

VERAMARK TECHNOLOGIES INC

Form 10-Q

August 13, 2008

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**FORM 10-Q**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**  
**Quarterly Report Under Section 13 or 15 (d)**  
**of the Securities Exchange Act of 1934**  
**For Quarter Ended June 30, 2008**  
**Commission File Number 0-13898**  
**Veramark Technologies, Inc.**  
(Exact name of registrant as specified in its charter)

Delaware

16-1192368

(State or other jurisdiction of Incorporation  
or Organization)

(IRS Employer Identification Number)

3750 Monroe Avenue, Pittsford, NY 14534  
(Address of principal executive offices)(Zip Code)

(585) 381-6000

(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 by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller Reporting  
Company

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

The number of shares of Common Stock, \$.10 par value, outstanding on June 30, 2008 was 9,552,988.

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**Table of Contents****PART I FINANCIAL INFORMATION****VERAMARK TECHNOLOGIES, INC.  
CONDENSED BALANCE SHEETS**

|  | <b>(Unaudited)<br/>June 30,<br/>2008</b> | <b>December 31,<br/>2007</b> |
|--|--|------------------------------|
| <b>ASSETS</b>  |  |                              |
| <b>CURRENT ASSETS:</b>   |  |                              |
| Cash and cash equivalents  | \$ 655,677                               | \$ 713,342                   |
| Investments  | 1,370,371                                | 1,492,288                    |
| Accounts receivable, trade (net of allowance for doubtful accounts of \$32,000 and \$30,000, respectively) | 960,347                                  | 1,303,240                    |
| Inventories, net   | 34,993                                   | 31,764                       |
| Prepaid expenses and other current assets  | 302,772                                  | 254,274                      |
| <b>Total Current Assets</b>  | <b>3,324,160</b>                         | <b>3,794,908</b>             |
| <b>PROPERTY AND EQUIPMENT</b>  |  |                              |
| Cost   | 3,904,673                                | 5,955,064                    |
| Less accumulated depreciation  | (3,408,464)                              | (5,433,650)                  |
| <b>Property and Equipment (Net)</b>  | <b>496,209</b>                           | <b>521,414</b>               |
| <b>OTHER ASSETS:</b>   |  |                              |
| Software development costs (net of accumulated amortization of \$2,729,035 and \$2,179,290, respectively)  | 2,901,489                                | 3,038,410                    |
| Pension assets   | 3,281,189                                | 3,210,204                    |
| Deposits and other assets  | 905,761                                  | 830,756                      |
| <b>Total Other Assets</b>  | <b>7,088,439</b>                         | <b>7,079,370</b>             |
| <b>TOTAL ASSETS</b>  | <b>\$ 10,908,808</b>                     | <b>\$ 11,395,692</b>         |

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

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**VERAMARK TECHNOLOGIES, INC.**  
**CONDENSED BALANCE SHEETS**

|  | <b>(Unaudited)</b><br><b>June 30,</b><br><b>2008</b> | <b>December 31,</b><br><b>2007</b> |
|--|--|------------------------------------|
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>   |  |                                    |
| <b>CURRENT LIABILITIES:</b>  |  |                                    |
| Accounts payable   | \$ 380,852   | \$ 317,127                         |
| Accrued compensation and related taxes   | 723,844  | 934,387                            |
| Deferred revenue   | 3,486,967  | 3,369,324                          |
| Current portion of pension obligation  | 462,059  | 440,084                            |
| Other accrued liabilities  | 194,793  | 270,524                            |
| <br>   |  |                                    |
| Total Current Liabilities  | 5,248,515  | 5,331,446                          |
| <br>   |  |                                    |
| Pension obligation   | 5,027,502  | 5,072,447                          |
| <br>   |  |                                    |
| Total Liabilities  | 10,276,017   | 10,403,893                         |
| <br>   |  |                                    |
| <b>STOCKHOLDERS EQUITY:</b>  |  |                                    |
| Common Stock, par value \$.10; shares authorized, 40,000,000; shares issued and outstanding, 9,633,213 and 9,169,093 | 963,321  | 916,909                            |
| Additional paid-in capital   | 22,240,938   | 22,171,341                         |
| Accumulated deficit  | (22,061,621)   | (21,607,785)                       |
| Treasury stock (80,225 shares, at cost)  | (385,757)  | (385,757)                          |
| Accumulated other comprehensive income   | (124,090)  | (102,909)                          |
| <br>   |  |                                    |
| Total Stockholders Equity  | 632,791  | 991,799                            |
| <br>   |  |                                    |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>   | <b>\$ 10,908,808</b>                                 | <b>\$ 11,395,692</b>               |

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

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**VERAMARK TECHNOLOGIES, INC.**  
**CONDENSED STATEMENTS OF OPERATIONS (Unaudited)**

|   | <b>Three Months Ended<br/>June 30,</b> |                     | <b>Six Months Ended<br/>June 30,</b> |                     |
|---|--|---------------------|--------------------------------------|---------------------|
|   | <b>2008</b>                            | <b>2007</b>         | <b>2008</b>                          | <b>2007</b>         |
| <b>NET SALES</b>                          |  |                     |                                      |                     |
| Product sales                             | \$ 542,661                             | \$ 828,542          | \$ 1,154,161                         | \$ 1,565,016        |
| Service sales                             | 1,995,622                              | 2,219,541           | 4,055,768                            | 4,831,709           |
| <b>Total Net Sales</b>                    | <b>2,538,283</b>                       | <b>3,048,083</b>    | <b>5,209,929</b>                     | <b>6,396,725</b>    |
| <b>COSTS AND OPERATING EXPENSES:</b>      |  |                     |                                      |                     |
| Cost of sales                             | 707,944                                | 749,835             | 1,422,907                            | 1,737,779           |
| Engineering and software development      | 334,243                                | 296,500             | 632,101                              | 547,447             |
| Selling, general and administrative       | 1,771,230                              | 2,334,527           | 3,642,903                            | 4,339,018           |
| <b>Total Costs and Operating Expenses</b> | <b>2,813,417</b>                       | <b>3,380,862</b>    | <b>5,697,911</b>                     | <b>6,624,244</b>    |
| <b>LOSS FROM OPERATIONS</b>               | <b>(275,134)</b>                       | <b>(332,779)</b>    | <b>(487,982)</b>                     | <b>(227,519)</b>    |
| <b>NET INTEREST INCOME</b>                | <b>15,425</b>                          | <b>12,635</b>       | <b>34,146</b>                        | <b>24,887</b>       |
| <b>LOSS BEFORE INCOME TAXES</b>           | <b>(259,709)</b>                       | <b>(320,144)</b>    | <b>(453,836)</b>                     | <b>(202,632)</b>    |
| <b>INCOME TAXES</b>                       |  |                     |                                      |                     |
| <b>NET LOSS</b>                           | <b>\$ (259,709)</b>                    | <b>\$ (320,144)</b> | <b>\$ (453,836)</b>                  | <b>\$ (202,632)</b> |
| <b>NET LOSS PER SHARE</b>                 |  |                     |                                      |                     |
| Basic                                     | \$ (0.03)                              | \$ (0.03)           | \$ (0.05)                            | \$ (0.02)           |
| Diluted                                   | \$ (0.03)                              | \$ (0.03)           | \$ (0.05)                            | \$ (0.02)           |

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

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**VERAMARK TECHNOLOGIES, INC.**  
**CONDENSED STATEMENTS OF CASH FLOWS (Unaudited)**

|   | <b>Six Months Ended</b> |                  |
|---|-------------------------|------------------|
|   | <b>June 30,</b>         |                  |
|   | <b>2008</b>             | <b>2007</b>      |
| <b>OPERATING ACTIVITIES:</b>  |                         |                  |
| Net income (loss)   | (453,836)               | (202,632)        |
| Adjustments to reconcile net income (loss) to net cash flows provided by operating activities |                         |                  |
| Depreciation and amortization   | 690,427                 | 571,403          |
| Bad debt expense  | 3,332                   | 4,470            |
| Share based compensation expense  | 47,116                  | 282,000          |
| Pension assets  | (70,985)                | (70,985)         |
| Loss on disposal of fixed assets  | 14,571                  |                  |
| Unrealized gain on sale of investments  | 7,068                   |                  |
| Changes in assets and liabilities   |                         |                  |
| Accounts receivable   | 339,561                 | 147,864          |
| Inventories   | (3,229)                 | 3,053            |
| Prepaid expenses and other current assets   | (48,498)                | (23,276)         |
| Deposits and other assets   | (75,005)                | (42,222)         |
| Accounts payable  | 63,725                  | (85,788)         |
| Accrued compensation and related taxes  | (210,543)               | 143,218          |
| Deferred revenue  | 117,643                 | 78,518           |
| Other accrued liabilities   | (75,731)                | (31,021)         |
| Pension obligation  | (51,219)                | 222,133          |
| Net cash flows provided by operating activities   | 294,397                 | 996,735          |
| <b>INVESTING ACTIVITIES:</b>  |                         |                  |
| Sale (purchase) of investments  | 121,917                 | (727,143)        |
| Capitalized software development costs  | (412,824)               | (524,847)        |
| Additions to property and equipment   | (130,048)               | (40,437)         |
| Net cash flows used by investing activities:  | (420,955)               | (1,292,427)      |
| <b>FINANCING ACTIVITY:</b>  |                         |                  |
| Exercise of stock options   | 57,150                  | 43,710           |
| Proceeds from employee stock purchase plan  | 11,743                  | 7,041            |
| Net cash flows provided by financing activities   | 68,893                  | 50,751           |
| <b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>  | <b>(57,665)</b>         | <b>(244,941)</b> |
| <b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>   | <b>713,342</b>          | <b>845,384</b>   |

|  |            |            |
|--|------------|------------|
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 655,677 | \$ 600,443 |
|--|------------|------------|

SUPPLEMENTAL CASH FLOW INFORMATION

Cash Transactions:

|                        |          |          |
|------------------------|----------|----------|
| Income taxes paid, net | \$ 7,725 | \$ 1,859 |
| Interest paid          | \$ 874   | \$ 575   |

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



**Table of Contents****NOTES TO CONDENSED FINANCIAL STATEMENTS**

(Unaudited)

**(1) GENERAL**

The accompanying unaudited financial statements include all adjustments of a normal and recurring nature which, in the opinion of Company's management, are necessary to present fairly the Company's financial position as of June 30, 2008, the results of its operations for the three and six months ended June 30, 2008 and 2007, and cash flows for the six months ended June 30, 2008 and 2007.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission. These condensed financial statements should be read in conjunction with the financial statements and related notes contained in the Company's Annual Report on Form 10-K to the Securities and Exchange Commission for the year ended December 31, 2007.

The results of operations and cash flows for the three and six months ended June 30, 2008 are not necessarily indicative of the results to be expected for the full year's operation.

**(2) PROPERTY AND EQUIPMENT**

The major classifications of property and equipment at June 30, 2008, and December 31, 2007 were:

|                                | <b>June 30,<br/>2008</b> | <b>December 31,<br/>2007</b> |
|--------------------------------|--------------------------|------------------------------|
| Machinery and equipment        | \$ 128,390               | \$ 795,905                   |
| Computer hardware and software | 1,348,974                | 2,093,026                    |
| Furniture and fixtures         | 1,041,512                | 1,677,783                    |
| Leasehold improvements         | 1,385,797                | 1,388,350                    |
|                                | <b>\$ 3,904,673</b>      | <b>\$ 5,955,064</b>          |

For the six months ended June 30, 2008, the Company recorded depreciation expense of \$140,682. Depreciation expense for the six months ended June 30, 2007 was \$126,027.

**Table of Contents****(3) STOCK-BASED COMPENSATION**

The Company's share-based compensation consists of restricted stock and stock options, generally vesting over periods ranging from one to four years. For the six months ended June 30, 2008, the company awarded restricted stock grants totaling 320,000 shares vesting over three years and 134,500 stock options generally vesting over four years. During the first six months of 2007 the Company granted 432,485 stock options to employees.

A summary of the status of the Company's stock option plan as of June 30, 2008 is presented below:

|   | Shares    | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Grant-Date<br>Fair Value | Remaining<br>Contractual<br>Term (Yrs) | Intrinsic<br>Value |
|---|-----------|--|---|--|--------------------|
| Outstanding as of December 31,<br>2007  | 2,257,943 | \$ 1.60                                  | \$ 1.32   | 5.1                                    | \$ 548,550         |
| Granted                                 | 134,500   | \$ 0.65                                  |   |  |                    |
| Exercised                               | (119,000) | 0.48                                     |   |  | (10,150)           |
| Canceled                                | (302,840) | 2.91                                     |   |  | (138,722)          |
| Outstanding as of June 30, 2008         | 1,970,603 | \$ 1.40                                  | \$ 1.16   | 5.1                                    | \$ 399,678         |
| Options exercisable at June 30,<br>2008 | 1,833,303 | \$ 1.45                                  | \$ 1.21   | 4.8                                    | \$ 399,117         |

As of June 30, 2008, there was \$65,895 of total unrecognized compensation cost related to non-vested stock options granted under the Plan and \$203,667 of unrecognized compensation cost related to non-vested restricted stock grants. The compensation cost for stock options will be recognized over a weighted-average period of 1.9 years. The compensation costs of restricted stock will be recognized over a weighted-average period of 1.4 years.

**(4) TOTAL COMPREHENSIVE INCOME (LOSS)**

Total comprehensive income (loss) for the three and six months ended June 30, 2008 and 2007 was as follows:

|   | Three Months Ended<br>June 30, |              | Six Months Ended<br>June 30, |              |
|---|--------------------------------|--------------|------------------------------|--------------|
|   | 2008                           | 2007         | 2008                         | 2007         |
| Net loss                                      | \$ (259,709)                   | \$ (320,144) | \$ (453,836)                 | \$ (202,632) |
| Reclassification to net periodic benefit cost | 22,123                         | 31,400       | 44,245                       | 31,400       |
| Unrealized change - pension                   | (36,247)                       |              | (72,494)                     |              |
| Unrealized change on investments              | (33,992)                       | (6,496)      | 7,068                        | (1,123)      |
| Total comprehensive loss                      | \$ (307,825)                   | \$ (295,240) | \$ (475,017)                 | \$ (172,355) |

**Table of Contents****(5) NET INCOME (LOSS) PER SHARE (EPS)**

SFAS 128 Earnings Per Share requires the Company to calculate net income (loss) per share based on basic and diluted net income (loss) per share, as defined. Basic EPS excludes dilution and is computed by dividing net income (loss) by the weighted average number of shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. The dilutive effect of outstanding options issued by the Company are reflected in diluted EPS using the treasury stock method. Under the treasury stock method, options will only have a dilutive effect when the average market price of common stock during the period exceeds the exercise price of the options.

**Calculations of Earnings (Loss) Per Share**

|   | <b>Three Months Ended<br/>June 30,</b> |              | <b>Six Months Ended<br/>June 30,</b> |              |
|---|--|--------------|--------------------------------------|--------------|
|   | <b>2008</b>                            | <b>2007</b>  | <b>2008</b>                          | <b>2007</b>  |
| <b>Basic</b>  |  |              |                                      |              |
| Net Loss  | \$ (259,709)                           | \$ (320,144) | \$ (453,836)                         | \$ (202,632) |
| Weighted average common shares outstanding  | 9,504,989                              | 8,940,855    | 9,425,951                            | 8,897,994    |
| Net loss per common share   | \$ (0.03)                              | \$ (0.03)    | \$ (0.05)                            | \$ (0.02)    |
| <b>Diluted</b>  |  |              |                                      |              |
| Net loss  | \$ (259,709)                           | \$ (320,144) | \$ (453,836)                         | \$ (202,632) |
| Weighted average common shares outstanding  | 9,504,989                              | 8,940,855    | 9,425,951                            | 8,897,994    |
| Additional dilutive effect of stock options and warrants after application of treasury stock method |  |              |                                      |              |
| Weighted average dilutive shares outstanding  | 9,504,989                              | 8,940,855    | 9,425,951                            | 8,897,994    |
| Net loss per common share assuming full obligation  | \$ (0.03)                              | \$ (0.03)    | \$ (0.05)                            | \$ (0.02)    |

There were no dilutive effects of stock options from the three and six months ended June 30, 2008 and 2007, as the effect would have been anti-dilutive due to the net loss incurred.

**(6) INDEMNIFICATION OF CUSTOMERS**

Our agreements with customers generally require us to indemnify the customer against claims that our software infringes third party patent, copyright, trademark or other proprietary rights. Such indemnification obligations are generally limited in a variety of industry-standard respects, including our right to replace an infringing product. As of June 30, 2008 we had not experienced any material losses related to these indemnification obligations and no material claims with respect thereto were outstanding. We do not expect significant claims related to these indemnification obligations, and consequently, we have not established any related reserves.

**Table of Contents****(7) BENEFIT PLANS**

The Company sponsors an employee incentive savings plan under Section 401(k) for all eligible employees. The Company's contributions to the plan are discretionary. There were no contributions to the plan for the three and six months ended June 30, 2008 and 2007.

The Company also sponsors an unfunded Supplemental Executive Retirement Program (SERP), which is a non-qualified plan that provides certain key employees defined pension benefits. Periodic pension expense for the three months and six months ended June 30, 2008 and 2007 consists of the following:

|                                    | Three Months Ended |            | Six Months Ended |            |
|------------------------------------|--------------------|------------|------------------|------------|
|                                    | June 30,           |            | June 30,         |            |
|                                    | 2008               | 2007       | 2008             | 2007       |
| Current Service Cost               | \$ 10,270          | \$ 68,180  | \$ 24,708        | \$ 136,360 |
| Amortization of Prior Service Cost | 22,123             | 15,700     | 44,245           | 31,400     |
| Interest Cost                      | 82,688             | 78,720     | 165,376          | 157,440    |
| Unrealized change                  | (36,247)           |            | (72,494)         |            |
| Pension Expense                    | \$ 78,834          | \$ 162,600 | \$ 161,835       | \$ 325,200 |

The Company paid pension obligations of 114,055 for the six months ended June 30, 2008 and 103,067 for the six months ended June 30, 2007.

The discount rate used in determining the actuarial present value of the projected benefit obligation was 6% for the three and six months ended June 30, 2008 and 2007.

The Company maintains life insurance covering certain key employees under its Supplemental Executive Retirement Program with the Company named as beneficiary. The Company intends to use the death benefits of these policies, as well as loans against the accumulating cash surrender value of the policies, to fund future pension obligations. The total death benefit associated with these policies is \$10.2 million, with an associated accumulated cash surrender value of approximately \$3,281,000 at June 30, 2008. The accumulated cash surrender values of these policies at December 31, 2007 was approximately \$3,210,000.

The projected pension benefits paid or expected to be paid under this plan are as follows, assuming retirement at 65 and a life expectancy of 80 years for all participants:

**Period Ending December 31, Unless Stated Otherwise,**

|              |           |
|--------------|-----------|
| Q1 - Q2 2008 | 114,055   |
| Q3 - Q4 2008 | 326,029   |
| 2009         | 498,192   |
| 2010         | 498,192   |
| 2011         | 468,058   |
| 2012         | 513,842   |
| 2013 - 2016  | 2,717,021 |

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The Company has a contractual obligation to maintain certain health benefits for two of its former executive officers. These benefits are accounted for as Post Retirement Healthcare Benefits, ( PRHB ). Periodic PRHB expensed and paid for the three and six months ended June 30, 2008 and 2007 consists of the following:

|                      | <b>Three Months Ended<br/>June 30,</b> |             | <b>Six Months Ended<br/>June 30,</b> |             |
|----------------------|--|-------------|--------------------------------------|-------------|
|                      | <b>2008</b>                            | <b>2007</b> | <b>2008</b>                          | <b>2007</b> |
| Current Service Cost | \$ 1,892                               | \$ 1,130    | \$ 3,784                             | \$ 2,260    |
| Interest Cost        | 1,521                                  | 620         | 3,042                                | 1,240       |
| <br>                 |  |             |                                      |             |
| PRHB Expense         | \$ 3,413                               | \$ 1,750    | \$ 6,826                             | \$ 3,500    |

The projected PRHB paid or expected to be paid are as follows:

**Period Ending December 31, Unless Stated Otherwise,**

|              |        |
|--------------|--------|
| Q1 - Q2 2008 | 6,826  |
| Q3 - Q4 2008 | 6,826  |
| 2009         | 13,649 |
| 2010         | 13,649 |
| 2011         | 13,649 |
| 2012         | 13,649 |
| 2013 - 2016  | 37,096 |

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

Management's Discussion and Analysis contains statements that are forward-looking. Such statements are identified by the use of words like plans, expects, intends, believes, will, anticipates, estimates and other words having that meaning in conjunction with, among other things, discussions of future operations, financial performance, the Company's strategy for growth, product development, regulatory approvals, market position and expenditures. Forward-looking statements are based on management's expectations as of the date of this report. The Company cannot guarantee that any forward-looking statement will be accurate, although the Company believes that it has been reasonable in its expectations and assumptions. Forward-looking statements are subject to the risks identified in Issues and Risks and elsewhere in this report. Readers are cautioned not to place undue reliance on forward-looking statements and are advised to review the risks identified in Issues and Risks and elsewhere in this report. The Company has no obligation to update forward-looking statements.

**Overview**

Sales of \$2,538,000 for the three months ended June 30, 2008 decreased from sales of \$3,048,000 for the three months ended June 30, 2007. For the six months ended June 30, 2008 sales of \$5,210,000 decreased from sales of \$6,397,000 for the first six months of 2007. The decline in year to date sales results from a non-recurring \$800,000 component of a managed service contract with Sears Holding Corporation (SHC) recorded as revenue in the first quarter of 2007 and approximately \$400,000 of maintenance revenues recognized during the first half of 2007 from the now discontinued Quantum series of products.

For the three months ended June 30, 2008 we incurred a net loss of \$260,000, or \$0.03 per share, which compared with a net loss of \$320,000, for the same quarter of 2007, also representing \$0.03 per share. The net loss for the six months ended June 30, 2008 of \$454,000, or \$0.05 per share, compares with a net loss of \$203,000, or \$0.02 per share, for the first six months of 2007.

Orders booked of \$3,267,000 for the second quarter ended June 30, 2008 increased 33% from orders booked during the first quarter of 2008. Orders booked for the first six months of 2008 of \$5,722,000 increased 6% from orders booked for the first six months of 2007.

In late May, the Company announced the release of the VeraSMART 8.0 Communications Management Suite introducing new international functionality designed to assist multinational organizations in reducing the cost of their global communications networks. The development of VeraSMART 8.0 came in response to requests from the many Fortune 500 corporations currently utilizing VeraSMART products, and is viewed as an essential component of a longer-term strategy to expand our markets beyond North America.

In June Veramark's VeraSMART Communications Management Suite received a 2007 product of the year award from Technology Marketing Corporation (TMC) for excellence in the advancement of voice, data, and /or video communications. This award recognized the VeraSMART solution for its ability to enable organizations to gain control over their telecommunication spend across all telecom expense management processes including: inventory audit and optimization, procurement and provisioning, invoice processing and payment, wireless management, asset and inventory management and call accounting.

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**Sales**

Sales of VeraSMART products and services, though down slightly for the second quarter of 2008 as compared with the same quarter of 2007, increased 11% for the six months ended June 30, 2008 as compared with the first six months of 2007. VeraSMART product and services accounted for 31% of revenues for the six months ended June 30, 2008, up from 23% of total revenues for the six months ended June 30, 2007.

Revenues generated from managed service contracts decreased 25% and 37% respectively, for the three and six months periods ended June 30, 2008 as compared with the same periods of 2007, entirely as a result of the nonrecurring revenues recorded in the first quarter of 2007 associated with the SHC managed service contract referred to in the overview of this report. The recurring portion of revenues associated with managed service contracts, including SHC, increased 34% for the first six months of 2008 from revenues generated for the first six months of 2007. During the second quarter of 2008 Thornton Americas Holding LLC, The Employment Development Division of the State of California and DHL Delivery were added to our portfolio of managed service clients, with revenues from those contracts expected to commence in the third quarter.

Sales of eCAS products and services decreased 8% for the three months ended June 30, 2008 and 14% for the six months ended June 30, 2008 as compared with the same period of 2007. The reduced sales of eCAS continue the trend of lower sales realized from the largest distribution channel for eCAS, Avaya, Inc and its master distribution channels.

**Cost of Sales**

Cost of sales of \$708,000 for the three months ended June 30, 2008 and \$1,423,000 for the six months ended June 30, 2008 decreased 6% and 18% respectively from cost of sales of \$750,000 and \$1,738,000 for the same three and six month periods of 2007. The reduction in cost of sales for both periods as compared with the prior year reflects lower costs associated with the SHC managed service contract for which a third party was utilized to provide certain portions of the contracted services.

Due to lower sales volumes for the three and six months ended June 30, 2008 as compared with the same periods of 2007, year to date gross margin (sales less cost of sales) as a percentage of sales remained unchanged from the prior year, representing 73% of sales.

**Operating Expenses**

Engineering and software development costs, net of software capitalization, of \$334,000 and \$632,000 increased from \$297,000 and \$548,000 for the three and six months ended June 30, 2008 and June 30, 2007, respectively. The increase in net expenses resulted from a reduction in development costs capitalized during the first half of 2008 as compared with the prior year. The chart below displays gross expenditures for engineering and software development, costs capitalized, and the resulting net engineering and software development costs charged to the Statement of Operations for the three and six month periods ended June 2008 and 2007.

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|   | <b>Three Months Ended</b> |             | <b>Six Months Ended</b> |              |
|---|---------------------------|-------------|-------------------------|--------------|
|   | <b>June 30,</b>           |             | <b>June 30,</b>         |              |
|   | <b>2008</b>               | <b>2007</b> | <b>2008</b>             | <b>2007</b>  |
| Gross expenditures for engineering & software development | \$ 547,000                | \$ 518,000  | \$ 1,045,000            | \$ 1,073,000 |
| Less: Software development costs capitalized              | (213,000)                 | (221,000)   | (413,000)               | (525,000)    |
| Net expense for engineering and software                  | \$ 334,000                | \$ 297,000  | \$ 632,000              | \$ 548,000   |

Selling, general and administrative (SG&A) expense for the three months ended June 30, 2008 of \$1,771,000 decreased 24% from SG&A expenses of \$2,335,000 for the same three months of 2007. For the six months ended June 30, 2008 SG&A expenses of \$3,643,000 decreased 16% from expenses of \$4,339,000 for the first six months of 2007. The significant decrease in expense levels is attributable to two factors. The first has been an aggressive restructuring of all functional areas within the organization which has reduced our direct selling, administrative, and support & service costs while at the same time increasing operating efficiencies. As a result of these efforts, payroll, benefit, and pension costs have been reduced. Secondly, the second quarter of 2007 included approximately \$280,000 of compensation expense associated with a contractual grant of stock options to the Company's former Chief Executive Officer.

**Liquidity and Capital Resources**

Our total cash position (cash on hand plus short-term investments) totaled \$2,026,000 at June 30, 2008, relatively unchanged from the cash position of \$2,049,000 at March 31, 2008. The total cash position at December 31, 2007 was \$2,206,000. During the next two quarters we anticipate a 10-15% decrease in cash balances as we invest in upgrades to our internal infrastructure.

Accounts receivable at June 30, 2008 of \$960,000 declined from accounts receivable of \$1,303,000 at December 31, 2007 due to a combination of lower sales volumes and the timing of payments from customers. The reserve for bad debts at June 30, 2008 is \$32,000, up slightly from a bad debt reserve of \$30,000 at December 31, 2007. The Company continues to experience no customer collection problems of significance.

Prepaid expenses at June 30, 2008 of \$302,000 consisting primarily of the unutilized portion of business insurances and maintenance contracts on specified equipment increased 19% from the December 31, 2007 balance of \$254,000. The increase in prepaid expenses reflect the renewal of business insurance policies, most of which have renewal dates falling in the first half of the year, and an increase in prepaid commissions for orders received in the second quarter that will be recognized as revenue in future periods.

During the second quarter of 2008 capital equipment purchases totaled \$75,000 increasing total capital expenditures to \$130,000 for the six months ended June 30, 2008. Capital spending for the first six months of 2007 totaled \$40,000. During the first six months of 2008 we disposed of \$2,180,000 of capital assets, primarily computer equipment, office furniture and fixtures deemed to be obsolete, or no longer in service. The net residual value of those assets totaled \$15,000 which has been charged against operations.



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At June 30, 2008 the net value of software development costs capitalized and included in the Company's balance sheet is \$2,901,000, a reduction of 5% from capitalized development costs of \$3,038,000 at December 31, 2007. For the six months ended June 30, 2008 we have capitalized \$413,000 of software development costs as compared to \$525,000 for the first six months of 2007. Amortization expense charged to cost of sales for the six months ended June 30, 2008 total \$550,000 versus amortization expense of \$445,000 for the first six months of 2007.

Pension assets, consisting of the cash surrender values of company-owned life insurance contracts designed to fund future pension obligations increased 2% from \$3,210,000 at December 31, 2007 to \$3,281,000 at June 30 2008. These cash surrender values are fully available to support current operating needs if required.

Total current liabilities of \$5,249,000 at June 30, 2008 decreased 2% from the December 31, 2007 total of \$5,331,000 due to a reduction of \$210,000 in accrued compensation costs accrued at the end of 2007 primarily associated with the retirement of the company's former Chief Executive Officer, and a decrease in vacation accruals required. The decrease in accrued compensation costs served to offset a \$64,000 increase in accounts payable and an \$118,000 increase in deferred revenues from December 31, 2007 balances. Deferred revenues consist of the unrecognized portions of orders received from customers for a variety of services including maintenance, training, and implementation services not yet provided, and as such, represent a portion of our total backlog. The majority of the current deferred revenues will be recognized as revenue over the next twelve months.

Stockholders equity at June 30, 2008 is \$633,000 as compared to \$992,000 at December 31, 2007. During the first six months of 2008 employees have exercised 119,000 stock options and purchased 25,120 shares of common stock through the employees stock purchase plan, yielding proceeds to the company of \$69,000.

Given the Company's overall cash position, operating expense levels and absence of debt, it is management's opinion that sufficient resources and liquidity exist to fully fund operations and strategic initiatives for the next twelve months and beyond.

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**Recent Accounting Pronouncements**

- 1) In December 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ( SFAS ) No. 141(R), Business Combinations . SFAS 141(R) establishes principles and requirements for how the acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree, recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141(R) is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. As such, the Company is required to adopt these provisions at the beginning of the fiscal year ending December 31, 2009. The Company does not expect adoption of SFAS 141(R) to have a material effect on its financial statements.
- 2) In December 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ( SFAS ) No. 160, Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51 . SFAS 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. As such, the Company is required to adopt these provisions at the beginning of the fiscal year ending December 31, 2009. The Company does not expect SFAS 160 to have a material effect on its financial statements.
- 3) In December 2007, the SEC issued Staff Accounting Bulletin No. 110 ( SAB 110 ). SAB 110 permits companies to continue to use the simplified method, under certain circumstances, in estimating the expected term of plain vanilla options beyond December 31, 2007. SAB 110 updates guidance provided in SAB 107 that previously stated that the Staff would not expect a company to use the simplified method for share option grants after December 31, 2007. Adoption of SAB 110 did not have a material impact on the Company s financial statements.
- 4) In March 2007, the Financial Accounting Standards Board ratified Emerging Issues Task Force ( EITF ) Issue No. 06-10, Accounting for Collateral Assignment Split-Dollar Life Insurance Agreements . EITF 06-10 provides guidance for determining a liability for the postretirement benefit obligation as well as recognition and measurement of the associated asset on the basis of the terms of the collateral assignment agreement. EITF 06-10 is effective for fiscal years beginning after December 15, 2007. As such, the Company adopted these provisions at the beginning of the fiscal year ending December 31, 2008. Adoption of EITF 06-10 did not have a material impact on the Company s financial statements.

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- 5) In March 2008, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standard ( SFAS ) No. 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133* . SFAS 161 requires enhanced disclosures about an entity s derivative and hedging activities. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008 with early application encouraged. As such, the Company is required to adopt these provisions at the beginning of the fiscal year ended December 31, 2009. The Company is currently evaluating the impact of SFAS 161 on its financial statements, but does not expect it to have a material effect.
- 6) In May 2008, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard ( SFAS ) No. 162, *The Hierarchy of Generally Accepted Accounting Principles* . SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States. SFAS 162 is effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles*. The Company is currently evaluating the impact of SFAS 162 on its financial statements, but does not expect it to have a material effect.
- 7) In May 2008, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standard ( SFAS ) No. 163, *Accounting for Financial Guarantee Insurance Contracts an interpretation of FASB Statement No. 60* ( SFAS 163 ). SFAS 163 interprets Statement 60 and amends existing accounting pronouncements to clarify their application to the financial guarantee insurance contracts included within the scope of that Statement. SFAS 163 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and all interim periods within those fiscal years. As such, the Company is required to adopt these provisions at the beginning of the fiscal year ended December 31, 2009. The Company is currently evaluating the impact of SFAS 163 on its financial statements, but does not expect it to have a material effect.

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**Critical Accounting Policies**

The preparation of financial statements requires management to make estimates and assumptions that affect amounts reported therein. The most significant of these involving difficult or complex judgments include:

- Revenue recognition
- Capitalization of software development costs
- Allowance for Doubtful Accounts
- Pension liability

In each situation, management is required to make estimates about the effects of matters or future events that are inherently uncertain.

The Company's revenue consists of revenues from the licensing of software to resellers and end user customers; fees for services rendered to include installation, training, implementation, and customer maintenance contracts; and the outsourcing or hosting of services.

The Company recognizes software license revenue under Statement of Position No 97-2 Software Revenue Recognition as amended by Statement of Position No. 98-9, Software Revenue Recognition With Respect to Certain Transactions, Emerging Issues Task Force 00-21, Revenue Arrangements with Multiple Deliverables, and related interpretations.

Sales of licensed software sold directly to an end user customer are recognized as revenue upon delivery and installation of the software at the customer site. Sales of licensed software to a reseller are recognized as revenue when delivery is made to the reseller. Regardless of the form of sale no revenue is recognized without persuasive evidence of an arrangement existing. Persuasive evidence is determined to be a signed purchase order received from the customer or an equivalent form for those customers lacking a formalized purchase order system. In the case of VeraSMART sales, a software license agreement signed by both parties is often required in addition to a purchase order or equivalent. Additionally, revenue is only recognized when a selling price is fixed or determinable and collectibility of the receivable is deemed to be probable.

Service revenues such as training, installation and implementation are recognized when the service is complete and acknowledged by the customer, regardless as to whether the sale is on a direct basis or through a reseller arrangement. Fees charged to customers for post-contract Customer Support are recognized ratably over the term of the contract. Costs related to maintenance obligations are expensed as incurred.

Sales which constitute a multiple-element arrangement are accounted for by determining if the elements can be accounted for as separate accounting units, and if so, by applying values to those units for which there is vendor specific objective evidence of their fair value. We use the residual method to apply any remaining balance to the remaining elements of the arrangement. More specifically, this methodology applies when there is embedded maintenance (post-contract customer support) involved in the sale of a software license, or when the sale of a software license is made in conjunction with installation services. In the latter case, the recognition of the software license is deferred until installation is completed.

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The Company's revenues generated through hosting solutions are recognized using the proportional performance method. Revenues are recognized in the month services are rendered and earned under service agreements with clients where service fees are fixed or determinable. Contracts can be terminated with 90 days written notice. All services provided by us through the date of cancellation are due and payable under the contract terms.

The Company believes its revenue recognition policies are appropriate, in all circumstances, and that its policies are reflective of complexities arising from customer arrangements involving such features as maintenance, warranty agreements, license agreements, and other normal course of business arrangements.

The Company capitalizes software development costs when technological feasibility has been established for the software in accordance with SFAS No. 86, Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed. Such capitalized costs are amortized on a product-by-product basis over their economic life or the ratio of current revenues to current and anticipated revenues from such software, whichever provides the greater amortization. The Company periodically reviews the carrying value of capitalized software development costs and impairments are recognized in the results of operations when the expected future undiscounted operating cash flow derived from the capitalized software is less than its carrying value. Should the Company inaccurately determine when a product reaches technological feasibility or the economic life of a product, results could differ materially from those reported. Veramark uses what it believes are reasonable assumptions and where applicable, established valuation techniques in making its estimates.

The Company maintains allowances for doubtful accounts for estimated losses resulting from the potential inability of its customers to make required payments. Management specifically analyzes accounts receivable, historical bad debts, credit concentrations and customer payment terms when evaluating the adequacy of the allowance for doubtful accounts.

The Company sponsors an unfunded Supplemental Executive Retirement Program (SERP), which is a nonqualified plan that provides certain key employees a defined pension benefit. In order to properly record the net present value of future pension obligations a number of assumptions are required to be made by Company's management. These assumptions include years of service, life expectancies, and projected future salary increases for each participant. In addition, management must make assumptions with regard to the proper long-term interest and liability discount rates to be applied to these future obligations.

Should the Company need to alter any of these assumptions, there is the potential for significant adjustments to future projected pension liabilities.

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### **Issues and Risks**

The following factors, among others discussed herein and in the Company's filings under the Act, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements: economic, competitive, governmental and technological factors, increased operating costs, failure to obtain necessary outside financing, risks related to natural disasters and financial market fluctuations. Such factors also include:

#### **Intellectual Property Rights**

Veramark regards its software as proprietary and attempts to protect it with a combination of copyright, trademark and trade secret protections, employee and third-party non-disclosure agreements and other methods of protection. Despite those precautions, it may be possible for unauthorized third parties to copy certain portions of Veramark's products, reverse engineer or obtain and use information that Veramark regards as proprietary. The laws of some foreign countries do not protect Veramark's proprietary rights to the same extent as the laws of the United States. Any misappropriation of Veramark's intellectual property could have a material adverse effect on its business and results of operations. Furthermore, although Veramark takes steps to prevent unlawful infringement of other's intellectual property, there can be no assurance that third parties will not assert infringement claims against Veramark in the future with respect to current or future products. Any such assertion could require Veramark to enter into royalty arrangements or result in costly litigation.

#### **New Products and Services**

Veramark has made significant investments in research, development and marketing for new products, services and technologies, including the VeraSMART® software offering and its service bureau outsourced solutions. Significant revenue from new product and service investments may not be achieved for a number of years, if at all. Moreover, if such products or services are profitable, operating margins may not be as high as the margins historically experienced by Veramark.

#### **Declines in Demand for Software**

If overall market demand for software and computer devices generally, as well as call accounting software or enterprise level products specifically, declines, or corporate spending for such products declines, Veramark's revenue will be adversely affected. Additionally, Veramark's revenues would be unfavorably impacted if customers reduce their purchases of new software products or upgrades to existing products.

#### **Product Development Schedule**

The development of software products is a complex and time-consuming process. New products and enhancements to existing products can require long development and testing periods. Significant delays in new product releases or significant problems in creating new products, particularly any delays in future releases of the VeraSMART® suite of products, could adversely affect Veramark revenues.

#### **Competition**

Veramark experiences intensive competition across all markets for its products and services. Some competing firms have greater name recognition and more financial, marketing and technological resources than Veramark. These competitive pressures may result in decreased sales volumes, price reductions, and/or increased operating costs, such as for marketing and sales incentives, resulting in lower revenues, gross margins and operating income.

#### **Marketing and Sales**

Veramark's marketing and distribution strategy is founded on building mutually beneficial relationships with companies that have established distribution networks. Some sell privately labeled, customized products developed and manufactured by Veramark to their specific specifications, while others resell Veramark's products. Any loss of the continued availability of those relationships could have a material adverse effect on Veramark's business and results of operations.

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**Item 3 Quantitative and Qualitative Disclosures About Market Risk**

The Company has no long-term bank debt obligations. The Company has no foreign currency exchange risk and has no foreign currency exchange contracts.

**Item 4 Controls and Procedures**

Based upon an evaluation as of the end of the period covered by this report, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. There have been no changes in the Company's internal controls over financial reporting, that occurred during the period covered by this report, that have materially affected, or are reasonably likely to materially affect the Company's internal controls over financial reporting.

The Company's disclosure controls and procedures and internal controls over financial reporting provide reasonable, but not absolute, assurance that all deficiencies in design or operation of those control systems, or all instances of errors or fraud, will be prevented or detected. Those control systems are designed to provide reasonable assurance of achieving the goals of those systems in light of the Company's resources and nature of the Company's business operations. The Company's disclosure controls and procedures and internal control over financial reporting remain subject to risks of human error and the risk that controls can be circumvented for wrongful purposes by one or more individuals in management or non-management positions.

**Table of Contents****PART II OTHER INFORMATION****Item 4: Submission of Matters to a Vote of Security Holders**

The 2008 Annual Meeting of stockholders was held on May 28, 2008. The following matters were voted upon and received the votes set forth below:

**A. Election of Directors.** The individuals named below were elected or re-elected to serve as members of the Board of Directors of the Company to serve until the next annual meeting of stockholders and until their successors shall have been elected and qualified:

| Director               | Votes Cast |                    |
|------------------------|------------|--------------------|
|                        | For        | Withheld Authority |
| Charles A. Constantino | 5,206,627  | 3,672,706          |
| John E. Gould          | 5,175,012  | 3,704,321          |
| Andrew W. Moylan       | 5,222,613  | 3,656,720          |
| Anthony C. Mazzullo    | 6,268,397  | 2,610,936          |
| Seth J. Collins        | 5,702,416  | 3,176,917          |

**B. Approval of 2008 Employee Stock Purchase Plan.** At the meeting the following votes were cast with respect to the adoption of the 2008 Employee Stock Purchase Plan:

|                  |           |
|------------------|-----------|
| For:             | 3,207,749 |
| Against:         | 2,619,676 |
| Abstain          | 52,904    |
| Broker non-votes | 2,999,004 |

**C. Ratification of the appointment of independent auditors for the year ending December 31, 2008.** At the meeting the following votes and abstentions were cast with respect to the ratification of the appointment of Rotenberg & Co., LLP as independent auditors for the year ending December 31, 2008:

|          |           |
|----------|-----------|
| For:     | 6,660,257 |
| Against: | 2,180,009 |
| Abstain  | 39,067    |



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**Item 5: Certification of Chief Executive Officer and Chief Financial Officer**

The Company's Chief Executive Officer and the Company's Chief Financial Officer have provided the certifications with respect to this Form 10-Q that are required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002. These certifications have been filed as Exhibits 31.1 and 31.2 and Exhibits 32.1 and 32.2, respectively.

**Item 6: Exhibits and Reports on Form 8-K**

**(a) Exhibits required by Item 601 of Regulation S-K**

(I) Registrant's Condensed Financial Statements for the three and six months ended June 30, 2008 and 2007 are set forth in Part I, Item 1 of this Quarterly Report on Form 10-Q.

(31.1) CEO Certification Pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

(31.2) CFO Certification Pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

(32.1) CEO Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(32.2) CFO Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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**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.

VERAMARK TECHNOLOGIES,  
INC.

REGISTRANT

Date: August 13, 2008

/s/ Anthony C. Mazzullo

Anthony C. Mazzullo  
President and Chief Executive Officer

Date: August 13, 2008

/s/ Ronald C. Lundy

Ronald C. Lundy  
Vice President of Finance and  
Chief Financial Officer

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**EXHIBIT INDEX**

| <b>Exhibit<br/>No.</b> | <b>Description</b>  |
|------------------------|---|
| 31.1                   | CEO Certification Pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2                   | CFO Certification Pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1                   | CEO Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.       |
| 32.2                   | CFO Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.       |