

SMART ONLINE INC
Form 10-Q
November 15, 2010

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

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2010

OR

Transition report pursuant to Section 13 of 15(d) of the Securities Exchange Act of 1934

Commission File Number: 001-32634

SMART ONLINE, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

95-4439334
(I.R.S. Employer
Identification No.)

4505 Emperor Blvd., Ste. 320
Durham, North Carolina
(Address of principal executive offices)

27703
(Zip Code)

(919) 765-5000

(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 a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Edgar Filing: SMART ONLINE INC - Form 10-Q

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

As of November 11, 2010, there were 18,343,542 shares of the registrant's common stock, par value \$0.001 per share, outstanding.

SMART ONLINE, INC.

FORM 10-Q

For the Quarterly Period Ended September 30, 2010

TABLE OF CONTENTS

		Page No.
PART I – FINANCIAL INFORMATION		
Item 1.	Financial Statements	3
	Consolidated Balance Sheets as of September 30, 2010 (unaudited) and December 31, 2009	3
	Consolidated Statements of Operations (unaudited) for the three and nine months ended September 30, 2010 and 2009	4
	Consolidated Statements of Cash Flows (unaudited) for the nine months ended September 30, 2010 and 2009	5
	Notes to Consolidated Financial Statements (unaudited)	6
Item 2.	Management’s Discussion and Analysis of Financial Condition and Results of Operations	20
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	34
Item 4.	Controls and Procedures	34
PART II – OTHER INFORMATION		
Item 1.	Legal Proceedings	34
Item 1A.	Risk Factors	36
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	37
Item 6.	Exhibits	37
	Signatures	38

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

SMART ONLINE, INC.
CONSOLIDATED BALANCE SHEETS

	September 30, 2010 (unaudited)	December 31, 2009
ASSETS		
Current Assets:		
Cash and Cash Equivalents	\$ 56,686	\$ 119,796
Accounts Receivable, Net	-	13,056
Note Receivable	-	-
Prepaid Expenses	203,339	240,840
Total current assets	260,025	373,692
Property and equipment, net	216,399	258,450
Capitalized software, net	-	450,782
Note Receivable, non-current	-	-
Prepaid expenses, non-current	-	110,700
Intangible assets, net	150,000	150,000
Other assets	5,000	2,496
TOTAL ASSETS	\$ 631,424	\$ 1,346,120
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities		
Accounts payable	\$ 537,928	\$ 518,309
Notes payable (See Note 3)	2,124,678	1,964,281
Deferred revenue (See Note 2)	27,561	40,115
Accrued liabilities – Nouri	1,400,000	1,802,379
Accrued liabilities (See Note 2)	2,266,165	2,623,959
Total current liabilities	6,356,332	6,949,043
Long-term liabilities:		
Long-term portion of notes payable (See Note 3)	12,370,367	9,785,255
Deferred revenue (See Note 2)	1,153	5,601
Total long-term liabilities	12,371,520	9,790,856
Total liabilities	18,727,852	16,739,899
Commitments and contingencies (See Note 4)		
Stockholders' equity (deficit):		
Preferred stock, 0.001 par value, 5,000,000 shares authorized, no shares issued and outstanding at September 30, 2010 and December 31, 2009		
Common Stock, \$.001 par value, 45,000,000 shares authorized, 18,342,542 and 18,332,542 shares Issued and Outstanding at September 30, 2010 and December 31, 2009 respectively.	18,343	18,333
Additional paid-in capital	67,059,722	67,036,836
Accumulated deficit	(85,174,493)	(82,448,948)
Total Stockholders' Deficit	(18,096,428)	(15,393,779)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	\$ 631,424	\$ 1,346,120

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

SMART ONLINE, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
REVENUES:				
Subscription fees	\$ 119,152	\$ 159,149	\$ 378,556	\$ 610,751
Professional service fees	12,600	63,200	82,425	261,699
License fees	65,850	11,250	224,500	33,750
Hosting fees	37,722	33,751	119,716	139,007
Other revenue	25,644	26,300	79,389	100,777
Total revenues	260,968	293,650	884,586	1,145,984
COST OF REVENUES	344,156	430,967	1,046,400	1,125,901
GROSS PROFIT (LOSS)	(83,188)	(137,317)	(161,814)	20,083
OPERATING EXPENSES:				
General and administrative	408,004	2,355,353	1,469,892	4,112,993
Sales and marketing	181,132	180,759	513,408	707,289
Research and development	7,695	36,406	50,080	540,232
Loss on impairment	-	-	-	438,286
(Gain) loss on disposal of assets, net	398,962	(12,307)	398,962	(22,574)
Total operating expenses	995,793	2,560,211	2,432,342	5,776,226
LOSS FROM OPERATIONS	(1,078,981)	(2,697,528)	(2,594,156)	(5,756,143)
OTHER INCOME (EXPENSE):				
Interest expense, net	(244,189)	(169,609)	(687,909)	(455,951)
Gain on legal settlements, net	2,547	-	556,517	6,000
Other Income	-	-	-	10,267
Total other expense	(241,642)	(169,609)	(131,392)	(439,684)
NET LOSS	\$ (1,320,623)	\$ (2,867,137)	\$ (2,725,548)	\$ (6,195,827)
NET LOSS PER COMMON SHARE:				
Basic and fully diluted	\$ (0.07)	\$ (0.16)	\$ (0.15)	\$ (0.34)
WEIGHTED-AVERAGE NUMBER OF SHARES USED IN COMPUTING NET LOSS PER COMMON SHARE				
Basic and fully diluted	18,342,542	18,332,542	18,342,542	18,332,542

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

SMART ONLINE, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Loss	\$ (2,725,548)	\$ (6,195,827)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	100,892	462,761
Bad debt expense	377,348	2,207,685
Stock-based compensation expense	22,884	88,235
Loss on impairment of intangible assets		438,228
(Gain) loss on disposal of assets	398,962	(22,574)
Changes in assets and liabilities:		
Accounts receivable	(309,404)	213,010
Notes receivable	(54,888)	(3,228,038)
Prepaid expenses	148,204	126,005
Other assets	(2,504)	(352)
Deferred revenue	(17,002)	(188,170)
Accounts payable	19,619	1,768,181
Accrued and other expenses	(760,173)	1,627,739
Net cash used in operating activities	(2,801,610)	(2,703,117)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of furniture and equipment	(7,009)	(14,565)
Capitalized software		