VERAMARK TECHNOLOGIES INC
Form 10-Q
August 13, 2007

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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 Quarter Ended June 30, 2007
Commission File Number 0-13898
Veramark Technologies, Inc.
(Exact name of registrant as specified in its charter)

Delaware	16-1192368
(State or other jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

3750 Monroe Avenue, Pittsford, NY 14534
(Address of principal executive offices)(Zip Code)
(585) 381-6000
(Registrant s telephone number, including area code)
N/A
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not 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-K or any amendment to this Form 10-K. o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer o Non-accelerated filer þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

YES o NO þ

The number of shares of Common Stock, $.10 par value, outstanding as of June 30, 2007 was 8,967,071.

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VERAMARK TECHNOLOGIES, INC.
CONDENSED BALANCE SHEETS

	(Unaudited) June 30, 2007	December 31, 2006
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 600,443	$ 845,384
Investments	1,575,675	849,655
Accounts receivable, trade (net of allowance for doubtful accounts of $35,000 and $30,000, respectively)	1,291,351	1,443,685
Inventories, net	29,845	32,898
Prepaid expenses and other current assets	285,409	262,133
Total Current Assets	3,782,723	3,433,755
PROPERTY AND EQUIPMENT		
Cost	5,894,188	5,904,647
Less accumulated depreciation	(5,310,529)	(5,235,398)
Property and Equipment (Net)	583,659	669,249
OTHER ASSETS:		
Software development costs (net of accumulated amortization of $1,691,497 and $1,246,121, respectively)	3,254,856	3,175,385
Pension assets	2,937,455	2,866,470
Deposits and other assets	830,756	788,534
Total Other Assets	7,023,067	6,830,389
TOTAL ASSETS	$ 11,389,449	$ 10,933,393

The accompanying notes are an integral part of these financial statements.

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VERAMARK TECHNOLOGIES, INC.
CONDENSED BALANCE SHEETS

	(Unaudited) June 30, 2007	December 31, 2006
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 231,370	$ 317,158
Accrued compensation and related taxes	824,148	680,930
Deferred revenue	3,395,637	3,317,119
Current portion of pension obligation	313,134	195,767
Other accrued liabilities	292,201	323,222
Total Current Liabilities	5,056,490	4,834,196
Pension obligation	5,169,397	5,096,031
Total Liabilities	10,225,887	9,930,227
STOCKHOLDERS EQUITY:		
Common Stock, par value $.10; shares authorized, 40,000,000; shares issued and outstanding, 9,047,296 and 8,935,026	904,730	893,503
Additional paid-in capital	22,045,774	21,724,250
Accumulated deficit	(21,104,368)	(20,901,736)
Treasury stock (80,225 shares, at cost)	(385,757)	(385,757)
Accumulated other comprehensive income	(296,817)	(327,094)
Total Stockholders Equity	1,163,562	1,003,166
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 11,389,449	$ 10,933,393

The accompanying notes are an integral part of these financial statements.

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VERAMARK TECHNOLOGIES, INC.
CONDENSED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
NET SALES				
Product sales	$ 828,542	$ 829,043	$ 1,565,016	$ 1,568,687
Service sales	2,219,541	1,777,238	4,831,709	3,481,790
Total Net Sales	3,048,083	2,606,281	6,396,725	5,050,477
COSTS AND OPERATING EXPENSES:				
Cost of sales	749,835	574,093	1,737,779	1,098,432
Engineering and software development	296,500	198,301	547,447	351,010
Selling, general and administrative	2,334,527	2,048,755	4,339,018	3,881,394
Total Costs and Operating Expenses	3,380,862	2,821,149	6,624,244	5,330,836
LOSS FROM OPERATIONS	(332,779)	(214,868)	(227,519)	(280,359)
NET INTEREST INCOME	12,635	7,816	24,887	15,830
LOSS BEFORE INCOME TAXES	(320,144)	(207,052)	(202,632)	(264,529)
INCOME TAXES				
NET LOSS	$ (320,144)	$ (207,052)	$ (202,632)	$ (264,529)
NET LOSS PER SHARE				
Basic	$ (0.03)	$ (0.02)	$ (0.02)	$ (0.03)
Diluted	$ (0.03)	$ (0.02)	$ (0.02)	$ (0.03)

The accompanying notes are an integral part of these financial statements.

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VERAMARK TECHNOLOGIES, INC.
CONDENSED STATEMENTS OF CASH FLOWS (Unaudited)

	Six Months Ended June 30, 2007	2006
OPERATING ACTIVITIES:		
Net loss	$ (202,632)	$ (264,529)
Adjustments to reconcile net loss to net cash flows provided by operating activities		
Depreciation and amortization	571,403	630,749
Expense of bad debts	4,470	(1,506)
Compensation expense-stock options	282,000	18,700
Increase in cash surrender value of company-owned life insurance Policies	(70,985)	(72,446)
Realized loss on sale of investments		(1,356)
Changes in assets and liabilities		
Accounts receivable	147,864	346,106
Inventories	3,053	(18,145)
Prepaid expenses and other current assets	(23,276)	(70,496)
Deposits and other assets	(42,222)	8,211
Accounts payable	(85,788)	(88,386)
Accrued compensation and related taxes	143,218	(20,498)
Deferred revenue	78,518	176,617
Other accrued liabilities	(31,021)	(3,106)
Pension obligation	222,133	246,933
Net cash flows provided by operating activities	996,735	886,848
INVESTING ACTIVITIES:		
Purchase of investments	(727,143)	(114,626)
Capitalized software development costs	(524,847)	(689,486)
Additions to property and equipment	(40,437)	(78,031)
Net cash flows used by investing activities:	(1,292,427)	(882,143)
FINANCING ACTIVITY:		
Exercise of stock options	43,710	932
Proceeds from employee stock purchase plan	7,041	4,706
Net cash flows provided by financing activities	50,751	5,638
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(244,941)	10,343
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	845,384	911,310
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 600,443	$ 921,653

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	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash Transactions:		
Income taxes paid, net	$ 1,859	$ 4,500
Interest paid	$ 575	$ 144

The accompanying notes are an integral part of these financial statements.

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NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)
(1) GENERAL

The accompanying unaudited financial statements include all adjustments of a normal and recurring nature which, in the opinion of Company s management, are necessary to present fairly the Company s financial position as of June 30, 2007, the results of its operations for the three and six months ended June 30, 2007 and 2006, and cash flows for the six months ended June 30, 2007 and 2006.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission. These condensed financial statements should be read in conjunction with the financial statements and related notes contained in the Company s annual report on Form 10-K to the Securities and Exchange Commission for the year ended December 31, 2006.

The results of operations and cash flows for the three and six months ended June 30, 2007 are not necessarily indicative of the results to be expected for the full year s operation.

(2) PROPERTY AND EQUIPMENT

The major classifications of property and equipment at June 30, 2007, and December 31, 2006 were:

	June 30, 2007	**December 31, 2006**
Machinery and equipment	$ 795,905	$ 795,905
Computer hardware and software	2,039,273	2,057,099
Furniture and fixtures	1,670,659	1,669,084
Leasehold improvements	1,388,351	1,382,559
	$ 5,894,188	$ 5,904,647

For the three and six months ended June 30, 2007, the Company recorded depreciation expense of $63,150 and $126,027. Depreciation expense for the three and six months ended June 30, 2006 was $66,530 and $133,724.

(3) STOCK-BASED COMPENSATION

The Company s primary type of share-based compensation consists of stock options. For the quarter ended June 30, 2007 the company issued 432,485 stock options, 400,000 of which vest immediately. The remaining 32,485 stock options vest one year from the date of grant. There were no stock options granted in the first quarter of 2007.

A summary of the status of the Company s stock option plan as of June 30, 2007 is presented below:

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	Shares	Average Exercise Price	Average Grant-Date Fair Value	Remaining Contractual Term (Yrs)	Intrinsic Value
Outstanding as of December 31, 2006	2,790,278	$ 2.35	$ 1.92	3.3	$ 1,157,625
Granted	432,485	0.78			
Exercised	(101,650)	0.43			(8,132)
Canceled	(619,600)	2.79			(303,551)
Outstanding as of June 30, 2007	2,501,513	$ 2.05	$ 1.69	4.6	$ 845,942
Options exercisable at June 30, 2007	2,439,678	$ 2.08	$ 1.71	4.5	$ 842,381

As of June 30, 2007, there was $23,162 of total unrecognized compensation cost related to non-vested share-based compensation arrangements related to stock options granted under the Plan. That cost is expected to be recognized over a weighted-average period of 0.6 years.

(4) TOTAL COMPREHENSIVE INCOME (LOSS)

Total comprehensive income (loss) for the three and six months ended June 30, 2007 and 2006 was as follows:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Net loss	$ (320,144)	$ (207,052)	$ (202,632)	$ (264,529)
Amortization of Prior Services	31,400		31,400	
Unrealized loss on investments	(6,496)	(4,232)	(1,123)	(6,357)
Total Comprehensive Loss	$ (295,240)	$ (211,284)	$ (172,355)	$ (270,886)

(5) NET INCOME (LOSS) PER SHARE (EPS)

SFAS 128 Earnings Per Share requires the Company to calculate net income (loss) per share based on basic and diluted net income (loss) per share, as defined. Basic EPS excludes dilution and is computed by dividing net income (loss) by the weighted average number of shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. The dilutive effect of outstanding options issued by the Company are reflected in diluted EPS using the treasury stock method. Under the treasury stock method, options will only have a dilutive effect when the average market price of common stock during the period exceeds the exercise price of the options.

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Calculations of Earnings (Loss) Per Share

	Three Months Ended June 30, 2007	Three Months Ended June 30, 2006	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Basic				
Net Loss	$ (320,144)	$ (207,052)	$ (202,632)	$ (264,529)
Weighted average common shares outstanding	8,940,855	8,839,452	8,897,994	8,838,913
Net loss per common share	$ (0.03)	$ (0.02)	$ (0.02)	$ (0.03)
Diluted				
Net loss	$ (320,144)	$ (207,052)	$ (202,632)	$ (264,529)
Weighted average common shares outstanding	8,940,855	8,839,452	8,897,994	8,838,913
Additional dilutive effect of stock options and warrants after application of treasury stock method				
Weighted average dilutive shares outstanding	8,940,855	8,839,452	8,897,994	8,838,913
Net loss per common share assuming full obligation	$ (0.03)	$ (0.02)	$ (0.02)	$ (0.03)

There were no dilutive effects of stock options for the three and six months ended June 30, 2007 and 2006, as the effect would have been anti-dilutive due to the net losses incurred.

(6) INDEMNIFICATION OF CUSTOMERS

Our agreements with customers generally require us to indemnify the customer against claims that our software infringes third party patent, copyright, trademark or other proprietary rights. Such indemnification obligations are generally limited in a variety of industry-standard respects, including our right to replace an infringing product. As of June 30, 2007 we had not experienced any material losses related to these indemnification obligations and no material claims with respect thereto were outstanding. We do not expect significant claims related to these indemnification obligations, and consequently, we have not established any related reserves.

(7) BENEFIT PLANS

The Company sponsors an employee incentive savings plan under Section 401(k) for all eligible employees. The Company s contributions to the plan are discretionary. There were no contributions to the plan for the three and six months ended June 30, 2007 and 2006.

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The Company also sponsors an unfunded Supplemental Executive Retirement Program (SERP), which is a non-qualified plan that provides certain key employees defined pension benefits. Periodic pension expense for the three and six months ended June 30, 2007 and 2006 consists of the following:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2007	**2006**	**2007**	**2006**
Current Service Cost	$ 68,180	$ 69,503	$ 136,360	$ 139,006
Amortization of Prior Service Cost	15,700	22,123	31,400	44,246
Interest Cost	78,720	73,374	157,440	146,748
Pension Expense	$ 162,600	$ 165,000	$ 325,200	$ 330,000

The Company paid pension obligations of $103,067 for the six months ended June 30, 2007 and $83,067 for the six months ended June 30, 2006.

The discount rate used in determining the actuarial present value of the projected benefit obligation was 6% for the three and six months ended June 30, 2007 and 2006.

The Company maintains life insurance covering certain key employees under its Supplemental Executive Retirement Program with the Company named as beneficiary. The Company intends to use the death benefits of these policies, as well as loans against the accumulating cash surrender value of the policies, to fund future pension obligations. The total death benefit associated with these policies is $10.2 million, with an associated accumulated cash surrender value of approximately $2,937,000 at June 30, 2007. The accumulated cash surrender values of these policies at December 31, 2006 was approximately $2,866,000.

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

Results of Operations

Management s Discussion and Analysis contains statements that are forward-looking. Such statements are identified by the use of words like plans, expects, intends, believes, will, anticipates, estimates and other w similar meaning in conjunction with, among other things, discussions of future operations, financial performance, the Company s strategy for growth, product development, regulatory approvals, market position and expenditures. Forward-looking statements are based on management s expectations as of the date of this report. The Company cannot guarantee that any forward-looking statement will be accurate, although the Company believes that it has been reasonable in its expectations and assumptions. Forward-looking statements are subject to the risks identified in Issues and Risks and elsewhere in this report. Readers are cautioned not to place undue reliance on forward-looking statements and are advised to review the risks identified in Issues and Risks and elsewhere in this report. The Company has no obligation to update forward-looking statements.

Overview

Sales of $3,048,000 for the three months ended June 30, 2007 increased 17% from sales of $2,606,000 for the three months ended June 30, 2006. For the six months ended June 30, 2007 sales of $6,397,000 increased 27% from sales of $5,050,000 for the first six months of 2006. The increase in sales for both periods was attributable to a growth in revenues generated from Managed Service contracts, in addition to increased sales of VeraSMART products and services.

The net loss incurred for the three months ended June 30, 2007 was $320,000 or $0.03 per share, which compares with a net loss of $207,000, or $0.02 per share for the same three month period of 2006. For the six months ended June 30, 2007 the net loss of $203,000, or $0.02 per share compares with a net loss of $265,000, or $0.03 per share, for the six months ended June 30, 2006.

Results for the second quarter and year were impacted by the grant of 432,485 stock options to selected long-term employees. In accordance with SFAS 123, Share-based Payments which requires the expensing of stock options, $279,000 of compensation expense was recorded during the second quarter. During the first six months of 2007 a total of 619,600 previously granted stock options either expired without being exercised, or were terminated. As of June 30, 2007 there are 2,501,513 stock options outstanding as compared with 2,760,878 stock options outstanding as of June 30, 2006. Results for the six months ended June 30, 2007 as compared with the prior year were also impacted by lower capitalization of software development costs, and an increase in cost of sales attributable to fees paid a third party contractor to fulfill portions of our managed service contract with Sears Holding Corporation.

Orders for the three months ended June 30, 2007 increased 11% from the same quarter of 2006 and increased 2% for the six months ended June 30, 2007 as compared to the six months ended June 30, 2006.

During the second quarter we announced the release of VeraSMART 6.0, the latest in a series of enhancements to our VeraSMART Communications Management suite. Key features of this new release include enhanced invoice processing, payment tracking, contract management capabilities, and new reporting functionality. VeraSMART 6.0 integrates with accounts payable and general ledger systems allowing for automatic invoice alerts, the measurement of invoiced charges against contractual commitments, and compares actual usage against wireless plans.

Cash and investments at June 30, 2007 totaled $2,176,000, an increase of 14%, or $266,000 from the March 31, 2007 total of $1,910,000.

Sales

Sales of VeraSMART products and services increased 130% and 76% respectively, for the three and six months ended June 30, 2007 as compared with the same three and six month periods of 2006. New client installations of VeraSMART completed during the second quarter included Kimberly Clark, Connecticut De