

Edgar Filing: DATA SYSTEMS & SOFTWARE INC - Form 10-Q/A

DATA SYSTEMS & SOFTWARE INC

Form 10-Q/A

November 17, 2004

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

AMENDMENT No. 1 on FORM 10-Q/A
To FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF
THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2004

COMMISSION FILE NUMBER 0-19771

DATA SYSTEMS & SOFTWARE INC.
(Exact name of registrant as specified in charter)

DELAWARE
(State or other jurisdiction of
incorporation or organization)

22-2786081
(I.R.S. employer
identification no.)

200 ROUTE 17, MAHWAH, NEW JERSEY
(Address of principal executive offices)

07430
(Zip code)

(201) 529-2026
Registrant's telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (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

☐ No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

☐ Yes

☒ No

Number of shares outstanding of the registrant's common
stock, as of November 12, 2004: 8,116,691

Explanatory Note

This Amendment No. 1 to the registrant's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2004 is being filed to (i) correct the number of outstanding shares of the registrant's common stock reflected on the cover page of the report and (ii) correct a typographical error in the column headings on the consolidated balance sheets included in Item 1. Unaudited Consolidated Financial Statements of Part I. Financial Information.

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PART I - Financial Information

Item 1. Unaudited Consolidated Financial Statements

DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS (in thousands, except share and per share data)

	As of December 31, 2003	As Septem 200
ASSETS	-----	-----
Current assets:		(unaud
Cash and cash equivalents	\$ 1,213	\$
Restricted cash	241	
Accounts receivable, net	7,053	6,
Inventory	88	
Other current assets	661	
	-----	-----
Total current assets	9,256	8,
	-----	-----
Investment in Comverge, net	68	
Property and equipment, net	814	
Other assets	613	
Funds in respect of employee termination benefits	2,379	2,
Goodwill	4,430	4,
Other intangible assets, net	114	
	-----	-----
Total assets	\$ 17,674	\$ 16,
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term bank credit and current maturities of long-term debt	\$ 1,517	\$ 1,
Trade accounts payable	2,586	2,
Accrued payroll, payroll taxes and social benefits	1,451	1,
Other current liabilities	2,973	2,
	-----	-----
Total current liabilities	8,527	7,
	-----	-----
Investment in Comverge, net	--	1,
	-----	-----
Long-term liabilities:		
Long-term debt	632	
Other liabilities	227	
Liability for employee termination benefits	3,721	4,
	-----	-----
Total long-term liabilities	4,580	4,
	-----	-----

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Minority interests	1,367	1,
	-----	-----
Shareholders' equity:		
Common stock - \$0.01 par value per share:		
Authorized - 20,000,000 shares;		
Issued - 8,740,729 and 8,842,395 shares as of		
December 31, 2003 and September 30, 2004, respectively	87	
Additional paid-in capital	39,595	39,
Warrants	461	
Stock-based deferred compensation	--	
Accumulated deficit	(33,069)	(33,
Treasury stock, at cost - 838,704 and 820,704		
shares at December 31, 2003 and		
September 30, 2004, respectively	(3,874)	(3,
Accumulated other comprehensive loss	--	(
	-----	-----
Total shareholders' equity	3,200	2,
	-----	-----
Total liabilities and shareholders' equity	\$ 17,674	\$ 16,
	=====	=====

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

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS (UNAUDITED) (in thousands, except net loss per share data)

	Nine months ended September 30,		Three Sep
	2003	2004	2003
	-----	-----	-----
Sales:			
Products	\$ 16,900	\$ 13,157	\$ 3,779
Services	7,306	6,831	2,327
Projects	2,459	2,049	564
	-----	-----	-----
Total sales	26,665	22,037	6,670
	-----	-----	-----
Cost of sales:			
Products	13,951	10,801	3,202
Services	5,082	5,049	1,665
Projects	2,087	1,655	601
	-----	-----	-----
Total cost of sales	21,120	17,505	5,468
	-----	-----	-----
Gross profit	5,545	4,532	1,202
	-----	-----	-----
Operating expenses:			
Research and development	153	--	--
Selling, marketing, general and administrative	8,345	5,496	1,982
	-----	-----	-----
Total operating expenses	8,498	5,496	1,982
	-----	-----	-----

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Operating loss	(2,953)	(964)	(780)
Interest income	42	79	15
Interest expense	(714)	(125)	(68)
Other income (expense), net	(408)	239	(243)
	-----	-----	-----
Loss before taxes on income	(4,033)	(771)	(1,076)
Taxes on income	7	17	(27)
	-----	-----	-----
Loss from operations of the Company and its consolidated subsidiaries	(4,040)	(788)	(1,049)
Share of losses in Comverge	(1,161)	(1,066)	(611)
Gain on sale of shares in Comverge	--	705	--
Minority interests	139	(59)	35
	-----	-----	-----
Net loss from continuing operations	(5,062)	(1,208)	(1,625)
Net income (loss) from discontinued operations, net of tax	(38)	348	(4)
	-----	-----	-----
Net loss	(5,100)	(860)	(1,629)
	-----	-----	-----
Differences from translation of financial statements of subsidiaries	--	(159)	--
	-----	-----	-----
Comprehensive loss	\$ (5,100)	\$ (1,019)	\$ (1,629)
	=====	=====	=====
Basic and diluted net income (loss) per share:			
Loss per share from continuing operations	\$ (0.66)	\$ (0.15)	\$ (0.21)
Discontinued operations	(0.00)	0.04	(0.00)
	-----	-----	-----
Basic and diluted net loss per share	\$ (0.66)	\$ (0.11)	\$ (0.21)
	=====	=====	=====
Weighted average number of shares outstanding:			
Basic and diluted	7,680	7,927	7,894
	=====	=====	=====

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

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED) NINE MONTHS ENDED SEPTEMBER 30, 2004 (in thousands)

	Number of Shares	Common Stock	Additional Paid-In Capital	Warrants	Stock-Based Deferred Compensation	Accumulated Deficit	Tre St
	-----	-----	-----	-----	-----	-----	-----
Balances as of							
December 31, 2003	8,741	\$ 87	\$ 39,595	\$ 461	\$ --	\$ (33,069)	\$ (
Exercise of							
options	1	*	(48)	--	--	--	--

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Shares issued as compensation	100	1	70	--	--	--	
Changes related to stock-based deferred compensation	--	--	68	--	(68)	--	
Amortization of stock-based deferred compensation	--	--	--	--	4	--	
Net loss	--	--	--	--	--	(860)	
Differences from translation of subsidiaries' financial statements	--	--	--	--	--	--	
Balances as of September 30, 2004	8,842	\$ 88	\$ 39,685	\$ 461	\$ (64)	\$ (33,929)	\$ (1,000)
	=====	=====	=====	=====	=====	=====	=====

* Less than \$1

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

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) (dollars in thousands)

	Nine months ended September 30, 2005	Nine months ended September 30, 2004
Cash flows used in operating activities:		
Net loss	\$ (5,100)	\$ (8,600)
Adjustments to reconcile net loss to net cash provided by operating activities - Schedule A:	4,900	(1,000)
Net cash used in operating activities	(1,000)	(9,600)
Cash flows provided by (used in) investing activities:		
Restricted cash	4,200	(1,000)
Proceeds from sale of property and equipment	(1,000)	(2,000)
Proceeds from sale of Converge shares	(3,500)	(2,000)
Acquisitions of property and equipment	(2,000)	(3,500)
Funding of termination benefits	(2,000)	(3,500)
Business disposition - see Schedule B	2,000	(3,500)
Net cash provided by investing activities	2,000	(10,000)

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Cash flows provided by (used in) financing activities:

Short-term debt, net	(5)
Borrowings of long-term debt	4
Repayments of long-term debt	(4)
Investment in subsidiary by minority interest	
Exercise of options	
Purchase of treasury stock	
Net cash used in financing activities	(5)
Net decrease in cash and cash equivalents	(4)
Cash and cash equivalents at beginning of period	1,1
Cash and cash equivalents at end of period	\$ 7
Supplemental cash flow information:	
Cash paid during period for interest	\$ 3
Cash paid during period for income taxes	\$ 1
Non-cash investing and financing activities:	
Issuance of common stock in lieu of debt repayment	\$ 8
Increase in investment in Comverge from issuance of common stock credited to additional paid in capital	\$ 1,0

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

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) (dollars in thousands)

Nine m

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Schedule A:

Adjustments to reconcile net loss to net cash (used in) provided by operating activities:

Depreciation and amortization.....	
Stock and stock-based compensation.....	
Accretion of discount on convertible note and amortization of related costs and warrants.....	
Minority interests.....	
Share of losses in Comverge.....	
Loss on write-off of stockholder's note.....	
Increase in liability for employee termination benefits.....	
Exchange adjustment on long-term debt.....	
Loss (gain) on disposition of property and equipment.....	
Gain on sale of Comverge shares.....	
Change in deferred taxes.....	
Change in operating assets and liabilities:	
Decrease in accounts receivable and other assets.....	

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Increase in inventory.....	(2)
Decrease in accounts payable and other liabilities.....	-----
Total.....	\$
	=====

Schedule B:

Assets and liabilities disposed of in disposition of Comverge:

Current assets.....	\$4
Property, equipment and other assets.....	1
Goodwill	
Intangibles.....	
Short-term debt.....	(3,
Current liabilities.....	(2,
Other liabilities.....	(
Cash investment in Comverge.....	(3,

	\$ (3,
	=====

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

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (dollars in thousands)

NOTE 1: BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Data Systems & Software Inc. ("DSSI") and subsidiaries (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete consolidated financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the nine-month period ended September 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2003. Certain reclassifications have been made to the Company's prior period's consolidated financial statements to conform to the current period's consolidated financial statement presentation.

NOTE 2: FINANCING OF OPERATIONS

As of September 30, 2004, the Company had working capital of \$1,149, including \$896 in non-restricted cash and cash equivalents. Net cash used in the nine months of 2004 was \$317. Net cash of \$542 was used in operating activities during the first three quarters of 2004. The net loss for the nine-month period ended September 30, 2004 of \$860, was due primarily to the net loss from the Company's investment in Comverge of \$361 and expenses incurred in the unsuccessful transaction with Kardan Communications Ltd. of \$342. The Company's use of cash in operating activities during the first nine months of 2004 was

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primarily for payment of accounts payable and other liabilities in excess of collections of trade accounts receivables of \$676, net. Net cash of \$671 provided by investing activities, was primarily from the net proceeds of \$975 from the sale by the Company of preferred shares of its Comverge equity investment, less amounts used to fund employee termination benefits in the Company's majority-owned dsIT subsidiary of \$257. Net cash of \$446 used in financing activities was primarily for payment of debt of \$481.

Approximately \$287 of the total working capital at September 30, 2004, was in dsIT. Due to Israeli tax and company law constraints, as well as the significant minority interest in dsIT, such working capital and cash flows from dsIT's operations are not readily available to finance U.S. activities.

dsIT was utilizing approximately \$859 of its \$1,100 lines of credit as of September 30, 2004. dsIT's lines of credit are denominated in NIS and bear an average interest rate of the Israeli prime rate plus 1.4% per annum. The Israeli prime rate fluctuates and as of September 30, 2004 was 5.6%.

The Company intends to fund its US activities with the cash available and anticipated profits from its US operations. The Company is seeking and considering various restructuring, merger or acquisition and/or financing transactions. Should the Company need additional liquidity to finance its US activities and should it be unsuccessful in completing a timely transaction providing the necessary liquidity, it may not have sufficient funds to finance its US activities. In such event, the Company might need to sell additional Comverge shares.

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (in thousands, except per share data)

Note 3: Investment in Comverge

Comverge's summary results of operations for the three and nine month periods ended September 30, 2004 are as follows:

	Nine months ended September 30, 2004	Three months ended September 30, 2004
Results of Operations	-----	-----
Sales	\$12,375	\$ 3,774
Gross profit	\$ 5,057	\$ 1,534
Net loss	\$(6,947)	\$(2,707)

The change in the Company's Comverge investment, during the nine months ended September 30, 2004 is as follows:

	Comverge common stock -----	Comverge preferred stock -----	Net investment in Comverge -----
Balances as of December 31, 2003	\$(1,824)	\$ 1,892	\$ 68
Shares sold	--	(270)	(270)

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Equity loss in Comverge	-- -----	(1,066) -----	(1,066) -----
Balances as of September 30, 2004	\$(1,824) =====	\$ 556 =====	\$(1,268) =====

In September 2004, the Company signed an agreement with certain other shareholders of Comverge's Series A Preferred Stock for the sale by the Company to other shareholders of shares of Comverge Series A Preferred Stock for approximately \$1,000, resulting in a gain of \$705. After giving effect to this transaction, the Company held approximately 11% of Comverge's preferred equity and approximately 34% of its total equity.

In October 2004 Comverge completed the sale of preferred stock to investors. For more detail see Note 9 - Subsequent Event.

Note 4: Goodwill

The entire balance of goodwill was in the software consulting and development segment. There were no acquisitions or impairments of goodwill recorded during the nine-month period ended September 30, 2004.

The Company's amortizable intangible assets consisted of software licenses, with a gross carrying amount of \$253, accumulated amortization of \$163 and \$139 and net balances of \$90 and \$114, as of September 30, 2004 and December 31, 2003, respectively. All intangibles assets are being amortized over their estimated useful lives, which averaged 5 years and the amortization expense for the nine months ended September 30, 2003 and 2004 amounted to \$59 and \$24, respectively.

Note 5: Warranty Provision

The Company grants its customers one-year product warranty. No provision was made in respect of warranties based on the Company's previous history.

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (in thousands, except per share data)

Note 6: Stock-Based Compensation

The Company applies Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees" and the related interpretations in accounting for its stock option grants to employees and directors, with the disclosure provisions of SFAS No. 123, "Accounting for Stock-Based Compensation". Under APB No. 25, compensation expense is computed under the intrinsic value method of accounting to the extent that the fair value of the underlying shares on the date of the grant exceed the exercise price of the share option, and thereafter amortized on a straight-line basis against income over the expected service period.

Had compensation cost for the Company's option plans been determined based on the fair value at the grant dates of awards, consistent with the method

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prescribed in SFAS No. 123, the Company's net loss and loss per share would have been changed to the pro forma amounts indicated below:

	Nine months ended September 30, -----		Three months September -----
	2003 -----	2004 -----	2003 -----
Net loss as reported	\$ (5,100)	\$ (860)	\$ (1,629)
Plus: Stock-based employee and director compensation expense included in reported net loss	55	75	2
Less: Total stock-based employee compensation expense determined under fair value based method for all awards	186	136	2
	-----	-----	-----
Pro forma net loss	\$ (5,231) =====	\$ (921) =====	\$ (1,629) =====
Net loss per share:			
Basic and diluted - as reported	\$ (0.66) =====	\$ (0.11) =====	\$ (0.21) =====
Basic and diluted - pro forma	\$ (0.68) =====	\$ (0.12) =====	\$ (0.21) =====

The pro forma information in the above table also gives effect to the application of SFAS No. 123 on the share option plans of the Company's subsidiaries.

The Company accounts for stock-based compensation issued to non-employees on a fair value basis in accordance with SFAS No. 123 and EITF Issue No. 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services" and related interpretations.

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DATA SYSTEMS & SOFTWARE INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (in thousands except per share data)

Note 7: Segment Information

	Software consulting and development (*) -----	Energy intelligence solutions (**) -----	Computer hardware -----	Ot
Nine months ended September 30, 2004:				
Revenues from external customers	\$ 8,676	\$ --	\$ 13,335	
Intersegment revenues	--	--	--	

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Segment gross profit	2,056	--	2,450
Segment income (loss)	208	(361)	231
Nine months ended September 30, 2003:			
Revenues from external customers	\$ 8,966	\$ 4,700	\$ 12,974
Intersegment revenues	--	284	20
Segment gross profit	1,931	1,313	2,276
Segment loss	(455)	(2,772)	(247)
Three months ended September 30, 2004:			
Revenues from external customers	\$ 2,675	\$ --	\$ 4,806
Intersegment revenues	--	--	--
Segment gross profit	562	--	893
Segment income (loss)	23	323	(60)
Three months ended September 30, 2003:			
Revenues from external customers	\$ 2,813	\$ --	\$ 3,856
Intersegment revenues	--	--	--
Segment gross profit	548	--	653
Segment loss	(24)	(909)	(156)

(*) Excludes the discontinued results of the US-based consulting activities - see Note 8.

(**) Operating results of Converge (in the energy intelligence solutions segment) are no longer consolidated beginning the second quarter of 2003.

(***) Represents the operations of a VAR software operation in Israel that did not meet the quantitative thresholds of SFAS No. 131.

Reconciliation of Segment Loss to Consolidated Net Loss

	Nine months ended September 30,		Three months September
	2003	2004	2003
Total income (loss) for reportable segments	\$ (3,474)	\$ 78	\$ (1,089)
Other operational segment income (loss)	(17)	6	(11)
Total operating income (loss)	(3,491)	84	(1,100)
Net loss of corporate headquarters	(1,571)	(1,292)	(525)
Discontinued operations income (loss)	(38)	348	(4)
Total consolidated net loss	\$ (5,100)	\$ (860)	\$ (1,629)
	=====	=====	=====

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Note 8: Discontinued Operations

Since the latter part of 2003, the Company has not recorded revenues from its US-based consulting business. During the second quarter of 2004, the Company decided to discontinue its efforts to reestablish this business as it was previously conducted. As a result, the Company recorded a gain from discontinued operations of \$348, net of tax.

Assets and liabilities of the discontinued operation were as follows:

	December 31, 2003	September 30, 2004
	-----	-----
Current assets	\$ 2	\$ --
	=====	=====
Fixed assets	\$ 2	\$ --
	=====	=====
Current liabilities	\$729	\$ --
	=====	=====

Profit and loss of the discontinued operations within consulting segment were as follows:

	Nine months ended September 30,		Three months ended September 30,	
	-----		-----	
	2003	2004	2003	2004
	----	----	----	----
	Restated		Restated	
	-----		-----	
Sales	\$ 172	\$ --	\$ 14	\$--
Cost of sales	154	--	13	--
	-----	-----	-----	---
Gross profit	18	--	1	--
	-----	-----	-----	---
Loss from operations	(31)	(2)	(1)	--
Interest expense	7	4	3	--
	-----	-----	-----	---
Net income (loss) from discontinued operations	\$ (38)	\$ 348	\$ (4)	\$--
	=====	=====	=====	===

Note 9: Subsequent Event

In October 2004, Comverge closed on the sale of additional preferred equity financing in the amount of \$13,600. The preferred equity is senior to the preferred stock of Comverge owned by the Company. This round of financing diluted the Company's holdings to approximately 7% of Comverge's preferred equity and approximately 25% of its total equity.

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PART II - Other information

Item 6: Exhibits and Reports on Form 8-K

(a) Exhibits

- 10.1 Employment Agreement executed on August 19, 2004 and effective as of January 1, 2004 between Databit Inc., Shlomie Morgenstern and the Registrant.*
- 10.2 Restricted Stock Award Agreement, dated as of August 19, 2004, between the Registrant and Shlomie Morgenstern.*
- 10.3 Stock Option Agreement dated as of August 19, 2004, between the Registrant and Shlomie Morgenstern.*
- 10.4 Second Amended and Restated Co-Sale And First Refusal Agreement dated as of October 26, 2004, by and among Converge, Inc., the Registrant, and other persons party thereto.*
- 31(a) Rule 13a-14(a) Certification by Chief Executive Officer
- 31(b) Rule 13a-14(a) Certification by Chief Financial Officer
- 32(a) Section 1350 Certification by Chief Executive Officer **
- 32(b) Section 1350 Certification by Chief Financial Officer **

* Previously filed.

** A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

(b) Reports on Form 8-K

- (i) Report on Form 8-K, filed on July 28, 2004 (earliest event reported July 26, 2004): Item 5 was reported.
- (ii) Report on Form 8-K, filed on August 13, 2004 (earliest event reported August 13, 2004): Item 2 was reported.
- (iii) Report on Form 8-K, filed on August 17, 2004 (earliest event reported August 13, 2004): Item 7 was reported.
- (iv) Report on Form 8-K, filed on August 19, 2004 (earliest event reported August 18, 2004): Item 5 was reported.
- (v) Report on Form 8-K, filed on September 10, 2004 (earliest event reported September 9, 2004): Item 1.01 was reported.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this amendment to its report to be signed on its behalf by its Principal Financial Officer thereunto duly authorized.

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DATA SYSTEMS & SOFTWARE INC.

Dated: November 16, 2004

By: /s/ YACOV KAUFMAN

Yacov Kaufman

Vice President and Chief Financial Officer

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