

NETZEE INC  
Form 10-Q  
August 14, 2002

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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**Form 10-Q**

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2002**

**Or**

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF  
1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ to \_\_\_\_\_, 20 \_\_\_\_\_.**

**Commission file number: 0-27925**

**Netzee, Inc.**

*(Exact name of registrant as specified in its charter)*

**Georgia**

*(State or other jurisdiction of  
incorporation or organization)*

**58-2488883**

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

**6190 Powers Ferry Road, Suite 400, Atlanta, Georgia 30339**

*(Address of principal executive offices)*

**(770) 850-4000**

*(Registrant's telephone number including area code)*

**N/A**

*(Former name, former address and former 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. Yes ☒ No ☐

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. As of August 12, 2002, there were 3,378,439 shares of the Registrant's Common Stock outstanding.

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CONSOLIDATED BALANCE SHEETS**

	<b>December 31, 2001</b>	<b>June 30, 2002</b>
		<b>(Unaudited)</b>
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 464,889	\$ 1,255,899
Restricted cash	325,000	435,000
Accounts receivable, net of allowance for doubtful accounts of \$375,202 and \$275,669, at December 31, 2001 and June 30, 2002, respectively	2,708,227	1,348,401
Leases receivable, current portion	630,083	506,978
Prepaid and other current assets	1,091,442	1,026,305
	<hr/>	<hr/>
Total current assets	5,219,641	4,572,583
Property and equipment, net of accumulated depreciation of \$3,007,404 and \$3,810,105, at December 31, 2001 and June 30, 2002, respectively	4,315,900	3,939,349
Intangible assets, net of accumulated amortization of \$50,028,727 and \$60,556,615, at December 31, 2001 and June 30, 2002, respectively	22,261,157	9,953,269
Leases receivable, net of current portion	638,267	421,224
Other non-current assets	65,607	
	<hr/>	<hr/>
<b>Total assets</b>	<b>\$ 32,500,572</b>	<b>\$ 18,886,425</b>
	<hr/>	<hr/>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)</b>		
<b>Current liabilities:</b>		
Accounts payable	\$ 1,303,835	\$ 454,116
Accrued liabilities	1,354,045	747,089
Deferred revenue	2,697,894	2,266,078
Redeemable preferred stock and accrued dividends, current portion	1,039,996	7,800,000
Related-party borrowings, current portion		14,037,179
	<hr/>	<hr/>
Total current liabilities	6,395,770	25,304,462
Related-party borrowings, net of current portion	13,191,715	
Deferred revenue, net of current portion	1,180,780	975,825
	<hr/>	<hr/>
Total liabilities	20,768,265	26,280,287
<b>Commitments and contingencies</b>		
Redeemable preferred stock, no par value; 5,000,000 shares authorized:		
8% convertible preferred stock, \$13 stated value; 500,000 shares authorized, issued and outstanding at December 31, 2001 and June 30, 2002	6,500,000	
<b>Shareholders' equity (deficit):</b>		
Common stock, no par value; 70,000,000 shares authorized at December 31, 2001 and June 30, 2002, 3,377,911 and 3,378,439 shares issued and outstanding at December 31, 2001 and June 30,	190,555,255	190,173,047

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2002, respectively		
Notes receivable from shareholders	(579,486)	(535,100)
Deferred stock compensation	(629,234)	(92,294)
Accumulated deficit	(184,114,228)	(196,939,515)
	<u>                    </u>	<u>                    </u>
Total shareholders' equity (deficit)	5,232,307	(7,393,862)
	<u>                    </u>	<u>                    </u>
<b>Total liabilities and shareholders' equity (deficit)</b>	<b>\$ 32,500,572</b>	<b>\$ 18,886,425</b>
	<u>                    </u>	<u>                    </u>

The accompanying notes are an integral part of these balance sheets.

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**NETZEE, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

	Three Months Ended		Six Months Ended	
	June 30, 2001	June 30, 2002	June 30, 2001	June 30, 2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
<b>Revenues:</b>				
Monthly maintenance and service	\$ 5,874,522	\$ 3,975,057	\$ 12,795,573	\$ 8,462,502
License, hardware, implementation and other	475,018	465,473	1,022,433	737,453
Total revenues	6,349,540	4,440,530	13,818,006	9,199,955
<b>Operating expenses:</b>				
Cost of services, license, hardware, implementation and maintenance	3,747,239	1,633,523	8,131,204	3,412,301
Selling and marketing	1,068,110	181,285	2,369,704	375,825
General and administrative, excluding amortization of stock-based compensation and restructuring costs	3,334,233	1,733,652	6,837,365	3,988,713
Amortization of stock-based compensation	248,054	66,154	728,187	154,722
Depreciation	484,620	426,681	979,691	966,212
Amortization	8,595,580	5,594,723	18,252,861	11,581,260
Restructuring costs	(323,452)		1,535,193	
(Gain)/loss on sales of assets	(1,213,458)		4,548,750	
Total operating expenses	15,940,926	9,636,018	43,382,955	20,479,033
Operating loss	(9,591,386)	(5,195,488)	(29,564,949)	(11,279,078)
Interest expense, net	(182,713)	(237,248)	(479,567)	(418,102)
Net loss before preferred dividends and cumulative effect of change in accounting principle	(9,774,099)	(5,432,736)	(30,044,516)	(11,697,180)
Cumulative effect of change in accounting principle				(743,065)
Net loss before preferred dividends	(9,774,099)	(5,432,736)	(30,044,516)	(12,440,245)
Preferred stock dividends	(130,000)	(255,042)	(260,000)	(385,042)
Net loss attributable to common shareholders	\$ (9,904,099)	\$ (5,687,778)	\$ (30,304,516)	\$ (12,825,287)
Basic and diluted net loss per share before preferred dividends and cumulative effect of change in accounting principle	\$ (2.92)	\$ (1.61)	\$ (8.97)	\$ (3.46)
Loss per share from cumulative effect of change in accounting principle				(0.22)
Loss per share before preferred dividends	(2.92)	(1.61)	(8.97)	(3.68)
Loss per share from preferred dividends	(0.04)	(0.07)	(0.08)	(0.12)
Net loss per share	\$ (2.96)	\$ (1.68)	\$ (9.05)	\$ (3.80)
Weighted average basic and diluted common shares outstanding	3,342,204	3,378,087	3,349,625	3,377,999

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



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**NETZEE, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Six Months Ended	
	June 30, 2001	June 30, 2002
	(Unaudited)	(Unaudited)
<b>Cash flows from operating activities:</b>		
Net loss before preferred dividends	\$ (30,044,516)	\$ (12,440,245)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Cumulative effect of change in accounting principle		743,065
Depreciation and amortization	19,232,552	12,547,472
Stock-based compensation expense	728,187	154,722
Net loss on sales of assets	4,548,750	
Provision for bad debt	141,174	(10,643)
Interest income on shareholder notes	(31,552)	(16,893)
Changes in assets and liabilities, net of effect of acquisitions and dispositions:		
Accounts receivable	1,049,288	1,370,469
Leases receivable	331,356	340,148
Prepaid and other assets	32,996	625,703
Accounts payable and accrued liabilities	(1,430,321)	(1,456,675)
Deferred revenue	(1,249,242)	(636,771)
Other	(304,154)	(32,430)
<b>Net cash (used in) provided by operating activities</b>	<b>(6,995,482)</b>	<b>1,187,922</b>
<b>Cash flows from investing activities:</b>		
Acquisitions, net of cash acquired	(420,954)	
Purchase of property, equipment and capitalized software	(1,145,674)	(674,441)
Proceeds from sale of assets	15,511,441	96,250
Purchase of short-term investments related to restricted cash	(475,000)	(110,000)
Proceeds from sales of short-term investments related to restricted cash	100,000	
<b>Net cash provided by (used in) investing activities</b>	<b>13,569,813</b>	<b>(688,191)</b>
<b>Cash flows from financing activities:</b>		
Related party borrowings	6,475,335	1,650,000
Payments on related party borrowings	(14,846,706)	(800,000)
Debt extension costs		(620,000)
Repayment of shareholder notes	995,179	61,279
Payments of notes payable	(22,372)	
Proceeds from exercise of options for common stock	71	
<b>Net cash (used in) provided by financing activities</b>	<b>(7,398,493)</b>	<b>291,279</b>
Net (decrease) increase in cash and cash equivalents	(824,162)	791,010
Cash and cash equivalents, beginning of period	960,231	464,889
<b>Cash and cash equivalents, end of period</b>	<b>\$ 136,069</b>	<b>\$ 1,255,899</b>

SUPPLEMENTAL DISCLOSURE OF CASH FLOW  
INFORMATION:

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Cash paid for interest	\$ 871,336	\$ 459,347
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The accompanying notes are an integral part of these consolidated statements.

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**NETZEE, INC. AND SUBSIDIARIES**

**CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. ORGANIZATION AND NATURE OF BUSINESS**

**Overview**

We are a provider of integrated Internet banking products generally to community financial institutions and their customers. We provide a suite of integrated Internet banking products and services and Internet commerce solutions to community financial institutions. This suite provides cost-effective, secure and scalable Internet banking and Internet commerce products that enable financial institutions to offer to their customers a wide array of financial products and services over the Internet in either an in-house or fully outsourced environment. Customers can select from the components of our suite to develop an e-commerce strategy that best suits their business requirements. Included in the suite are full service Internet banking, bill payment, cash management, and Internet commerce services, as well as custom web site design and hosting services, branded portal services, targeted marketing services, access to brokerage services, and implementation and marketing services.

**Formation and Acquisitions**

Direct Access Interactive, Inc. ( "Direct Access" or the "Predecessor" ) was incorporated on October 10, 1996. On March 9, 1999, Direct Access was purchased by InterCept, Inc. ( "InterCept" ). Direct Access was operated as a separate subsidiary of InterCept. On August 6, 1999, Direct Access purchased the remote banking operations of SBS Corporation ( "SBS" ). SBS provided automated technology products and services to community financial institutions nationwide. Direct Access was later merged with and into Netzee, Inc. ( "Netzee" ). On September 3, 1999, we purchased the Internet banking divisions of TIB The Independent BankersBank ( "TIB" ) and The BankersBank (collectively, the "Divisions" ), and we acquired Dyad Corporation and subsidiaries ( "Dyad" ) and Call Me Bill, LLC ( "Call Me Bill" ). Call Me Bill provided 24-hour electronic bill payment services to financial institutions' customers. In November 1999, we completed an initial public offering of our common stock. On December 15, 1999, we purchased DPSC Software, Inc. ( "DPSC" ), which provided regulatory reporting and related software to community financial institutions.

On March 7, 2000, we purchased Digital Visions, Inc. ( "DVI" ), which provided Internet-based information and analytic tools to financial institutions. In July 2000, we acquired Card Plus, Inc., ( "Card Plus" ), which provided outsourced technology consulting and programming services. In November 2000, we acquired the Internet banking and bill payment businesses of John H. Harland Company ( "Harland" ). In March 2001, we acquired the Internet banking assets of HomeCom, Inc. ( "HomeCom" ). We collectively refer to SBS, the Divisions, Dyad, Call Me Bill, DPSC, DVI, Card Plus, the internet banking and bill payment businesses acquired from Harland and the internet banking assets acquired from HomeCom as the "Acquired Operations".

**Dispositions**

On February 2, 2001, we sold to InterCept the regulatory reporting business acquired from DPSC in 1999, and InterCept assumed certain of the related operating liabilities. Effective May 1, 2001, we sold to iPay, LLC ( "iPay" ) certain assets not considered to be part of our core business related to our bill payment operations formerly located in Elizabethtown, Kentucky, and iPay assumed certain of the related operating liabilities. On November 15, 2001, we sold substantially all the assets acquired from DVI to SS&C Technologies, Inc. ( "SS&C" ), and SS&C assumed substantially all the related operating liabilities.

**Significant Accounting Policies**

The accompanying statements have been prepared in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the accompanying unaudited consolidated financial statements reflect all adjustments, which are of a normal recurring nature, to present fairly our financial position,

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results of operations and cash flows at the dates and for the periods presented. Interim results of operations are not necessarily indicative of results to be expected for a 12-month period. The interim financial statements should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2001 as filed with the Securities and Exchange Commission on April 1, 2002.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires us to make certain estimates regarding the reported amounts of revenue, expenses, assets and liabilities, as well as certain contingencies. We evaluate these estimates and the underlying assumptions for reasonableness on an on-going basis. Actual results may vary from these estimates.

The unaudited consolidated financial statements include the accounts of our company and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been elim