

INTERNATIONAL MICROCOMPUTER SOFTWARE INC /CA/
Form 10QSB
February 14, 2006

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

FORM 10-QSB

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

For the quarterly period ended **December 31, 2005**

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

For the transition period from: _____ to _____

Commission File Number 0-15949

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC.

(Exact name of Small business issuer in its charter)

CALIFORNIA

(State or other jurisdiction of incorporation or organization)

94-2862863

(I.R.S. Employer Identification No.)

100 ROWLAND WAY, NOVATO, CALIFORNIA

(Address of principal executive offices)

94945

(Zip code)

(415) 878-4000

Issuer's telephone number

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. YES NO

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 January 31, 2006, 30,107,284 shares of Issuer's common stock, no par value, were outstanding.

Transitional Small Business Disclosure Format: YES NO

**INTERNATIONAL MICROCOMPUTER SOFTWARE, INC.
AND SUBSIDIARIES**

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PART I - FINANCIAL INFORMATION**Item 1- Condensed Consolidated Financial Statements****INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands, except share amounts)

Unaudited	December 31, 2005	June 30, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	\$9,849	\$4,347
Trading securities	-	714
Receivables, less allowances for doubtful accounts, discounts and returns of \$551 as of December 31, 2005 and \$626 as of June 30, 2005.	1,384	773
Inventories, net	873	758
Receivables, other (related to discontinued operations)	-	2,000
Receivables, other	-	30
Other current assets	1,278	530
Assets related to discontinued operations	-	12,231
Total current assets	13,384	21,383
Fixed assets, net	340	377
Intangible assets		
Capitalized software, net	322	494
Domain names and brands, net	1,960	1,574
Distribution rights and proprietary plans, net	773	170
Capitalized customer lists, agreements and relationships, net	1,327	326
Goodwill	3,678	2,090
Trademarks, net	19	1
Total intangible assets	8,079	4,655
Total assets	\$21,803	\$26,415
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term debt	873	2,764
Trade accounts payable	1,364	2,245
Accrued and other liabilities	1,577	1,871
Deferred revenues	45	38
Liabilities related to discontinued operations	-	1,037
Total current liabilities	3,859	7,955
Long-term debt and other obligations	173	230
Total liabilities	4,032	8,185
Shareholders' equity	44,843	43,663

Common stock, no par value; 300,000,000 authorized; 29,845,877
 issued and outstanding
 as of December 31, 2005 and 28,796,886 issued and outstanding as
 of June 30, 2005

Accumulated deficit	(27,161)	(25,331)
Accumulated other comprehensive income (loss)	89	(102)
Total shareholders' equity	17,771	18,230
Total liabilities and shareholders' equity	\$21,803	\$26,415

See Notes to Condensed Consolidated Financial Statements

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INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS and COMPREHENSIVE INCOME /
(LOSS)

(In thousands, except per share amounts)
(Unaudited)

	Three months ended December 31,		Six months ended December 31,	
	2005	2004	2005	2004
Net revenues	\$3,719	\$3,478	\$7,684	\$6,613
Product costs	1,328	1,122	2,783	2,143
Gross margin	2,391	2,356	4,901	4,470
Costs and expenses				
Sales and marketing	1,658	1,538	3,189	2,888
General and administrative	1,329	982	2,754	1,841
Research and development	553	368	988	837
Total operating expenses	3,540	2,888	6,931	5,566
Operating loss	(1,149)	(532)	(2,030)	(1,096)
Other income (expense)				
Interest and other, net	17	33	(52)	39
Realized / unrealized gain on securities	923	471	765	422
Loss before income tax	(209)	(28)	(1,317)	(635)
Income tax provision	(39)	(2)	(39)	(8)
Loss from continuing operations	(248)	(30)	(1,356)	(643)
Income from discontinued operations, net of income tax	-	159	-	444
Gain (loss) from the sale of discontinued operations, net of income tax	369	-	(474)	53
Net income (loss)	\$121	\$129	(\$1,830)	(\$146)
Other comprehensive income (loss)				
Unrealized loss on restricted securities	(478)	-	-	-
Foreign currency translation adjustments	2	(24)	191	(34)
Comprehensive income (loss)	(\$355)	\$105	(\$1,639)	(\$180)
Basic earnings (loss) per share:				
Loss from continuing operations	(\$0.01)	\$0.00	(\$0.05)	(\$0.02)
Income from discontinued operations, net of income tax	\$0.00	\$0.01	\$0.00	\$0.02
Gain (loss) from the sale of discontinued operations, net of income tax	\$0.01	\$0.00	(\$0.02)	\$0.00
Net income (loss)	\$0.00	\$0.00	(\$0.06)	(\$0.01)

Diluted earnings (loss) per share:				
Loss from continuing operations	(\$0.01)	\$0.00	(\$0.05)	(\$0.02)
Income from discontinued operations, net of income tax	\$0.00	\$0.01	\$0.00	\$0.02
Gain (loss) from the sale of discontinued operations, net of income tax	\$0.01	\$0.00	(\$0.02)	\$0.00
Net income (loss)	\$0.00	\$0.00	(\$0.06)	(\$0.01)
Shares used in computing basic earnings (loss) per share	29,821	27,196	29,755	27,605
Shares used in computing diluted earnings (loss) per share	31,831	29,885	29,755	27,605

See Notes to Condensed Consolidated Financial Statements

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Six months ended December 31, 2005

(In thousands, except share amounts)

(Unaudited)

Common Stock

	Shares	Amount	Accumulated deficit	Accumulated other comprehensive income (loss)	Total
Balance at July 1, 2005	28,796,886	\$43,663	(\$25,331)	(\$102)	\$18,230
Issuance of common stock related to:					
Stock options exercised	85,291	73			73
Warrants exercised	117,117	-			-
Acquisitions	826,583	1,021			1,021
Finder's fee related to acquisition	20,000	25			25
Issuance of stock options related to:					
Consulting services rendered		21			21
Issuance of warrants related to:					
Acquisitions		6			6
Procurement of short-term debt		68			68
Accrual of stock buy-back		(30)			(30)
Issuance of stock options		2			2
Variable accounting adjustment		(6)			(6)
Net loss			(1,830)		(1,830)
Foreign currency translation adjustment				191	191
Balance at December 31, 2005	29,845,877	\$44,843	(\$27,161)	\$89	\$17,771

See Notes to Condensed Consolidated Financial Statements

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Six months ended December 31,	
	2005	2004
Cash flows from operating activities:		
Net cash provided by (used in) operating activities	(\$753)	\$248
Cash flows from investing activities:		
Proceeds from sale of discontinued operations	9,466	650
Proceeds from sale of product line	-	258
Acquisition of subsidiaries	(1,807)	(1,356)
Acquisition of software development, domain names and trademarks	-	(600)
Purchases of equipment and software	(29)	(163)
Transfer cash to escrow for Jupitermedia	-	(499)
Proceeds from the sale of marketable securities	1,524	1,780
Other	(8)	25
Cash provided by discontinued operations in investing activities	-	464
Net cash provided by investing activities	9,146	559
Cash flows from financing activities:		
Proceeds from borrowings	850	400
Repayments of notes	(3,802)	(1,730)
Proceeds from warrants and options exercised	73	137
Cash provided by discontinued operations in financing activities	-	12
Net cash used in financing activities	(2,879)	(1,181)
Effect of exchange rate change on cash and cash equivalents	(12)	(34)
Net increase (decrease) in cash and cash equivalents	5,502	(408)
Cash and cash equivalents at beginning of period	4,347	3,212
Cash and cash equivalents at end of the period	\$9,849	\$2,804

	Six months ended December 31,	
	2005	2004
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Interest paid	128	125

SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES		
Capital stock issued in conjunction with acquisitions	1,046	1,602
Warrants issued in conjunction with acquisitions	6	-
Notes payable incurred in conjunction with acquisitions	1,000	505
Warrants issued in conjunction with short-term debt	68	-

See Notes to Condensed Consolidated Financial Statements

**INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

1. Basis of Presentation

The interim condensed consolidated financial statements have been prepared from the records of International Microcomputer Software, Inc., a California corporation, and Subsidiaries ("we" or the "Company") without audit. All significant inter-company balances and transactions have been eliminated in consolidation. In the opinion of management, all adjustments, which consist of only normal recurring adjustments, to present fairly the financial position at December 31, 2005 and the results of operations and cash flows for the three and six months ended December 31, 2005 and 2004, have been made. The interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in our Annual Report on Form 10-KSB, for the fiscal year ended June 30, 2005. The results of operations for the three and six months ended December 31, 2005 are not necessarily indicative of the results to be expected for any other interim period or for the full year.

2. Use of Estimates

Our condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). These accounting principles require us to make certain estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions upon which we rely are reasonable based upon information available to us at the time that these estimates, judgments and assumptions are made. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities as of the date of our condensed consolidated financial statements as well as the reported amounts of revenues and expenses during the periods presented. Our condensed consolidated financial statements would be affected to the extent there are material differences between these estimates and actual results. In many cases, the accounting treatment of a particular transaction is specifically dictated by GAAP and does not require management's judgment in its application. There are also areas in which management's judgment in selecting any available alternative would not produce a materially different result.

3. Reclassifications

Reclassifications have been made to the amounts reported for the three and six months ended December 31, 2004 to conform to the current period's presentation. The amounts reported for the three and six months ended December 31, 2004, present the assets, liabilities and results of operations for Allume Systems, Inc. ("Allume") as discontinued operations due to the sale of Allume to Smith Micro Software Inc. ("Smith Micro") on July 1, 2005.

Also, the amounts reported for the six months ended December 31, 2004 include the assets, liabilities and results of operations for Keynomics, Inc. ("Keynomics") as discontinued operations due to the sale of Keynomics on July 29, 2004.

4. Discontinued Operations

Gain (loss) from the sale of discontinued operations, net of income tax

Three and six months ended December 31, 2005: Sale of Allume

On July 1, 2005, we sold all of the issued and outstanding capital stock of Allume to Smith Micro for an aggregate sales price of \$12.8 million consisting of \$11.0 million cash and 397,547 unregistered shares of Smith Micro's common stock, having a market value (based on the five-trading-day average price of Smith Micro's common stock surrounding the date the business combination was announced) of \$1.8 million. At closing, a portion of the proceeds

from the sale was deposited in an indemnity escrow, which included \$1.25 million in cash and 170,378 shares of Smith Micro's common stock having a closing date market value of \$784,000, to secure certain representations and warranties included in our stock purchase agreement with Smith Micro. In November 2005, we replaced the shares of Smith Micro common stock in escrow with cash, as permitted by the escrow agreement and sold 100% of our holdings of Smith Micro shares at a gain of \$923,000. In December 2005, Smith Micro released \$500,000 of the escrowed cash to us.

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As a result of this sale, we have categorized the assets, liabilities and operations of Allume as discontinued operations for the three and six months ended December 31, 2004 and in the three months ended December 31, 2005 we recorded a gain on the sale of discontinued operations of \$369,000 primarily representing the difference between the actual amount released from escrow and the estimated amount to be released as of September 30, 2005. The loss on the sale of Allume for the six months ended December 31, 2005 totaled \$474,000. This loss calculation does not include the remaining cash held in escrow of approximately \$1.2 million and is subject to change in future reporting periods depending upon the future release of cash from escrow.

Six months ended December 31, 2004: Sale of Keynomics

In July 2004, we sold the assets and customer related liabilities of our wholly owned subsidiary Keynomics. We evaluated the Keynomics business segment and its long-term prospects during the quarter ended June 30, 2004 and with our focus on direct marketing and the on-line distribution of utilities and precision design content, we determined that Keynomics no longer represented a strategic fit for our Company. The \$53,000 gain from the sale of discontinued operations for the six months ended December 31, 2004 relates to the sale of Keynomics and represents the excess of the total consideration received over its net carrying value.

Income from discontinued operations, net of income tax

Income from discontinued operations totaling \$159,000 for the three months ended December 31, 2004 represents the pre-tax net income from Allume. Allume’s net revenues were \$2.6 million for the three months ended December 31, 2004.

Income from discontinued operations totaling \$444,000 for the six months ended December 31, 2004 represents the pre-tax net income of Allume of \$449,000 offset by the net loss of Keynomics of \$5,000. Allume’s net revenues were \$5.1 million and Keynomics net revenues were \$68,000 for the six months ended December 31, 2004.

5. Acquisition of Weinmaster Homes, Ltd.

On July, 1, 2005, Houseplans, Inc. (“Houseplans”), our wholly owned subsidiary, consummated the acquisition of all of the issued and outstanding stock of Weinmaster Homes, Ltd. (“WHL”), pursuant to a Stock Purchase Agreement, between WHL, Bruce and Janice Weinmaster and Houseplans.

The preliminary purchase price of approximately \$4.2 million was comprised as follows:

(In millions)

Description	Amount
Fair value of 826,583 shares of our common stock	\$