000	$1,917,000	$327,000	$11,028,000
Segment profit (loss)	$1,738,000	$957,000	$53,000	$2,748,000

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Year Ended December 31, 2004:

	MEC	FGC	CA	Total
Total revenue	$5,940,000	$2,122,000	$355,000	$8,417,000
Segment profit (loss)	$996,000	$964,000	$34,000	$1,994,000

A reconciliation of the reported total segment profit to net income for the periods shown above is as follows:

	2005	200
Total segment profit	$ 2,748,000	$1,994
Non-allocated general and administrative expenses	(1,940,000)	(1,458
Depreciation and amortization	(157,000)	(153
Interest, other income/expenses and tax (provision) benefit	12,000	(47
Net income	$ 663,000	$ 336

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