ERESEARCHTECHNOLOGY INC /DE/
Form 10-Q
August 10, 2001

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 205498

FORM 10-Q

(Mark One)

[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. For the quarterly period ended June 30, 2001

or

[ ] Transitional report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. For the transitional period from _____________ to__________________

Commission file number 0-29100

eResearchTechnology, Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

(I.R.S. Empl

30 South 17th Street
Philadelphia, PA
(Address of principal executive offices)

215-972-0420
(Registrant's telephone number, including area code)

(Former name, former address and formal 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.

X Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

The number of shares of Common Stock, $.01 par value, outstanding as of July 31, 2001, was 6,960,887.

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Part 1. Financial Information

Item 1. Consolidated Financial Statements

eResearchTechnology, Inc. and Subsidiaries
Consolidated Balance Sheets
(in thousands, except share amounts)

	June 30, 2001

	(unaudited)
Assets	
Current assets:	
Cash and cash equivalents	$ 13,603
Short-term investments	6,019
Marketable securities	1,348
Accounts receivable, net	4,903
Prepaid expenses and other	1,995
Deferred income taxes	277
Total current assets	28,145
Property and equipment, net	5,786
Goodwill, net	1,370
Investments in non-marketable securities	1,226
Other assets	58
Deferred income taxes	3,776
	$ 40,361
Liabilities and Stockholders' Equity	
Current liabilities:	
Accounts payable	$ 1,431
Accrued expenses	3,681
Income taxes payable	1,224
Deferred revenues	3,609
Total current liabilities	9,945
Minority interest in subsidiary	-
Commitments and contingencies	
Stockholders' equity:	
Preferred stock - $10 par value, 500,000 shares authorized, none issued and outstanding	-
Common stock - $.01 par value, 15,000,000 shares authorized, 7,470,687 shares issued	75
Additional paid-in capital	38,890
Unrealized loss on marketable securities, net of tax	(409)
Treasury stock, 509,800 and 499,800 shares at cost	(2,766)
Accumulated deficit	(5,374)
Total stockholders' equity	30,416
	$ 40,361

The accompanying notes are an integral part of these statements.

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eResearchTechnology, Inc. and Subsidiaries
Consolidated Statements of Operations
(in thousands, except per share information)

Three Months Ended June 30,

	2001	2000
	(unaudited)	
Net revenues:		
Licenses	$ 198	$ 1,362
Services	6,760	5,699
Total net revenues	6,958	7,061
Costs of revenues:		
Cost of licenses	128	153
Cost of services	3,041	3,289
Total costs of revenues	3,169	3,442
Gross margin	3,789	3,619
Operating expenses:		
Selling and marketing	1,401	1,275
General and administrative	1,272	1,739
Research and development	1,216	1,155
Asset impairment charge	-	-
Total operating expenses	3,889	4,169
Operating loss	(100)	(550)
Interest income, net	243	382
Gain on sale of domestic CRO operations	-	248
Income (loss) before income taxes	143	80
Income tax benefit (provision)	(57)	(32)
Minority interest dividend	-	-
Net income (loss)	$ 86	$ 48
Basic and diluted net income (loss) per share	$ 0.01	$ 0.01

The accompanying notes are an integral part of these statements.

eResearchTechnology, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
(in thousands)

Operating activities:
Net loss
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:
Gain on sale of the domestic CRO operations
Depreciation and amortization
Provision for losses on accounts receivable
Issuance of common stock options and warrants for services rendered
Deferred income taxes
Asset impairment charge
Changes in assets and liabilities:
Accounts receivable
Prepaid expenses and other
Accounts payable
Accrued expenses
Income taxes payable
Deferred revenues

Net cash provided by (used in) operating activities

Investing activities:
Purchases of property and equipment
Purchase of marketable securities
Purchase of non-marketable securities
Net purchase of short-term investments
Net proceeds from sale of the domestic CRO operations

Net cash provided by (used in) investing activities

Financing activities:
Net proceeds from the issuance of convertible preferred stock in subsidiary
Net proceeds from exercise of stock options
Purchase of convertible preferred stock in subsidiary
Minority interest dividend paid
Repurchase of common stock for treasury

Net cash provided by (used in) financing activities

Net increase (decrease) in cash and cash equivalents

Cash and cash equivalents, beginning of period

Cash and cash equivalents, end of period

The accompanying notes are an integral part of these statements.

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ResearchTechnology, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements, which include the

accounts of eResearchTechnology, Inc. (the "Company") and its wholly owned subsidiaries, have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for fair presentation have been included. Operating results for the periods ended June 30, 2001 are not necessarily indicative of the results that may be expected for the year ending December 31, 2001. Further information on potential factors that could affect the Company's financial results can be found in the Company's Reports on Forms 10-K and 10-Q filed with the Securities and Exchange Commission.

Note 2. Summary of Significant Accounting Policies

Principles of Consolidation. The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

Reclassifications. The consolidated financial statements for prior periods have been reclassified to conform to the current period's presentation.

Management's Use of Estimates. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note 3. Asset Impairment Charge - Marketable and Non-Marketable Securities

At June 30, 2001, marketable securities consisted of an investment in the common stock of Medical Advisory Systems (MAS), a publicly traded company, which the Company purchased in March 2000 for $5,775,000. This investment has been classified as available-for-sale, pursuant to Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Available-for-sale securities are carried at fair value, based on quoted market prices, with unrealized gains and losses, net of tax, reported as a separate component of stockholders' equity. As of December 31, 2000, an unrealized loss of $2,042,000, net of tax, was reported as a separate component of stockholders' equity. In March 2001, in accordance with SFAS No. 115, management determined the decline in the fair value of MAS common stock to be other than temporary, and as a result wrote down the cost basis of the MAS investment to $2,029,000, which was the market value of the MAS common stock held on March 31, 2001. In connection with this write-down, an asset impairment charge of $3,746,000 was recorded during the quarter ended March 31, 2001. As of June 30, 2001, an unrealized loss of $409,000, net of tax, was reported as a separate component of stockholders' equity.

At June 30, 2001, investments in non-marketable securities include the carrying value of the Company's investment in AmericasDoctor.com, Inc., which is accounted for under the cost method in accordance with Accounting Principles Board (APB) No. 18, "The Equity Method of Accounting for Investments in Common Stock." In March 2001, in accordance with APB No. 18, management determined that a decrease in the value of the investment occurred which was deemed to be other than temporary, and as a result wrote down the cost basis of the investment to $1,076,000. In connection with this write-down, an asset impairment charge of $1,224,000 was recorded during the quarter ended March 31, 2001.

Note 4. Net Income (Loss) per Share

The Company follows SFAS No. 128 "Earnings per Share". This statement requires the presentation of basic and diluted earnings per share. Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of shares of common stock outstanding during the period. Diluted net income (loss) per share is computed by dividing net income (loss) by the weighted average number of shares of common stock outstanding during the period, adjusted for the dilutive effect of common stock equivalents, which consist primarily of stock options, using the treasury stock method.

The table below sets forth the reconciliation of the numerators and denominators of the basic and diluted net income (loss) per share computations.

Three Months Ended June 30,

2001	Net Income	Shar
Basic net income...	$ 86,000	6,965
Effect of dilutive shares................................	--	26
Diluted net income.......................................	$ 86,000	6,991
2000		
Basic net income...	$ 48,000	6,960
Effect of dilutive shares................................	--	154
Diluted net income.......................................	$ 48,000	7,114

Options to purchase 147,000 and 491,000 shares of common stock were outstanding at June 30, 2001 and 2000, respectively, and were included in the computation of diluted net income per share. Options to purchase 1,089,000 and 253,000 shares of common stock were outstanding at June 30, 2001 and 2000, respectively, but were not included in the computation of diluted net income per share because the option exercise prices were greater than the average market price of the Company's common stock during the period.

Six Months Ended June 30,

2001	Net Loss	Shar
Basic net loss...	$(5,361,000)	6,968
Effect of dilutive shares................................	--	
Diluted net loss...	$(5,361,000)	6,968

2000

Basic net loss	$ (165,000)	6,942
Effect of dilutive shares	--	
Diluted net loss	$ (165,000)	6,942

Options to purchase 1,236,000 and 744,000 shares of common stock were outstanding at June 30, 2001 and 2000, respectively, but were not included in the diluted computation because the Company incurred a net loss and the inclusion would be anti-dilutive.

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Note 5. Comprehensive Income

The Company follows SFAS No. 130, "Reporting Comprehensive Income." The Company's comprehensive income includes net income and unrealized gains and losses from foreign currency translation and marketable securities. The unrealized gains and losses from foreign currency translation were immaterial as of June 30, 2001 and 2000. For the six months ended June 30, 2001 and 2000, the Company recorded an unrealized loss of $409,000 and $41,000, respectively, net of tax, from its investment in marketable securities.

Note 6. New Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board issued SFAS No. 141, "Business Combinations" (effective July 1, 2001), and SFAS No. 142 "Goodwill and Other Intangible Assets" (effective for the Company on January 1, 2002). SFAS No.141 prohibits pooling-of-interests accounting for acquisitions. SFAS No. 142 specifies that goodwill and some intangible assets will no longer be amortized but instead will be subject to periodic impairment testing. The Company is in the process of evaluating the financial statement impact of adoption of SFAS No. 142.

Note 7. Operating Segments

The Company's operating segments are strategic business units that offer different products and services to a common client base. The Company's products and services are provided both in the United States and internationally through two reportable business segments: Clinical Operations, which includes centralized core-diagnostic electrocardiographic services; and Technology Operations, which includes the development, marketing and support of clinical trial and data management software and consulting services. Results of operations and identifiable assets that cannot be directly attributed to either Clinical or Technology Operations are included in Other.

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The Company evaluates performance based on the net revenues and operating earnings performance of the respective business segments. Segment information is as follows:

	Three Months Ended June 30, 2		
	Clinical Operations	Technology Operations	Othe
License revenues	$ -	$ 198,000	$
Services revenues	4,966,000	1,794,000	
Net revenues from external customers	4,966,000	1,992,000	
Income (loss) from operations	991,000	(1,091,000)	
Identifiable assets	9,626,000	4,486,000	26,249

	Three Months Ended June 30, 2		
	Clinical Operations	Technology Operations	Othe
License revenues	$ -	$ 1,362,000	$
Services revenues	3,678,000	2,021,000	
Net revenues from external customers	3,678,000	3,383,000	
Loss from operations	(134,000)	(416,000)	
Identifiable assets	7,307,000	5,923,000	40,134

	Six Months Ended June 30, 200		
	Clinical Operations	Technology Operations	Othe
License revenues	$ -	$ 224,000	$
Services revenues	9,089,000	3,539,000	
Net revenues from external customers	9,089,000	3,763,000	
Income (loss) from operations	1,139,000	(2,472,000)	(4,970
Identifiable assets	9,626,000	4,486,000	26,249

	Six Months Ended June 30, 200		
	Clinical Operations	Technology Operations	Othe
License revenues	$ -	$ 2,355,000	$
Services revenues	6,617,000	4,170,000	
Net revenues from external customers	6,617,000	6,525,000	
Loss from operations	(218,000)	(959,000)	
Identifiable assets	7,307,000	5,923,000	40,134

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

Cautionary Statement for Forward-Looking Information

The following discussion and analysis should be read in conjunction with the Company's financial statements and the related notes to the financial statements appearing elsewhere in this report. The following includes a number of forward-looking statements that reflects the Company's current views with respect to future events and financial performance. The Company uses words such

as anticipate, believe, expect, future, and intend, and similar expressions to identify forward-looking statements. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this report. These forward-looking statements are subject to risks and uncertainties such as competitive factors, technology development, market demand and the Company's ability to obtain new contracts and accurately estimate net revenues due to variability in size, scope and duration of projects, and internal issues of the sponsoring client. These and other risk factors have been further discussed in the Company's Report on Form 10-Q dated March 31, 2001. Such risks and uncertainties could cause actual results to differ materially from historical results or future predictions. Further information on potential factors that could affect the Company's financial results can be found in the Company's Registration Statement on Form S-1 and its Reports on Forms 10-K and 10-Q filed with the Securities and Exchange Commission.

Overview

eResearchTechnology, Inc. (the "Company") is a business-to-business provider of integrated software applications and technology consulting services to the pharmaceutical, biotechnology and medical device industries. The Company offers Internet and other technology-based solutions designed to streamline the clinical trials process by enabling its customers to automate many parts of a clinical trial. The Company is also a market leader in providing centralized core-diagnostic electrocardiographic services on a global basis. Historically, the Company's products and services have been provided, both in the United States and internationally, through two business segments: Clinical Operations and Technology Operations. Clinical Operations include centralized core-diagnostic electrocardiographic services. Technology Operations include the development, marketing and support of clinical trial and data management software and consulting services.

The Company has been continuously committed to the effective use of technology in clinical applications for over 20 years. This commitment included the Company's filing of the first computer-assisted new drug application with the Food and Drug Administration in 1985, the Company's introduction of a technology-enhanced electrocardiogram service in 1988 and the Company's acquisition of DLB Systems in October 1997. The research and development and baseline technology obtained in the DLB Systems acquisition provided the platform for the development of the Company's current software applications. Over time, the Company has also conducted various clinical and diagnostic operations, including operating a clinical research organization from 1995 until December 31, 1999. The sale of the Company's domestic clinical research operations to SCP Communications, Inc. (SCP) on December 31, 1999 marked the completion of its efforts to cease providing clinical research services and allowed the Company to focus exclusively on providing technology-based solutions to the clinical trials market.

The Company's license revenues consist of up-front software license fees. The Company's service revenues consist of technology consulting and training services, software maintenance services and centralized core-diagnostic electrocardiographic (Diagnostic) services.

The Company recognizes software revenues in accordance with Statement of Position 97-2, Software Revenue Recognition, as amended by Statement of Position 98-9. Accordingly, the Company recognizes license revenues when a formal agreement exists, delivery of the software and related documentation has occurred, collectibility is probable and the license fee is fixed or determinable. The Company recognizes revenues from software maintenance contracts on a straight-line basis over the term of the maintenance contract, which is typically twelve months. The Company provides consulting and training services on a time and materials basis and recognizes revenues as the Company performs the services. Diagnostic service revenues consist of revenues from

services that the Company provides on a fee-for-service basis. The Company recognizes diagnostic service revenues as the services are performed.

The Company's strategy is to create more of a recurring revenue business model by deploying eResNets and modular solutions under agreements that permit their use in multiple clinical trials at any number of sites. An eResNet integrates the Company's analytical processing tools with any combination of the Company's products and services that includes the data capture system called eDataEntry and the Company's software for collecting, editing and managing clinical trial data called eDataManagement. By offering the eResNet and modular solutions to its customers, the Company gives the customer the option of either using an existing license, purchasing an additional license or paying monthly for the use of these solutions on a per user, per trial, per site basis. However, this business model is in an emerging state and its revenue and income potential is unproven. Furthermore, the Company's historical revenue sources will likely continue to be major contributors to the Company's overall revenues.

The Company experienced a decrease in license revenues in the first and second quarters of 2001. Even though the Company's pipeline of new business opportunities is strong, growing caution in the general business climate and particularly in the technology sector has impacted final decisions on new software licenses in 2001. The Company completed extensions to two existing technology agreements in the second quarter. The Company introduced a new strategy in 2001 which offers customers a flexible acquisition option to purchase or rent the Company's applications on either a monthly or annual basis. The Company also launched its first customers under the applications service provider (ASP) model in 2001 and currently has four clients operational. The ASP approach also offers the Company the opportunity to build market share and obtain accounts that basically were not willing to purchase legacy solutions through a license fee.

Diagnostic service revenues vary based on the conduct of the Company's customers' clinical trials. Customers terminate or delay trials for a variety of reasons, including the failure of the product being tested to satisfy safety or efficacy requirements, unexpected or undesired clinical results, a customer's decision to forgo a particular study, insufficient patient enrollment or investigator recruitment, and production problems resulting in shortages of required supplies. Under a typical contract for diagnostic services, customers pay the Company a portion of the Company's fee for these services upon contract execution as an upfront deposit, which is typically nonrefundable upon contract termination.

Cost of licenses consists primarily of the cost of application provider services, the cost of producing compact disks and related documentation and royalties paid to third parties in connection with their contributions to the Company's product development. Cost of services includes the cost of technology consulting and maintenance services and the cost of diagnostic services. Cost of technology consulting and maintenance services consists primarily of wages, fees paid to outside consultants and other direct operating costs related to the Company's consulting and customer support functions. Cost of diagnostic services consists primarily of direct costs related to the Company's centralized electrocardiogram services and includes wages, fees paid to outside consultants, shipping expenses and other direct operating costs. Selling and marketing expenses consist primarily of salaries and commissions paid to sales and marketing personnel or paid to third parties under marketing assistance agreements, travel expenses and advertising and promotional expenditures. General and administrative expenses consist primarily of salaries, benefits and direct costs for the Company's finance, administrative, corporate information technology and executive management functions, in addition to professional

service fees. Research and development expenses consist primarily of salaries and benefits paid to the Company's product development staff, costs paid to outside consultants and direct costs associated with the development of the Company's technology products.

The Company conducts its operations with offices in the United States and the United Kingdom (UK). The Company's international net revenue represented 20.1% and 15.2% of total net revenue for the three months ended June 30, 2001 and 2000, respectively, and 24.6% and 17.2% of total net revenue for the six months ended June 30, 2001 and 2000, respectively.

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Results of Operations

The following table presents certain financial data as a percentage of total net revenues:

	Three Months Ended June 30,	
	2001	2000
	(unaudited)	
Net revenues:		
Licenses	2.8%	19.3%
Services	97.2	80.7
Total net revenues	100.0	100.0
Costs of revenues:		
Cost of licenses	1.8	2.2
Cost of services	43.7	46.6
Total costs of revenues	45.5	48.7
Gross margin	54.5	51.3
Operating expenses:		
Selling and marketing	20.1	18.1
General and administrative	18.3	24.6
Research and development	17.5	16.4
Asset impairment charge	-	-
Total operating expenses	55.9	59.1
Operating loss	(1.4)	(7.8)
Interest income, net	3.5	5.4
Gain on sale of domestic CRO	-	3.5
Income (loss) before income taxes	2.1	1.1
Income tax benefit (provision)	(0.9)	(0.4)

Minority interest dividends	-	-	
Net income (loss)	1.2%	0.7%	

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Three months ended June 30, 2001 compared to three months ended June 30, 2000.

Total net revenues decreased 1.4% to $7.0 million for the three months ended June 30, 2001 compared to $7.1 million for the three months ended June 30, 2000.

License revenues decreased 85.9% to $198,000 for the three months ended June 30, 2001 compared to $1.4 million for the three months ended June 30, 2000. The decrease in license revenues was primarily due to fewer license contract signings in the second quarter of 2001. The Company believes the decrease in license contract signings was primarily the result of growing caution in the general business climate and particularly in the technology sector, which has impacted final decisions on new software licenses in the second quarter of 2001. Services revenues increased 19.3% to $6.8 million for the three months ended June 30, 2001 compared to $5.7 million for the three months ended June 30, 2000. Technology consulting and training service revenues decreased 31.4% to $755,000 for the three months ended June 30, 2001 compared to $1.1 million for the three months ended June 30, 2000. The decrease in technology consulting and training service revenues was due primarily to the termination of a two-year consulting contract in December 2000, which accounted for $575,000 of revenue in the second quarter of 2000. This decrease was partially offset by additional support revenues from new software installations and increased consulting activity in support of the Company's software and client needs. Software maintenance revenues increased 8.5% to $1.0 million for the three months ended June 30, 2001 compared to $922,000 for the three months ended June 30, 2000. The increase in software maintenance was due to a larger installed base of software licenses during the second quarter of 2001 compared to the second quarter of 2000. Diagnostic service revenues increased 35.1% to $5.0 million for the three months ended June 30, 2001 compared to $3.7 million for the three months ended June 30, 2000. The increase was primarily due to increased sales volume with both new and existing clients.

Total cost of revenues decreased 5.9% to $3.2 million, or 45.5% of total net revenues, for the three months ended June 30, 2001 compared to $3.4 million, or 48.7% of total net revenues for the three months ended June 30, 2000.

The cost of license revenues decreased 16.3% to $128,000 for the three months ended June 30, 2001 from $153,000 for the three months ended June 30, 2000. The decrease in the cost of license revenues was primarily due to third party royalties incurred in the second quarter of 2000 from software sales. There were minimal royalties payable to third parties in the second quarter of 2001. This decrease was partially offset by application service provider hosting fees incurred in the second quarter of 2001. There were no application service provider hosting fees in the second quarter of 2000. As a percentage of license revenues, the cost of license revenues increased to 64.6% for the three months ended June 30, 2001 from 11.2% for the three months ended June 30, 2000. The increase in the cost of license revenues as a percentage of license revenues was due to the significant decrease in license revenues in the second quarter of 2001 with only a small reduction in costs, some of which are relatively fixed in nature. The cost of services revenues decreased 9.1% to $3.0 million for the three months ended June 30, 2001 from $3.3 million for the three months ended June 30, 2000. As a percentage of services revenues, the cost of services revenues decreased to 44.1% for the three months ended June 30, 2001 from 57.9% for the three months ended June 30, 2000. The cost of technology consulting and

training service revenues increased 29.0% to $601,000, or 79.6% of technology consulting and training service revenues, for the three months ended June 30, 2001 compared to $466,000, or 42.4% of technology consulting and training service revenues, for the three months ended June 30, 2000. The increase in both the costs of technology consulting and training service revenues and the cost of technology consulting and training service revenues as a percentage of technology consulting and training service revenues was due primarily to additional personnel, subcontracting costs and travel and increased facility and depreciation expenses. The increase in the costs of technology and training service revenues as a percentage of technology consulting and training service revenues was also due to the termination of a two-year consulting contract in December 2000 which accounted for $575,000 of revenue for the second quarter of 2000 at a higher than typical margin. The cost of software maintenance revenues decreased 44.7% to $374,000, or 37.4% of software maintenance revenues, for the three months ended June 30, 2001 compared to $676,000, or 73.3% of software maintenance revenues, for the three months ended June 30, 2000. The decrease in both the cost of software maintenance revenues and the cost of software maintenance revenues as a percentage of software maintenance revenues was due primarily to a reduction in subcontracting costs, recruitment fees and personnel dedicated to software maintenance during the second quarter of 2001. The cost of diagnostic service revenues decreased 4.5% to $2.1 million, or 42.0% of diagnostic service revenues, for the three months ended June 30, 2001 compared to $2.2 million, or 59.5% of diagnostic service revenues, for the three months ended June 30, 2000. The decrease in the cost of diagnostic service revenues was due primarily to a cost control initiative which took effect during the second quarter of 2001. This decrease was partially offset by an increase in variable costs associated with the increase in diagnostic service revenues. The decrease in the cost of diagnostic service revenues as a percentage of diagnostic service revenues was due primarily to the increase in diagnostic service revenues without a comparable increase in costs, many of which are fixed in nature.

Selling and marketing expenses increased 7.7% to $1.4 million, or 20.1% of total net revenues, for the three months ended June 30, 2001 compared to $1.3 million, or 18.1% of total net revenues, for the three months ended June 30, 2000. The increase was primarily due to increased payroll costs associated with expanding the Company's sales force during the fourth quarter of 2000. This increase was partially offset by lower advertising and promotion costs in the second quarter of 2001.

General and administrative expenses decreased 23.5% to $1.3 million, or 18.3% of total net revenues, for the three months ended June 30, 2001 from $1.7 million, or 24.6% of total net revenues, for the three months ended June 30, 2000. The decrease was primarily due to bad debt expense recognized in the second quarter of 2000 that was not recognized in 2001.

Research and development expenses were $1.2 million the three months ended June 30, 2001 and 2000. As a percentage of total net revenues, research and development expenses increased to 17.5% from 16.4%. The increase in research and development expenses as a percentage of total net revenues was primarily due to a decrease in revenue in 2001 without a comparable decrease in costs, many of which are fixed in nature.

Interest income consisted of interest earned on the Company's cash, cash equivalents and short-term investments, and decreased to $243,000 from $382,000 for the three months ended June 30, 2001 and 2000, respectively. The decrease was due to lower cash and short-term investment balances in 2001.

The Company's effective tax rate was 39.9% and 40.0% for the three months ended June 30, 2001 and 2000, respectively.

Six months ended June 30, 2001 compared to six months ended June 30, 2000.

Total net revenues decreased 1.5% to $12.9 million for the six months ended June 30, 2001 compared to $13.1 million for the six months ended June 30, 2000.

License revenues decreased 90.7% to $224,000 for the six months ended June 30, 2001 compared to $2.4 million for the six months ended June 30, 2000. The decrease in license revenues was primarily due to fewer license contract signings in the first and second quarters of 2001. The Company believes the decrease in license contract signings was primarily the result of growing caution in the general business climate and particularly in the technology sector, which has impacted final decisions on new software licenses in 2001. Services revenues increased 16.7% to $12.6 million for the six months ended June 30, 2001 compared to $10.8 million for the six months ended June 30, 2000. Technology consulting and training service revenues decreased 31.8% to $1.5 million for the six months ended June 30, 2001 compared to $2.3 million for the six months ended June 30, 2000. The decrease in technology consulting and training service revenues was due primarily to the termination of a two-year consulting contract in December 2000, which accounted for $1.2 million of revenue in the six months ended June 30, 2000. This decrease was partially offset by additional support revenues from new software installations and increased consulting activity in support of the Company's software and client needs. Software maintenance revenues increased 5.3% to $2.0 million for the six months ended June 30, 2001 compared to $1.9 million for the six months ended June 30, 2000. The increase in software maintenance revenues was due to a larger installed base of software licenses during the six months ended June 30, 2001 compared to the six months ended June 30, 2000. Diagnostic service revenues increased 37.9% to $9.1 million for the six months ended June 30, 2001 compared to $6.6 million for the six months ended June 30, 2000. The increase was primarily due to increased sales volume with both new and existing clients.

Total cost of revenues decreased 3.0% to $6.4 million, or 49.7% of total net revenues, for the six months ended June 30, 2001 compared to $6.6 million, or 50.4% of total net revenues, for the six months ended June 30, 2000.

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The cost of license revenues decreased 2.1% to $234,000 for the six months ended June 30, 2001 from $239,000 for the six months ended June 30, 2000. The decrease in the cost of license revenues was primarily due to third party royalties incurred in the six months ended June 30, 2000 from software sales. There were minimal royalties payable to third parties in the six months ended June 30, 2001. This decrease was partially offset by application service provider hosting fees incurred in the six months ended June 30, 2001. There were no application service provider hosting fees in the six months ended June 30, 2000. As a percentage of license revenues, the cost of license revenues increased to 104.5% for the six months ended June 30, 2001 from 10.1% for the six months ended June 30, 2000. The increase in the cost of license revenues as a percentage of license revenues, was due to the significant decrease in license revenues with only a small reduction in costs, some of which are relatively fixed in nature. The cost of services revenues decreased 3.1% to $6.2 million, or 49.2% of services revenues, for the six months ended June 30, 2001 from $6.4 million, or 59.3% of services revenues, for the six months ended June 30, 2000. The cost of technology consulting and training service revenues increased 9.1% to $1.2 million, or 80.0% of technology consulting and training service revenues, for the six months ended June 30, 2001 compared to $1.1 million, or 50.0% of technology consulting and training services revenues, for the six months ended June 30, 2000. The increase in both the cost of technology consulting and training service revenues and the cost of technology consulting and training service revenues as a percentage of technology consulting and training service revenues was due primarily to additional personnel, subcontracting costs and

travel and increased facility and depreciation expenses. The increase in the costs of technology consulting and training service revenues as a percentage of technology consulting and training service revenues was also due to the termination of a two-year consulting contract in December 2000 that accounted for $1.2 million of revenue in the six months ended June 30, 2000 at a higher than typical margin. The cost of software maintenance revenues decreased 43.2% to $738,000, or 36.9% of software maintenance revenues, for the six months ended June 30, 2001 compared to $1.3 million, or 68.4% of software maintenance revenues, for the six months ended June 30, 2000. The decrease in both the cost of software maintenance revenues and the cost of software maintenance revenues as a percentage of software maintenance revenues was due primarily to a reduction in subcontracting costs, recruiting fees, and personnel dedicated to software maintenance during the six months ended June 30, 2001. The cost of diagnostic service revenues increased 5.0% to $4.2 million for the six months ended June 30, 2001 compared to $4.0 million for the six months ended June 30, 2000. The increase was due primarily to an increase in variable costs associated with the increase in diagnostic service revenues. This increase was partially offset by a cost control initiative which took effect during the second quarter of 2001. As a percentage of diagnostic service revenues, the cost of diagnostic service revenues decreased to 46.2% for the six months ended June 30, 2001 from 60.6% for the six months ended June 30, 2000. The decrease in the cost of diagnostic service revenues as a percentage of diagnostic service revenues was due primarily to the increase in diagnostic service revenues without a comparable increase in costs, many of which are fixed in nature.

Selling and marketing expenses increased 8.0% to $2.7 million, or 21.2% of total net revenues, for the six months ended June 30, 2001 compared to $2.5 million, or 18.8% of total net revenues, for the six months ended June 30, 2000. The increase was primarily due to increased payroll costs associated with expanding the Company's sales force during the fourth quarter of 2000. This increase was partially offset by lower advertising and promotion costs in the six months ended June 30, 2001.

General and administrative expenses decreased 21.2% to $2.6 million, or 20.2% of total net revenues, for the six months ended June 30, 2001 from $3.3 million, or 24.9% of total net revenues, for the six months ended June 30, 2000. The decrease was primarily due to bad debt expense recognized in 2000 that was not recognized in 2001 and a decrease in professional fees in the six months ended June 30, 2001.

Research and development expenses increased 25.0% to $2.5 million, or 19.2% of total net revenues, for the six months ended June 30, 2001 from $2.0 million, or 14.9% of total net revenues, for the six months ended June 30, 2000. The Company has increased its investment in research related activities to implement its new business model during the first quarter of 2001, which includes the deployment of its eResNet products and its applications service provider applications. The increase was primarily due to increased payroll, training and facility costs.

The Company recorded an asset impairment charge of $5.0 million in the six months June 30, 2001. This charge was the result of continued negative market conditions affecting the carrying value of the Company's investments in Medical Advisory Systems, Inc. and AmericasDoctor.com, Inc., both of which are Internet based service organizations.

Interest income consisted of interest earned on the Company's cash, cash equivalents and short-term investments, and decreased to $604,000 from $654,000 for the six months ended June 30, 2001 and 2000, respectively. The decrease was due to lower cash and short-term investment balances in 2001.

The Company's effective tax rate was 4.1% and 40.0% for the six months ended June 30, 2001 and 2000, respectively. The decrease in the Company's effective tax rate in 2001 was due primarily to the Company fully reserving for the long-term capital loss deferred tax asset associated with the asset impairment charge of $5.0 million recognized during the first quarter of 2001, due to the uncertainty of the realization of any tax benefit associated with these long-term capital losses in future periods.

Liquidity and Capital Resources

At June 30, 2001, the Company had $13.6 million of cash and cash equivalents and $6.0 million invested in short-term investments. The Company generally places its investments in A1P1 rated commercial bonds and paper, municipal securities and certificates of deposit with maturities of less than one year.

For the six months ended June 30, 2001, the Company's operations provided cash of $865,000 million compared to cash used in operations of $4.3 million for the six months ended June 30, 2000. The change was primarily the result of decreased accounts receivable and changes to other working capital accounts for the six months ended June 30, 2001 compared to the six months ended June 30, 2000.

During the six months ended June 30, 2001, the Company purchased $1.4 million of equipment compared to $1.1 million during the six months ended June 30, 2000. The increase was primarily the result of furniture and equipment purchases for the Company's office expansion in the first quarter of 2001 at its Bridgewater, NJ location, the purchase of diagnostic rental equipment, and the costs associated with the development of a new data and communications management services software product to be used in connection with the Company's centralized core-diagnostic electrocardiographic services.

In January 2001, the Company received $167,000 from an escrow account established under the Company's agreement with SCP in relation to the sale of its domestic clinical research operations, which was recorded as additional gain on sale in the fourth quarter of 2000. In April 2001, the Company received $2.6 million from a related escrow account of which $1.5 million was recorded as additional gain on sale in the fourth quarter of 2000 and $232,000 was recorded as additional gain on sale in the first quarter of 2001. The remaining balance of $893,000 is included in accrued expenses as of June 30, 2001. The Company anticipates the remaining balance will be recognized as additional gain on sale upon finalization of the accounting for the escrow account which is expected to be completed by December 31, 2001.

In March 2000, the Company's wholly-owned subsidiary, eRT Operating Company (eRT OC), sold 95,000 shares of its convertible preferred stock to Communicade, Inc. and agreed to issue a warrant to purchase 2.5% of eRT's outstanding common stock for a total gross proceeds of $9.5 million. The preferred stock would have automatically converted into common stock upon consummation of an eRT OC initial public offering. In March 2000, eRT OC issued a warrant to purchase common stock to Scirex Corporation. The warrant entitles Scirex to purchase the number of common shares equal to $1.0 million divided by eRT OC's initial public offering price per share, at an exercise price per share equal to eRT OC's initial public offering price per share. On March 1, 2001, eRT OC withdrew the registration statement associated with its initial public offering and the Company purchased the convertible preferred stock sold to Communicade, Inc. for the original purchase price of $9.5 million plus $639,000 in accrued dividends. The agreement to issue a warrant to Communicade, Inc. and the warrant issued to Scirex Corporation remain outstanding.

In February 2001, the Board of Directors authorized a stock buy-back program of up to 500,000 shares of the Company's common stock. The share purchase authorization allows the Company to make purchases from time to time on the open market at prevailing prices or in privately negotiated transactions. Company

management will make the purchase decisions based upon market conditions and other considerations. During the six months ending June 30, 2001, the Company used $55,000 to purchase 10,000 shares of its common stock on the open market at an average price of $5.51 per share.

The Company has a line of credit arrangement with First Union National Bank totaling $3.0 million. At June 30, 2001, the Company had no outstanding borrowings under the line.

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The Company expects that existing cash and cash equivalents, short-term investments, marketable securities, cash flows from operations and available borrowings under its line of credit will be sufficient to meet its foreseeable cash needs for at least the next year. However, there may be acquisition and other growth opportunities that require additional external financing and the Company may from time to time seek to obtain additional funds from the public or private issuances of equity or debt securities. There can be no assurance that such financings will be available or available on terms acceptable to the Company.

Inflation

The Company believes the effects of inflation generally do not have a material adverse effect on its results of operations or financial condition.

Item 3. Qualitative and Quantitative Disclosures About Market Risk

There have been no material changes in qualitative and quantitative market risk from the disclosure within the December 31, 2000 Form 10-K which is incorporated here by reference.

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Part II. Other Information

Item 2. Changes in Securities and Use of Proceeds

(1) Effective Date of Securities Act Registration Statement: February 3, 1997
registration No.: 333-17001

(2) Offering Date: February 4, 1997

(3) Not Applicable

(4) (i) The offering terminated after all shares registered were sold

(ii) Managing Underwriters: Montgomery Securities
Furman Selz
Genesis Merchant Group

(iii) Class of Securities Registered: Common Stock

(iv)

	Account of Company	Account of Selling S
Amount Registered	2,206,250 common stock	956,250 common stock

Aggregate price of Amount Registered	$37,506,250	$16,256,250
Amount Sold	2,206,250	956,250
Aggregate Offering Price of Amount Sold	$37,506,250	$16,256,250

(v) Expenses of offering for account of the Company:

Underwriting Discount and Commission	$2,625,437
Other expenses	698,813
Total Expenses	$3,324,250

(A) There were no direct or indirect payments to directors, officers, general partners of the issuer or their associates; to persons owning ten (10) percent or more of common stock of the Company; or affiliates of the Company.

(B) All of the above payments were direct or indirect payments to others not described in clause (A).

(vi) Net Offering Proceeds to the Company: $34,182,000

(vii) Use of Proceeds as of June 30, 2001:

Net cash paid for business acquisition	8,655,000
Net cash paid for minority investments	8,725,000
Purchases of equipment	11,797,000
Net cash paid for repurchase of common stock	2,766,000
Temporary Investments (consisting of short-term, Investment-grade securities)	2,239,000

All of the above payments were to others not described in item (v) (A) above.

(viii) The use of proceeds is consistent with the Prospectus

Item 4. Submission of Matters to a Vote of Security Holders

The Company held its Annual Meeting of Shareholders on April 24, 2001. Matters submitted to the shareholders for vote were the election of three directors to each serve a three-year term until 2004, approval of an amendment to the Company's 1996 Stock Option Plan to reserve an additional 300,000 shares of Common Stock for issuance thereunder, approval of an amendment to the Company's Restated Certificate of Incorporation to change its name to "eResearchTechnology, Inc.", and ratification of the appointment of Arthur Andersen LLP as the Company's independent auditors for the year ending December 31, 2001.

At the meeting, the shareholders elected Sheldon Bonovitz, Arthur H. Hayes, Jr., M.D., and Howard D. Ross to the Board of Directors. Sheldon Bonovitz was elected with 6,137,335 shares voted for the election or 87.5% of the 7,017,887 shares outstanding and eligible to vote with 158,560 shares withheld. Arthur H. Hayes, Jr., M.D. was elected with 6,137,635 shares voted for the election or 87.5% of the 7,017,887 shares outstanding and eligible to vote with 158,260 shares withheld. Howard D. Ross was elected with 6,075,895 shares voted for the election or 86.6% of the 7,017,887 shares outstanding and eligible to vote with 220,000 shares withheld. With their election, they join Joel Morganroth, MD,

Joseph Esposito, James C. Gale, Jerry D. Lee, and John M. Ryan, as Directors of the Company.

The shareholders approved the amendment to the Company's 1996 Stock Option Plan to reserve an additional 300,000 shares of Common Stock for issuance thereunder with 5,923,350 shares voted for approval or 84.4% of the 7,017,887 shares outstanding and eligible to vote with 369,366 shares voted against the amendment and 3,179 shares abstained.

The shareholders approved the amendment to the Company's Restated Certificate of Incorporation to change its name to "eResearchTechnology, Inc." with 6,176,734 shares voted for approval or 88.0% of the 7,017,887 shares outstanding and eligible to vote with 116,227 shares voted against the amendment and 2,934 shares abstained.

In addition, the shareholders ratified the appointment of Arthur Andersen LLP as the Company's independent auditors for 2001 with 6,282,391 shares voting for ratification or 89.5% of the 7,017,887 shares outstanding and eligible to vote with 4,250 votes against ratification and 9,254 shares abstained.

Item 6. Exhibits and Reports on Form 8-K

a.) Exhibits

10.56 Management Employment Agreement effective May 21, 2001 between Dr. Joel Morganroth and the Company

10.57 Management Consulting Agreement effective May 21, 2001 between Dr. Joel Morganroth and the Company

10.58 Letter of Extension for Promissory Note to First Union National Bank (filed herewith)

b.) Reports on Form 8-K

On July 25, 2001, the Company filed a report on Form 8-K relating to financial information for eResearchTechnology, Inc. for the quarter ended June 30, 2001 and forward-looking statements relating to 2001 and the third and fourth quarters of 2001 as presented in a press release of July 25, 2001.

Signatures

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

eResearchTechnology, Inc.

(Registrant)

Date: August 10, 2001 By: /s/ Joseph Esposito

Joseph Esposito
Chief Executive Officer

Date: August 10, 2001 By: /s/ Bruce Johnson

Bruce Johnson
Chief Financial Officer
(Principal Financial and Accounting Officer)