CREATIVE COMPUTER APPLICATIONS INC
Form 10QSB
January 14, 2004

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended November 30, 2003.

o	**TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT**

For the transition period from to

Commission file number 0-12551

CREATIVE COMPUTER APPLICATIONS, INC.

(Exact name of small business issuer as specified in its charter)

California	**95-3353465**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

26115-A Mureau Road, Calabasas, California 91302
(Address of principal executive offices)

(818) 880-6700
Issuer s telephone number:

State the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable date: 3,318,900 common shares as of December 31, 2003.

Transitional Small Business Disclosure Format (check one):
Yes o No ý

CREATIVE COMPUTER APPLICATIONS, INC.

FORM 10-QSB

INDEX

CREATIVE COMPUTER APPLICATIONS, INC.

PART 1 - FINANCIAL INFORMATION

Item 1. Financial Statements

CONDENSED CONSOLIDATED BALANCE SHEETS

		November 30, 2003 (Unaudited)		August 31, * 2003
ASSETS				
CURRENT ASSETS:				
Cash	$	871,216	$	1,075,323
Receivables, net		1,903,453		2,063,311
Inventories		149,774		164,581
Prepaid expenses and other assets		198,737		231,117
Deferred tax asset		362,850		362,850
TOTAL CURRENT ASSETS		3,486,030		3,897,182
PROPERTY AND EQUIPMENT, net		206,300		219,627
INVENTORY OF COMPONENT PARTS		252,275		267,275
CAPITALIZED SOFTWARE COSTS, net of accumulated amortization of $1,216,337 and $1,114,645		1,387,682		1,360,374
DEFERRED TAX ASSET		536,885		536,885
	$	5,869,172	$	6,281,343
LIABILITIES AND SHAREHOLDERS EQUITY				
CURRENT LIABILITIES:				
Notes payable to bank (Note 4)	$		$	
Accounts payable		258,238		207,624
Accrued liabilities:				
Vacation Pay		203,922		185,508
Accrued Payroll		31,434		105,768
Other		164,815		159,241
Deferred service contract income		1,143,950		1,115,366
Deferred revenue on system sales		314,503		501,507
Capital lease obligation, current portion				361
TOTAL CURRENT LIABILITIES		2,116,862		2,275,375
SHAREHOLDERS EQUITY:				
Common shares, no par value; 20,000,000 shares authorized; 3,318,900 and 3,318,900 shares outstanding		6,192,692		6,192,692
Accumulated deficit		(2,440,382)		(2,186,724)
TOTAL SHAREHOLDERS EQUITY		3,752,310		4,005,968
	$	5,869,172	$	6,281,343

*** As presented in the audited consolidated financial statements**

See Notes to Condensed Consolidated Financial Statements.

CREATIVE COMPUTER APPLICATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended November 30, 2003		Three Months Ended November 30, 2002	
	(unaudited)			
NET SYSTEM SALES AND SERVICE REVENUE (Note 3)				
System sales	$	471,355	$	802,469
Service revenue		1,124,206		1,079,692
		1,595,561		1,882,161
COST OF PRODUCTS AND SERVICES SOLD				
System sales		447,375		579,177
Service revenue		405,054		356,683
		852,429		935,860
Gross profit		743,132		946,301
OPERATING EXPENSES:				
Selling, general and administrative		740,484		651,440
Research and development		256,236		213,510
Total Operating Expenses		996,720		864,950
Operating income (loss)		(253,588)		81,351
INTEREST AND OTHER INCOME		1,357		3,725
INTEREST EXPENSE		(1,427)		(2,347)
Income (loss) before provision for income taxes		(253,658)		82,729
PROVISION FOR INCOME TAXES				34,746
NET INCOME (LOSS)	$	(253,658)	$	47,983
EARNINGS (LOSS) PER SHARE (Note 2):				
Basic	$	(.08)	$	.02
Diluted	$	(.08)	$	.01
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING				

Basic	3,318,900	3,266,400
Diluted	3,318,900	3,382,486

See Notes to Condensed Consolidated Financial Statements.

4

CREATIVE COMPUTER APPLICATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Increase (Decrease) in Cash

	Three Months Ended November 30, 2003	2002
	(unaudited)	
OPERATING ACTIVITIES:		
Net income (loss)	$ (253,658)	$ 47,983
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	33,639	41,901
Provision for doubtful accounts	10,000	
Amortization of capitalized software costs	101,692	105,009
Deferred tax provision		34,746
Increase (decrease) from changes in:		
Receivables	149,858	254,602
Inventories	29,807	13,221
Prepaid expenses and other assets	32,380	751
Accounts payable	50,614	72,737
Accrued liabilities	(50,346)	(199,957)
Deferred revenues	(158,420)	(144,632)
Net cash provided by (used in) operating activities	(54,434)	226,361
INVESTING ACTIVITIES		
Additions to property and equipment	(20,312)	(20,980)
Additions to capitalized software costs	(129,000)	(114,000)
Net cash used in investing activities	(149,312)	(134,980)
FINANCING ACTIVITIES:		
Payments on capital lease obligations	(361)	(5,688)
Proceeds from issuance of stock and exercises of stock options		2,250
Net cash used in financing activities	(361)	(3,438)
NET INCREASE (DECREASE) IN CASH	(204,107)	87,943

Cash, beginning of period		1,075,323		1,027,810
Cash, end of period	$	871,216	$	1,115,753

See notes to Condensed Consolidated Financial Statements.

CREATIVE COMPUTER APPLICATIONS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (which include only normal recurring accruals) necessary to present fairly the Company s financial position as of November 30, 2003, the results of its operations for the three months ended November 30, 2003 and 2002, and cash flows for the three months ended November 30, 2003 and 2002. These results have been determined on the basis of accounting principles generally accepted in the United States of America and practices applied consistently with those used in preparation of the Company s Annual Report on Form 10-KSB for the fiscal year ended August 31, 2003.

The results of operations for the three months ended November 30, 2003 are not necessarily indicative of the results expected for any other period or for the entire year.

Note 2. The Company accounts for its earnings per share in accordance with SFAS No.128, which requires presentation of basic and diluted earnings per share. Basic earnings per share is computed by dividing income or loss available to common shareholders by the weighted average number of common shares outstanding for the reporting period. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts, such as stock options, to issue common stock were exercised or converted into common stock.

Earnings per share has been computed as follows:

		Three Months Ended November 30, 2003		**Three Months Ended November 30, 2002**
NET INCOME (LOSS)	$	(253,658)	$	47,983
Basic weighted average number of common shares outstanding		3,318,900		3,266,400
Dilutive effect of stock options				116,086
Diluted weighted average number of common shares outstanding		3,318,900		3,382,486
Basic earnings (loss) per share	$	(.08)	$	.02
Diluted earnings (loss) per share	$	(.08)	$	.01

At November 30, 2003, options to purchase 645,000 shares of common stock at a per share price ranging from $.72 to $1.76 were not included in the computation of diluted loss per share because inclusion would have been anti-dilutive. At November 30, 2002, warrants to purchase 125,000 shares of common stock at $1.50 per share were not included in the computation of diluted earnings per share because the exercise price exceeded average market price and would have been anti-dilutive.

Note 3. The Company accounts for its software revenue recognition in accordance with Statement of Position 97-2, Software Revenue Recognition , (SOP 97-2). SOP 97-2 requires companies to recognize revenue when (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the vendor s fee is fixed and determinable, and (iv) collectability is probable. The SOP also requires companies to allocate the fee on a multiple element contract between the various elements based on vendor-specific objective evidence of fair value. The Company s policies are in accordance with Staff Accounting Bulletin 101, Revenue Recognition , (SAB 101). SAB 101 provides interpretive guidance on the recognition, presentation and disclosure of revenue in financial statements. SAB 101 expands on the issues not explicitly covered in the SOP.

Note 4. The Company s line of credit with its bank provides for $500,000 on a revolving basis through February 1, 2004, and contains certain loan covenants and financial ratio requirements. On November 30, 2003, there were no amounts outstanding under the line of credit. The Company was in compliance with all of the covenants and financial ratios required by its bank as of November 30, 2003.

Note 5. As allowed by SFAS 123, the Company has adopted the intrinsic value method of accounting for employee stock options under the principles of APB Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and discloses the pro forma effect on net income and income per share as if the fair value based method had been applied. For equity instruments, including stock options, issued to non-employees, the fair value of the equity instruments or the fair value of the consideration received, whichever is more readily determinable, is used to determine the value of services or goods received and the corresponding charge to operations.

The following table illustrates the effect on net income and income per share as if the Company had applied the fair value recognition provision of SFAS No. 123 to stock-based employee compensation.

	Three Months Ended November 30, 2003	Three Months Ended November 30, 2002
Net Income (Loss), as reported	$ (253,658)	$ 47,983
Less: total stock based employee compensation expense determined under fair value method for all awards	(16,835)	(7,865)
Pro forma net income (loss)	$ (270,493)	$ 40,118
Basic net earnings (loss) per share, as reported	$ (.08)	$ .02
Basic net earnings (loss) per share, pro forma	$ (.08)	$ .01
Diluted net earnings (loss) per share, as reported	$ (.08)	$ .01
Diluted net earnings (loss) per share, pro forma	$ (.08)	$ .01

As required by SFAS 123, the Company provides the following disclosure of estimated values for these awards.

The fair value of each option was estimated on the date of grant using a Black-Scholes option-pricing model with the following weighted average assumptions for 2003 and 2002: risk free interest rates ranging from 3.8% to 6.1%, expected lives of 5 years; volatility ranging from 67% to 126% and no assumed dividends. The weighted-average grant-date fair value of options granted during 2003 was estimated to be $1.25. There were no options granted in the three months ended November 30, 2003.

Note 6. In accordance with the bylaws of the Company, officers and directors are indemnified for certain events or occurrences arising as a result of the officer or director s serving in such capacity. The term of the indemnification period is for the lifetime of the officer or director. The maximum potential amount of future payments the Company could be required to make under the indemnification provisions of its bylaws is unlimited. However, the Company has a director and officer liability insurance policy that reduces its exposure and enables it to recover a portion of any future amounts paid. As a result of its insurance policy coverage, the Company believes the estimated exposure for the indemnification provisions of its bylaws is minimal and therefore, the Company has not recorded any related liabilities.

The Company enters into indemnification provisions under agreements with various parties in the normal course of business, typically with customers and landlords. Under these provisions, the Company generally indemnifies and holds harmless the indemnified party for losses suffered or incurred by the indemnified party as a result of the Company s activities or, in some cases, as a result of the indemnified party s activities under the agreement. These indemnification provisions often include indemnifications relating to representations made by the Company with regard to intellectual property rights. These indemnification provisions generally survive termination of the underlying agreement. The maximum potential amount of future payments the Company could be required to make under these indemnification provisions cannot be estimated. The Company maintains general liability, errors and omissions, and professional liability insurance in order to mitigate such risks. The Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification agreements. As a result, the Company believes the estimated exposure under these agreements is minimal. Accordingly, the Company has not recorded any related liabilities.

Note 7. New Accounting Pronouncements - On December 17, 2003, the SEC s Office of the Chief Accountant and Division of Corporation Finance issued Staff Accounting Bulletin (SAB) 104, Revenue Recognition. The SAB updates portions of the interpretive guidance included in Topic 13 of the codification of staff accounting bulletins (SAB 103 codification) in order to make the guidance consistent with current authoritative accounting literature. The principal revisions relate to the incorporation of certain sections of the staff s FAQ document on revenue recognition into Topic 13. The Company does not expect the adoption of SAB 104 to have a material effect on the Company s financial statements.

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

This Quarterly Report on Form 10-QSB includes forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 that involve risk and uncertainty, such as forward-looking statements relating to sales and earnings per share expectations, expectations regarding the Company s liquidity and the impact of seasonality on the Company s operations and is subject to the Risk Factors set forth below. We disclaim any obligation to update our forward-looking statements

Overview

CCA generates revenues primarily from the sale of its Clinical Information Systems (CIS), which includes the licensure of proprietary application software, the licensure of third party software, and the sale of servers upon which the application software operates. In connection with its sales of CIS products, the Company provides implementation services for the installation, integration, and training of end users personnel. The Company generates sales of ancillary software and hardware, including its data acquisition products, to its CIS clients and to third parties. The Company also generates recurring revenues from the provision of comprehensive post implementation services to its CIS clients, pursuant to extended service agreements.

Because of the nature of its business, CCA makes significant investments in research and development for new products and enhancements to existing products. Historically, CCA has funded its research and development programs through cash flow primarily generated from operations. Management anticipates that future expenditures in research and development will either continue at current levels or may increase for the foreseeable future, and will be funded primarily out of the Company s cash flow.

CCA s results of operations for the first fiscal quarter ended November 30, 2003 were marked by a decrease in sales over the comparable quarter in 2003 and a decrease in earnings. The Company s decrease in revenues for the first fiscal quarter was due to a number of factors. The primary factor was a transition to a new version of our core product, CyberLAB® 7.0 that impacted sales of the previou