EMTEC INC/NJ
Form 10-Q
February 13, 2002

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For The Quarter Ended
December 31, 2001

Commission file number: 0-32789

EMTEC, INC.
(Exact name of Registrant as specified in charter)

Delaware	87-0273300
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

817 East Gate Drive
Mt. Laurel, New Jersey 08054
(Address of principal executive offices)

(856) 235-2121
(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 [X]   No [ ]

The number of shares of Common Stock outstanding as of February 6, 2002 was 7,080,498.

EMTEC, INC.
FORM 10-Q FOR THE QUARTER ENDED DECEMBER 31, 2001

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

EMTEC, INC.
CONSOLIDATED BALANCE SHEETS

	December 31, 2001 (unaudited)	March 31, 2001
Assets		
Current Assets		
Cash and cash equivalents	$ 143,300	$ 2,098,198
Marketable securities	4,090	292,346
Receivables:		
Trade, less allowance		

for doubtful accounts	10,055,478	12,828,456
Others	323,339	433,580
Inventories, net of reserve	773,928	1,019,715
Prepaid expenses	213,716	296,939
Total Current Assets	11,513,851	16,969,234
Net property and equipment	661,458	919,110
Investment in geothermal power unit	531,508	549,626
Deferred tax asset	16,796	22,996
Other assets	182,249	175,711
Total Assets	$12,905,862	$18,636,677

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

EMTEC, INC.
CONSOLIDATED BALANCE SHEETS

	December 31, 2001 (unaudited)	March 31, 2001
Liabilities and Shareholders' Equity		
Current Liabilities		
Line of credit	$ --	$ 6,535,405
Due to related party	19,000	19,000
Accounts payable	7,423,262	7,284,625
Income taxes payable	2,087	2,087
Customer deposits	--	203,202
Accrued liabilities	1,195,660	1,023,556
Deferred revenue	1,162,051	899,352
Total Current Liabilities	9,802,060	15,967,227
Deferred revenue	810,085	841,922
Total Liabilities	10,612,145	16,809,149

Shareholders' Equity		
Common stock, $.01 par value; 25,000,000 shares authorized; 7,080,498 shares issued and outstanding	70,805	70,805
Additional paid-in capital	2,210,805	2,210,805
Accumulated other comprehensive income (loss)	3,010	(5,458)
Accumulated deficit	9,097	(448,624)
Total Shareholders' Equity	2,293,717	1,827,528
Total Liabilities and Shareholders' Equity	$12,905,862	$18,636,677

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

EMTEC, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2001	2000	2001	2000
Revenues:				
Procurement services	$14,255,967	$16,448,293	$42,959,628	$60,104,5
Service and consulting	6,228,978	4,755,475	14,414,918	10,984,2
Geothermal	45,256	-	134,654	-
Total Revenues	20,530,201	21,203,768	57,509,200	71,088,7
Cost of Revenues:				
Procurement services	12,783,001	14,634,844	38,150,746	53,795,3
Service and consulting	4,958,895	3,949,715	11,359,382	8,768,5
Geothermal	13,262	-	46,769	-
Total Cost of Revenues	17,755,158	18,584,559	49,556,897	62,563,8

Gross Profit:				
Procurement services	1,472,966	1,813,449	4,808,882	6,309,2
Service and consulting	1,270,083	805,760	3,055,536	2,215,6
Geothermal	31,994	-	87,885	-
Total Gross Profit	2,775,043	2,619,209	7,952,303	8,524,8
Operating Expenses:				
Selling, general and administrative	2,564,068	2,530,717	6,781,684	7,569,9
Termination costs	-	239,285	-	291,2
Interest	36,347	206,217	204,093	540,9
Startup costs, E-Business	145,248	368,477	502,605	909,3
Total Operating Expenses	2,745,663	3,344,696	7,488,382	9,311,5
Income (Loss) From Continuing Operations Before Litigation Settlements And Income Tax Expense	29,380	(725,487)	463,921	(786,6
Litigation settlements	-	(18,801)	-	175,1
Income tax expense	-	-	6,200	-
Income (Loss) From Continuing Operations, Net of Income Taxes	29,380	(744,288)	457,721	(611,5
Loss from discontinued operations, net of income taxes	-	(15,812)	-	(63,9
Net Income (Loss)	$ 29,380	$ (760,100)	$ 457,721	$ (675,4
Income (Loss) Per Share From Continuing Operations (Basic And Diluted)	$.00	$(.14)	$.06	$(.11
Net Income (Loss) Per Share (Basic And Diluted)	$.00	$(.14)	$.06	$(.13
Weighted Average Number Of Shares Outstanding (Basic And Diluted)	7,080,498	5,329,501	7,080,498	5,329,5

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

EMTEC, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Nine Months Ended December 31, 2001	Nine Months Ended December 31, 2000
Cash Flows From Operating Activities		
Net income (loss) for the nine months	$ 457,721	$ (675,475)
Adjustments to Reconcile Net Income To Net Cash Provided By (Used In) Operating Activities:		
Depreciation and amortization	386,075	297,080
Deferred income taxes	6,200	
Unrealized gain on marketable securities	8,476	
Changes In Operating Assets and Liabilities		
Decrease (increase) in marketable securities	288,256	(6,063)
Decrease in receivables	2,883,219	1,816,307
Decrease (increase) in inventories	245,787	(418,390)
Decrease in prepaid expenses	83,223	144,301
Decrease (increase) in other assets	2,364	(3,413)
Increase (decrease) in accounts payable	138,637	(2,333,802)
Decrease in customer deposits	(203,206)	(358,000)
Increase (decrease) in accrued liabilities	172,104	(67,658)
Increase (decrease) in deferred revenue	230,862	(76,784)
Net Cash Provided By (Used In) Operating Activities	4,699,718	(1,681,897)
Cash Flows Used In Investing Activities		
Purchases of equipment	(99,211)	(170,099)
Additional security deposit	(20,000)	--
	(119,211)	(170,099)
Cash Flows Used In Financing Activities		
Net decrease in line of credit	(6,535,405)	(1,664,525)
Net Decrease in Cash and Cash Equivalents	(1,954,898)	(3,516,521)
Beginning Cash and Cash Equivalents	2,098,198	686,413
Ending Cash and Cash Equivalents	$ 143,300	$(2,830,108)

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

EMTEC, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
NINE MONTHS ENDED DECEMBER 31, 2001 AND 2000

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and note disclosures required by generally accepted accounting principles in the United States. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Quarterly results are not necessarily indicative of results for the full year. For further information, refer to the annual financial statements and notes thereto included in the Company's Form 10-K.

2. Stock-Based Compensation

Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," (SFAS No. 123) encourages, but does not require companies to record compensation cost for stock-based employee compensation plans at fair value. The Company has adopted Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB No. 25). APB No. 25 provides that the compensation expense relative to the Company's employee stock options is measured based on the intrinsic value of the stock option. SFAS No. 123 requires companies that continue to follow APB No. 25 to provide a pro forma disclosure of the impact of applying the fair value method of SFAS No. 123.

All stock options granted for the nine months ended December 31, 2001 and 2000 were determined to have a fair value of zero. The exercise price of these options were set at amounts in excess of 150% of the fair value of the underlying stock. Therefore, no options granted have been exercised during the nine months ended December 31, 2001 and 2000. A pro forma presentation of compensation cost and earnings per share is not required due to the zero fair value determination. Option activity is summarized in the following table:

Options outstanding - April 1, 2001	465,259
Activity for the nine months ended December 31, 2001:	

Options granted	82,746
Options exercised	0
Options forfeited or expired	(166,677)
Options outstanding - December 31, 2001	381,328

3. Net Income (Loss) per Share

Computations of net income (loss) per share and the income (loss) per share from continuing operations have been made in accordance with Statement of Financial Accounting Standards No. 128 "Earnings Per Share" (SFAS No. 128). These per share computations use the weighted average number of shares outstanding during the period. SFAS No. 128 requires a separate presentation of diluted income per share from continuing operations and diluted net income per share for the potential dilutive effect of securities such as stock options. The Company maintains a stock option plan as discussed in Note 2. The pricing of the options were in excess of the underlying value of the Company stock during the Nine months ended December 31, 2001 and 2000, therefore, the stock options are antidilutive.

4. Line of Credit

On November 21, 2001, the Company entered into a $10.0 million revolving credit facility with Fleet Capital Corporation, formerly Summit Business Capital Corporation ("Fleet") whereas the Company may borrow on 85% of its eligible trade receivables. The Company simultaneously terminated its prior financing agreement with IBM Credit Corporation ("IBM") by paying IBM an aggregate of $2,270,636. Interest on outstanding loans under the revolving credit facility with Fleet is charged monthly at a fluctuating rate per annum equal to 0.25% above the prime rate and, at our option, interest on up to 50% of the outstanding loans may be charged at libor plus 2.75%. The Fleet revolving credit facility is collateralized by a lien upon and security interest in substantially all of the Company assets. Since current credit facilities with two of the Company's primary trade vendors, (GE Access, and Ingram Micro.,) were also collateralized by substantially all Company assets, Fleet, GE Access and Ingram Micro, have entered into intercreditor agreements, which provide that as regards to these vendors, debt obligations to Fleet are accorded priority. The credit facility agreement with Fleet contains financial covenants. At December 31, 2001, the Company was in compliance with all of its covenants and had no outstanding balance under the credit facility with Fleet.

5. Subsequent Events

On January 9, 2002, the Company acquired substantially all of the assets of Devise Associates, Inc., an information technology consulting and managed services organization located in New York City. The Company paid an aggregate price of $355,051 in cash to be allocated as follows:

$200,000	Goodwill
152,220	Equipment
2,831	Prepaid Expenses

$355,051	Aggregate purchase price
========	

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

The following discussion and analysis should be read in conjunction with, and is qualified in its entirety by, the unaudited financial statements, including the notes thereto, appearing elsewhere in this quarterly report, 10-Q.

A. Results of Operations

a) Three Months Ended December 31, 2001 Compared to Three Months Ended December 31, 2000.

(1) Total Revenues

Total revenues from the IT business decreased by 3.39%, or $718,823, to $20.48 million for the three months ended December 31, 2001. Services and consulting revenue increased by 30.99%, or $1.47 million, to $6.23 million for the three months ended December 31, 2001 compared to $4.76 million for the three months ended December 31, 2000. This increase is attributable to $1.50 million increase in our third party service contract revenues. Product procurement revenues decreased by 13.33%, or $2.19 million, to $14.25 million for the three months ended December 31, 2001. This decline in product procurement revenues is mainly due to our greater emphasis on our services and consulting organization as well as a slow-down in the economy.

Geothermal revenues of $45,256 for the three months ended December 31, 2001 are consistent with the previous period's revenues for a comparable period.

(2) Gross Profit

Our aggregate gross profit from the IT business increased by 4.73%, or $123,840, to $2.74 million for the three months ended December 31, 2001. This increase is mainly attributable to 30.99% increase in our service and consulting revenues. Also, measured as a percentage of net sales, our overall gross profit margin increased to 13.39% for the three months ended December 31, 2001 from 12.35% for the three months ended December 31, 2000. This increase is also due to higher services and consulting revenues.

Gross profit margin attributable to product sales decreased to 10.33% for the three months ended December 31, 2001 from 11.03% for the three months ended December 31, 2000. This decrease in product procurement gross margin is because of the higher competition in the marketplace and a slow-down in the economy. Gross margin attributable to services and consulting revenue increased to 20.39% for the three months ended December 31, 2001 from 16.94% for the three months ended December 31, 2000. Again, this increase is mainly due to higher services and consulting revenues.

The geothermal gross profit of $31,994 for the three months ended December 31, 2001 is consistent with the gross profit for comparable previous periods.

(3) Sales, General, and Administrative Expenses

Sales, general, and administrative expenses increased by 1.32%, or $33,351, to $2.56 million for the three months ended December 31, 2001 from $2.53 million for the three months ended December 31, 2000. This increase is primarily due to higher sales commission expenses for service and consulting revenues for the three months ended December 31, 2001.

(4) Interest Expense

Interest expense decreased by 82.37%, or $169,870 to $36,347 for the three months ended December 31, 2001 from $206,217 for the three months ended December 31, 2000. This decrease is primarily a result of lower sales volume and lower interest rates as well as our continued efforts to streamline our accounts receivable credit policies and collection functions.

(5) Startup Costs; e-Business

Startup Costs; e-Business for the three months ended December 31, 2001 was $145,248, compared to $368,477 for the three months ended December 31, 2000. This decrease is primarily due to: 1) lower head count within the group; and 2) generation of $42,663 revenue from e-Business activities during three months ended December 31, 2001 as compared to $8,750 from three months ended December 31, 2000.

(6) Income Taxes

Income Tax expense was $0, and $0 for the three months ended December 31, 2001 and 2000, respectively, because of the loss carry forward.

b) Nine months Ended December 31, 2001 Compared to Nine months Ended December 31, 2000.

(1) Total Revenues

Total revenues from the IT business decreased by 19.29%, or $13.71 million, to $57.37 million for the nine months ended December 31, 2001. Services and consulting revenue increased by 31.23%, or $3.43 million, to $14.14 million for the nine months ended December 31, 2001 compared to $10.98 million for the nine months ended December 31, 2000. This increase is attributable to $3.43 million increase in our third party service contract revenues. Product procurement revenues decreased by 28.53%, or $17.14 million, to $42.96 million for the nine months ended December 31, 2001. This decline in product procurement revenues is mainly due to the continued focus on our services and consulting organization as well as a slow-down in the economy.

Geothermal Revenues of $134,654 for the nine months ended December 31, 2001 are consistent with the previous period's revenues for a comparable period.

(2) Gross Profit

Our aggregate gross profit from the IT business declined by 7.75%, or $660,461, to $7.86 million for the nine months ended December 31, 2001. This decrease is mainly due to lower product procurement revenues. Measured as a percentage of net sales, our overall gross profit margin increased to 13.71% for the nine months ended December 31, 2001 from 11.99% for the nine months ended December 31, 2000.

Gross profit margin attributable to product sales increased to 11.19% for the nine months ended December 31, 2001 from 10.50% for the nine months ended December 31, 2000. This increase in product procurement gross margin is attributable to lower cost of products obtained from our vendors as well as lower inventory write-offs during this period. Gross margin attributable to services and consulting revenue increased to 21.20% of services and consulting revenue for the nine months ended December 31, 2001 from 20.17% for the nine months ended December 31, 2000. This increase is mainly due to higher services and consulting revenues

The geothermal gross profit of $87,885 for the nine months ended December 31, 2001 is consistent with the gross profit for comparable previous periods.

(3) Sales, General, and Administrative Expenses

Sales, general, and administrative expenses decreased by 10.41%, or $788,286, to $6.78 million for the nine months ended December 31, 2001 from $7.57 million for the nine months ended December 31, 2000. This decrease is primarily a result of lower sales commission expenses as well as our continued efforts to streamline many of our sales and operational functions.

(4) Interest Expense

Interest expense decreased by 62.27%, or $336,893 to $204,093 for the nine months ended December 31, 2001 from $540,986 for the nine months ended December 31, 2000. This decrease is primarily a result of lower sales volume and lower interest rates as well as our continued efforts to streamline our accounts receivable credit policies and collection functions.

(5) Startup Costs; e-Business

Startup Costs; e-Business for the nine months ended December 31, 2001 was $502,605, compared to $909,308 for the nine months ended December 31, 2000. This decrease is primarily due to: 1) lower head count within the group; 2) generation of $155,782 revenue from e-Business activities during nine months ended December 31, 2001 as compared to $8,750 from nine months ended December 31, 2000.

(6) Income Taxes

Income Tax expense was $6200 and $0 for the nine months ended December 31, 2001 and 2000, respectively, because of the loss carry forward.

Recently Issued Accounting Standards

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin ("SAB") No. 101 "Revenue Recognition in Financial Statements." This SAB summarizes certain of the SEC staff's views in applying generally accepted accounting principles to revenue recognition in financial statements. Adoption of SAB No. 101 did not have a material effect on the Company's results of operations.

In July 2001, the Financial Accounting Standard Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 141, "Business Combinations," which supersedes Accounting Principles Board (APB) Opinion No. 16. SFAS No. 141 requires all business combinations initiated after June 30, 2001 be accounted for under the purchase method. In addition, SFAS No. 141 establishes criteria for the recognition of intangible assets separately from goodwill. The Company does not expect the adoption of SFAS No. 141 will have a material effect on the Company's results of operations, financial position or cash flow.

Also in July 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets," which supersedes APB Opinion No. 17. Under SFAS No. 142 goodwill and indefinite lived intangible assets will no longer be amortized, but rather will be tested for impairment at least annually. In addition, the amortization period of intangible assets with finite lives will no longer be limited to 40 years. SFAS No. 142 is effective for fiscal years beginning after December 15, 2001, which for the Company means the standard will be adopted on April 1, 2002. The Company is currently assessing the impact of SFAS No. 142 on its results of operations.

B. Liquidity and Capital Resources

Cash and cash equivalents at December 31, 2001 of $143,300 decreased by $1,954,898, from $2,098,198 at March 31, 2001. We are a net borrower; consequently, we believe our cash and cash equivalents balance must be viewed along with available balance on our line of credit.

Since our inception, we have funded our operations primarily from borrowings under our credit facility. On November 21, 2001, we entered into a $10.0 million revolving credit facility with Fleet Capital Corporation, formerly Summit Business Capital Corporation ("Fleet"). We simultaneously terminated our prior financing agreement with IBM Credit Corporation ("IBM") by paying IBM an aggregate of $2,270,636. Interest on outstanding loans under our revolving credit facility with Fleet is charged monthly at a fluctuating rate per annum equal to 0.25% above the Prime Rate and, at our option, interest on up to 50% of the outstanding loans may be charged at LIBOR plus 2.75%. Our Fleet revolving credit facility is collateralized by a lien upon and security interest in substantially all of our assets. As our current credit facilities with two of our primary trade vendors, GE Access, and Ingram Micro, were also collateralized by substantially all of our assets, we, Fleet, GE Access and Ingram Micro, have entered into intercreditor agreements, which provide that as regards to these vendors, our obligations to Fleet are accorded priority. At December 31, 2001, we had no outstanding balance under the credit facility with Fleet.

At December 31, our credit facilities with primary trade vendors such as GE Access, Ingram Micro, and Tech Data were as follows: 1) Credit Line with GE Access was $4.5 million, no interest charged, and an outstanding balance of $4.48 million. 2) Credit line with Ingram Micro was $1.5 million, an 18% APR interest rate and an outstanding balance of $398,791. 3) Credit line with Tech Data was $1.5 million, no interest charged and an outstanding balance of $737,645. Under these credit lines we are obligated to pay each invoice within 30 days from the date of such invoice.

Capital expenditures of $99,000 during nine months ended December 31, 2001, were primarily for the purchase of computer equipment for internal use.

We believe that our available funds, together with existing and anticipated credit facilities, will be adequate to satisfy our current and planned operations for at least the next 12 months.

Item 3. Quantitative and Qualitative Information About Market Risk

We do not engage in trading market risk sensitive instruments and do not purchase hedging instruments or "other than trading" instruments that are likely to expose us to market risk, whether interest rate, foreign currency exchange, commodity price or equity price risk. We have issued no debt instruments, entered into no forward or future contracts, purchased no options and entered into no swaps. Our primary market risk exposures are those of interest rate fluctuations. A change in interest rates would affect the rate at which we could borrow funds under our revolving credit facility. Our average balance on the line of credit for the last nine months has been approximately $3.40 million. Assuming no material increase or decrease in such balance, a one percent change in the interest rate would change our interest expense by approximately $34,000 annually.

PART II- OTHER INFORMATION

Item 3. Exhibits and Reports on Form 8-K

Reports on Form 8-K

On December 20, 2001, the Company filed with the Commission a current report on Form 8-K reporting an event under Item 2 - Acquisition or Disposition of Assets.

On November 27, 2001, the Company filed with the Commission a current report on Form 8-K reporting an event under Item 5-Other Events.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized

EMTEC, INC.

By: /s/ JOHN P. HOWLETT
John P. Howlett
Chairman, President, and Chief
Executive Officer
(Principal Executive Officer)

By: /s/ SAM BHATT
Sam Bhatt
Vice President - Finance and Operations
(Principal Financial and
Accounting Officer)

Date: February 13, 2002