

EPLUS INC
Form 10-Q
August 14, 2008

UNITED STATES
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, 2008

OR

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

For the transition period from ____ to ____ .

Commission file number: 0-28926

ePlus inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

54-1817218
(I.R.S. Employer Identification No.)

13595 Dulles Technology Drive, Herndon, VA 20171-3413
(Address, including zip code, of principal executive offices)

Registrant's telephone number, including area code: (703) 984-8400

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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

The number of shares of common stock outstanding as of July 31, 2008 was 8,283,541.

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Cautionary Language About Forward-Looking Statements

This Quarterly Report on Form 10-Q contains certain statements that are, or may be deemed to be, “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are made in reliance upon the protections provided by such acts for forward-looking statements. Such statements are not based on historical fact, but are based upon numerous assumptions about future conditions that may not occur. Forward-looking statements are generally identifiable by use of forward-looking words such as “may,” “will,” “should,” “intend,” “estimate,” “believe,” “expect,” “anticipate,” “project” and other similar expressions. Readers are cautioned not to place undue reliance on any forward-looking statements made by us or on our behalf. Any such statement speaks only as of the date the statement was made. We do not undertake any obligation to publicly update or correct any forward-looking statements to reflect events or circumstances that subsequently occur, or of which we hereafter become aware. Actual events, transactions and results may materially differ from the anticipated events, transactions or results described in such statements. Our ability to consummate such transactions and achieve such events or results is subject to certain risks and uncertainties. Such risks and uncertainties include, but are not limited to, the matters set forth below.

Although we have been offering IT financing since 1990 and direct marketing of IT products since 1997, our comprehensive set of solutions—the bundling of our direct IT sales, professional services and financing with our proprietary software—has been available since 2002. Consequently, we may encounter some of the challenges, risks, difficulties and uncertainties frequently faced by companies providing new and/or bundled solutions in an evolving market. Some of these challenges relate to our ability to:

- manage a diverse product set of solutions in highly competitive markets;
- increase the total number of customers utilizing bundled solutions by up-selling within our customer base and gain new customers;
- adapt to meet changes in markets and competitive developments;
- maintain and increase advanced professional services by retaining highly skilled personnel and vendor certifications;
- integrate with external IT systems including those of our customers and vendors; and
- continue to update our software and technology to enhance the features and functionality of our products.

We cannot be certain that our business strategy will be successful or that we will successfully address these and other challenges, risks and uncertainties. For a further list and description of various risks, relevant factors and uncertainties that could cause future results or events to differ materially from those expressed or implied in our forward-looking statements, see the “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” sections contained elsewhere in this document, as well as our Annual Report on Form 10-K for the fiscal year ended March 31, 2008, any subsequent Reports on Form 10-Q and Form 8-K and other filings with the SEC.

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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

ePlus inc. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

	As of June 30, 2008	As of March 31, 2008
	(in thousands)	
ASSETS		
Cash and cash equivalents	\$ 61,848	\$ 58,423
Accounts receivable—net	112,047	109,706
Notes receivable	6,531	726
Inventories	8,641	9,192
Investment in leases and leased equipment—net	153,566	157,382
Property and equipment—net	4,386	4,680
Other assets	19,201	13,514
Goodwill	26,245	26,125
TOTAL ASSETS	\$ 392,465	\$ 379,748
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Accounts payable—equipment	\$ 5,887	\$ 6,744
Accounts payable—trade	24,999	22,016
Accounts payable—floor plan	57,055	55,634
Salaries and commissions payable	5,139	4,789
Accrued expenses and other liabilities	33,315	30,372
Non-recourse notes payable	95,516	93,814
Deferred tax liability	2,677	2,677
Total Liabilities	224,588	216,046
COMMITMENTS AND CONTINGENCIES (Note 6)		
STOCKHOLDERS' EQUITY		
Preferred stock, \$.01 par value; 2,000,000 shares authorized; none issued or outstanding	-	-
Common stock, \$.01 par value; 25,000,000 shares authorized; 11,260,531 issued and 8,281,541 outstanding at June 30, 2008 and 11,210,731 issued and 8,231,741 outstanding at March 31, 2008	113	112
Additional paid-in capital	77,757	77,287
Treasury stock, at cost, 2,978,990 and 2,978,990 shares, respectively	(32,884)	(32,884)
Retained earnings	122,316	118,623
Accumulated other comprehensive income—foreign currency translation adjustment	575	564
Total Stockholders' Equity	167,877	163,702

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$	392,465	\$	379,748
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See Notes to Unaudited Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)Three Months Ended June 30,
2008 2007

(amounts in thousands, except per share data)

Sales of product and services	\$	165,759	\$	206,554
Sales of leased equipment		1,265		8,586
		167,024		215,140
Lease revenues		11,625		19,146
Fee and other income		3,637		4,380
		15,262		23,526
TOTAL REVENUES		182,286		238,666
COSTS AND EXPENSES				
Cost of sales, product and services		143,717		185,207
Cost of leased equipment		1,226		8,182
		144,943		193,389
Direct lease costs		3,794		6,023
Professional and other fees		2,545		3,667
Salaries and benefits		19,464		19,694
General and administrative expenses		3,788		4,483
Interest and financing costs		1,485		2,496
		31,076		36,363
TOTAL COSTS AND EXPENSES (1)		176,019		229,752
EARNINGS BEFORE PROVISION FOR INCOME TAXES		6,267		8,914
PROVISION FOR INCOME TAXES		2,574		3,904
NET EARNINGS	\$	3,693	\$	5,010
NET EARNINGS PER COMMON SHARE—BASIC	\$	0.45	\$	0.61
NET EARNINGS PER COMMON SHARE—DILUTED	\$	0.43	\$	0.59
WEIGHTED AVERAGE SHARES OUTSTANDING—BASIC		8,253,552		8,231,741
WEIGHTED AVERAGE SHARES OUTSTANDING—DILUTED		8,580,659		8,434,774

(1)

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Includes amounts to related parties of \$278 thousand and \$243 thousand for the three months ended June 30, 2008 and 2007, respectively.

See Notes to Unaudited Condensed Consolidated Financial Statements.

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ePlus inc. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (UNAUDITED)

	Three Months Ended June 30,	
	2008	2007
	(in thousands)	
Cash Flows From Operating Activities:		
Net earnings	\$ 3,693	\$ 5,010
Adjustments to reconcile net earnings to net cash used in operating activities:		
Depreciation and amortization	4,290	6,137
Reserves for credit losses and sales returns	17	216
Provision for inventory losses and inventory returns	96	93
Impact of stock-based compensation	31	1,511
Excess tax benefit from exercise of stock options	(66)	-
Tax benefit of stock options exercised	97	-
Deferred taxes	-	(251)
Payments from lessees directly to lenders—operating leases	(2,835)	(3,818)
Loss on disposal of property and equipment	8	2
Gain on disposal of operating lease equipment	(372)	(48)
Changes in assets and liabilities, net of acquisition:		
Accounts receivable—net	(2,431)	(36,959)
Notes receivable	(5,805)	21
Inventories	455	(3,957)
Investment in direct financing and sale-type leases—net	(9,274)	2,803
Other assets	(5,411)	(1,682)
Accounts payable—equipment	(501)	2,259
Accounts payable—trade	3,011	3,352
Salaries and commissions payable, accrued expenses and other liabilities	3,266	12,764
Net cash used in operating activities	(11,731)	(12,547)
Cash Flows From Investing Activities:		
Proceeds from sale of operating lease equipment	750	634
Purchases of operating lease equipment	(1,302)	(4,583)
Purchases of property and equipment	(231)	(357)
Premiums paid on officers' life insurance	(79)	(62)
Cash used in acquisitions	(364)	-
Net cash used in investing activities	(1,226)	(4,368)

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ePlus inc. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - continued
 (UNAUDITED)

	Three Months Ended June 30,	
	2008	2007
	(in thousands)	
Cash Flows From Financing Activities:		
Borrowings:		
Non-recourse	16,299	11,935
Repayments:		
Non-recourse	(1,757)	(3,374)
Proceeds from issuance of capital stock, net of expenses	343	-
Excess tax benefit from exercise of stock options	66	-
Net borrowings on floor plan facility	1,420	16,124
Net cash provided by financing activities	16,371	24,685
Effect of Exchange Rate Changes on Cash	11	147
Net Increase in Cash and Cash Equivalents	3,425	7,917
Cash and Cash Equivalents, Beginning of Period	58,423	39,680
Cash and Cash Equivalents, End of Period	\$ 61,848	\$ 47,597
Supplemental Disclosures of Cash Flow Information:		
Cash paid for interest	\$ 141	\$ 383
Cash paid for income taxes	\$ 2,432	\$ 1,158
Schedule of Non-cash Investing and Financing Activities:		
Purchase of property and equipment included in accounts payable	\$ 19	\$ 48
Purchase of operating lease equipment included in accounts payable	\$ 13	\$ 291
Principal payments from lessees directly to lenders	\$ 12,842	\$ 15,632

See Notes to Unaudited Condensed Consolidated Financial Statements.

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ePlus inc. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
As of and for the three months ended June 30, 2008 and 2007

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Unaudited Condensed Consolidated Financial Statements of ePlus inc. and subsidiaries and Notes thereto included herein are unaudited and have been prepared by us, pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and reflect all adjustments that are, in the opinion of management, necessary for a fair statement of results for the interim periods. All adjustments made were of a normal recurring nature.

Certain information and note disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) have been condensed or omitted pursuant to SEC rules and regulations.

These interim financial statements should be read in conjunction with our Consolidated Financial Statements and Notes thereto contained in our Annual Report on Form 10-K for the year ended March 31, 2008. Operating results for the interim periods are not necessarily indicative of results for an entire year.

PRINCIPLES OF CONSOLIDATION — The Unaudited Condensed Consolidated Financial Statements include the accounts of ePlus inc. and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated.

REVENUE RECOGNITION — The majority of our revenues is derived from three sources: sales of products and services, leased revenues and sales of software. Our revenue recognition policies vary based upon these revenue sources.

Revenue from Technology Sales Transactions

We adhere to guidelines and principles of sales recognition described in Staff Accounting Bulletin (“SAB”) No. 104, “Revenue Recognition” (“SAB No. 104”), issued by the staff of the SEC. Under SAB No. 104, sales are recognized when the title and risk of loss are passed to the customer, there is persuasive evidence of an arrangement for sale, delivery has occurred and/or services have been rendered, the sales price is fixed or determinable and collectability is reasonably assured. Using these tests, the vast majority of our product sales are recognized upon delivery.

We also sell services that are performed in conjunction with product sales, and recognize revenue for these sales in accordance with Emerging Issues Task Force (“EITF”) 00-21, “Accounting for Revenue Arrangements with Multiple Deliverables.” Accordingly, we recognize sales from delivered items only when the delivered item(s) has value to the client on a stand alone basis, there is objective and reliable evidence of the fair value of the undelivered item(s), and delivery of the undelivered item(s) is probable and substantially under our control. For most of the arrangements with multiple deliverables (hardware and services), we generally cannot establish reliable evidence of the fair value of the undelivered items. Therefore, the majority of revenue from these services, and hardware sold in conjunction with those services, is recognized when the service is complete and we have received an acceptance certificate. However, in some cases, we do not receive an acceptance certificate and we determine the completion date based upon our records.

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We also sell certain third-party service contracts and software assurance or subscription products for which we evaluate whether the subsequent sales of such services should be recorded as gross sales or net sales in accordance with the sales recognition criteria outlined in SAB No. 104, EITF 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent" and Financial Accounting Standards Board ("FASB") Technical Bulletin 90-1, "Accounting for Separately Priced Extended Warranty and Product Contracts." We must determine whether we act as a principal in the transaction and assume the risks and rewards of ownership or if we are simply acting as an agent or broker. Under gross sales recognition, the entire selling price is recorded in sales of product and services and our costs to the third-party service provider or vendor is recorded in cost of sales, product and services on the accompanying Unaudited Condensed Consolidated Statements of Operations. Under net sales recognition, the cost to the third-party service provider or vendor is recorded as a reduction to sales resulting in net sales equal to the gross profit on the transaction and there is no cost of sales. In accordance with EITF 00-10, "Accounting for Shipping and Handling Fees and Costs," we record freight billed to our customers as sales of product and services and the related freight costs as a cost of sales, product and services.

Revenue from Leasing Transactions

Our leasing revenues are accounted for in accordance with Statement of Financial Accounting Standards ("SFAS") No. 13, "Accounting for Leases." The accounting for revenue is different depending on the type of lease. Each lease is classified as either a direct financing lease, sales-type lease, or operating lease, as appropriate. If a lease meets one or more of the following four criteria, the lease is classified as either a sales-type or direct financing lease, otherwise, it will be classified as an operating lease:

- the lease transfers ownership of the property to the lessee by the end of the lease term;
 - the lease contains a bargain purchase option;
- the lease term is equal to 75 percent or more of the estimated economic life of the leased property; or
- the present value at the beginning of the lease term of the minimum lease payments equals or exceeds 90 percent of the excess of the fair value of the leased property at the inception of the lease.

For direct financing and sales-type leases, we record the net investment in leases, which consists of the sum of the minimum lease payments, initial direct costs (direct financing leases only), and unguaranteed residual value (gross investment) less the unearned income. For direct finance leases, the difference between the gross investment and the cost of the leased equipment is recorded as unearned income at the inception of the lease. Under sales-type leases, the difference between the fair value and cost of the leased property plus initial direct costs (net margins) is recorded as unearned revenue at the inception of the lease. Revenue for both sales-type and direct-financing leases are recognized as the unearned income is amortized over the life of the lease using the interest method. For operating leases, rental amounts are accrued on a straight-line basis over the lease term and are recognized as lease revenue.

Sales of leased equipment represent revenue from the sales of equipment subject to a lease (lease schedule) in which we are the lessor. If the rental stream on such a lease has non-recourse debt associated with it, sales revenue is recorded at the amount of consideration received, net of the amount of debt assumed by the purchaser. If there is no non--recourse debt associated with the rental stream, sales revenue is recorded at the amount of gross consideration received, and costs of sales is recorded at the book value of the lease. Sales of leased equipment represents revenue generated through the sale of equipment sold primarily through our financing business unit.

Lease revenues consist of rentals due under operating leases, amortization of unearned income on direct financing and sales-type leases and sales of leased assets to lessees. Equipment under operating leases is recorded at cost and depreciated on a straight-line basis over the lease term to the estimated residual value.

SFAS No. 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities” (“SFAS No. 140”), establishes criteria for determining whether a transfer of financial assets in exchange for cash or other consideration should be accounted for as a sale or as a pledge of collateral in a secured borrowing. Certain assignments of direct finance leases we make on a non-recourse basis meet the criteria for surrender of control set forth by SFAS No. 140 and have therefore been treated as sales for financial statement purposes. We assign all rights, title, and interests in a number of our leases to third-party financial institutions without recourse. These assignments are recorded as sales since we have completed our obligations as of the assignment date, and we retain no ownership interest in the equipment under lease.

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Revenue from Software Sales Transactions

We derive revenue from licensing our proprietary software for a fixed term or for perpetuity in an enterprise license. In addition, we receive revenues from hosting our proprietary software for our clients. Revenue from hosting arrangements is recognized in accordance with EITF 00-3, "Application of AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware." Our hosting arrangements do not contain a contractual right to take possession of the software. Therefore, our hosting arrangements are not in the scope of Statement of Position 97-2 ("SOP 97-2"), "Software Revenue Recognition," and require that the portion of the fee allocated to the hosting elements be recognized as the service is provided. Currently, the majority of our software revenue is generated through hosting agreements and is included in fee and other income on our Unaudited Condensed Consolidated Statements of Operations.

Revenue from sales of our software is recognized in accordance with SOP 97-2, as amended by SOP 98-4, "Deferral of the Effective Date of a Provision of SOP 97-2," and SOP 98-9, "Modification of SOP 97-2 With Respect to Certain Transactions." We recognize revenue when all the following criteria exist:

- there is persuasive evidence that an arrangement exists;
 - delivery has occurred;
- no significant obligations by us related to services essential to the functionality of the software remain with regard to implementation;
 - the sales price is determinable; and
 - it is probable that collection will occur.

Revenue from sales of our software is included in fee and other income on our Unaudited Condensed Consolidated Statements of Operations.

Our software agreements often include implementation and consulting services that are sold separately under consulting engagement contracts or as part of the software license arrangement. When we determine that such services are not essential to the functionality of the licensed software and qualify as "service transactions" under SOP 97-2, we record revenue separately for the license and service elements of these agreements.

Generally, we consider that a service is not essential to the functionality of the software based on various factors, including if the services may be provided by independent third parties experienced in providing such consulting and implementation in coordination with dedicated customer personnel. When consulting qualifies for separate accounting, consulting revenues under time and materials billing arrangements are recognized as the services are performed. Consulting revenues under fixed-price contracts are generally recognized using the percentage-of-completion method. If there is a significant uncertainty about the project completion or receipt of payment for the consulting services, revenue is deferred until the uncertainty is sufficiently resolved. Consulting revenues are classified as fee and other income on our Unaudited Condensed Consolidated Statements of Operations.

If a service arrangement is essential to the functionality of the licensed software and therefore does not qualify for separate accounting of the license and service elements, then license revenue is recognized together with the consulting services using either the percentage-of-completion or completed-contract method of contract accounting. Under the percentage-of-completion method, we may estimate the stage of completion of contracts with fixed or "not to exceed" fees based on hours or costs incurred to date as compared with estimated total project hours or costs at completion. If we do not have a sufficient basis to measure progress towards completion, revenue is recognized upon completion of the contract. When total cost estimates exceed revenues, we accrue for the estimated losses immediately. The use of the percentage-of-completion method of accounting requires significant judgment relative to estimating total contract costs, including assumptions relative to the length of time to complete the project, the nature

and complexity of the work to be performed, and anticipated changes in salaries and other costs. When adjustments in estimated contract costs are determined, such revisions may have the effect of adjusting, in the current period, the earnings applicable to performance in prior periods.

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For agreements that include one or more elements to be delivered at a future date, we generally use the residual method to recognize revenues when evidence of the fair value of all undelivered elements exists. Under the residual method, the fair value of the undelivered elements (e.g., maintenance, consulting and training services) based on vendor-specific objective evidence (“VSOE”) is deferred and the remaining portion of the arrangement fee is allocated to the delivered elements (i.e., software license). If evidence of the fair value of one or more of the undelivered services does not exist, all revenues are deferred and recognized when delivery of all of those services has occurred or when fair values can be established. We determine VSOE of the fair value of services revenue based upon our recent pricing for those services when sold separately. VSOE of the fair value of maintenance services may also be determined based on a substantive maintenance renewal clause, if any, within a customer contract. Our current pricing practices are influenced primarily by product type, purchase volume, maintenance term and customer location. We review services revenue sold separately and maintenance renewal rates on a periodic basis and update our VSOE of fair value for such services to ensure that it reflects our recent pricing experience, when appropriate.

Maintenance services generally include rights to unspecified upgrades (when and if available), telephone and Internet-based support, updates and bug fixes. Maintenance revenue is recognized ratably over the term of the maintenance contract (usually one year) on a straight-line basis and is included in fee and other income on our Unaudited Condensed Consolidated Statements of Operations. Training services include on-site training, classroom training and computer-based training and assessment. Training revenue is recognized as the related training services are provided and is included in fee and other income on our Unaudited Condensed Consolidated Statements of Operations.

Revenue from Other Transactions

Other sources of revenue are derived from: (1) income from events that occur after the initial sale of a financial asset; (2) remarketing fees; (3) brokerage fees earned for the placement of financing transactions; (4) agent fees received from various manufacturers in the IT reseller business unit; (5) settlement fees related to disputes or litigation; and (6) interest and other miscellaneous income. These revenues are included in fee and other income on our Unaudited Condensed Consolidated Statements of Operations.

VENDOR CONSIDERATION — We receive payments and credits from vendors, including consideration pursuant to volume sales incentive programs, volume purchase incentive programs and shared marketing expense programs. Vendor consideration received pursuant to volume sales incentive programs is recognized as a reduction to costs of sales, product and services in accordance with EITF Issue No. 02-16, “Accounting for Consideration Received from a Vendor by a Customer (Including a Reseller of the Vendor’s Products).” Vendor consideration received pursuant to volume purchase incentive programs is allocated to inventories based on the applicable incentives from each vendor and is recorded in cost of sales, product and services, as the inventory is sold. Vendor consideration received pursuant to shared marketing expense programs is recorded as a reduction of the related selling and administrative expenses in the period the program takes place only if the consideration represents a reimbursement of specific, incremental, identifiable costs. Consideration that exceeds the specific, incremental, identifiable costs is classified as a reduction of cost of sales, product and services.

RESIDUALS — Residual values, representing the estimated value of equipment at the termination of a lease, are recorded in our Unaudited Condensed Consolidated Financial Statements at the inception of each sales-type or direct financing lease as amounts estimated by management based upon its experience and judgment. Unguaranteed residual values for sales-type and direct financing leases are recorded at their net present value and the unearned income is amortized over the life of the lease using the interest method. The residual values for operating leases are included in the leased equipment’s net book value.

We evaluate residual values on an ongoing basis and record any downward adjustment, if required. No upward revision of residual values is made subsequent to lease inception.

RESERVES FOR CREDIT LOSSES — The reserve for credit losses (the “reserve”) is maintained at a level believed by management to be adequate to absorb potential losses inherent in our lease and accounts receivable portfolio. Management’s determination of the adequacy of the reserve is based on an evaluation of historical credit loss experience, current economic conditions, volume, growth, the composition of the lease portfolio, and other relevant factors. The reserve is increased by provisions for potential credit losses charged against income. Accounts are either written off or written down when the loss is both probable and determinable, after giving consideration to the customer’s financial condition, the value of the underlying collateral and funding status (i.e., discounted on a non–-recourse or recourse basis).

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Sales are reported net of returns and allowances. Allowance for sales returns is maintained at a level believed by management to be adequate to absorb potential sales returns from product and services in accordance with SFAS No. 48, "Revenue Recognition when the Right of Return Exist" ("SFAS No. 14"). Management's determination of the adequacy of the reserve is based on an evaluation of historical sales returns, current economic conditions, volume and other relevant factors. These determinations require considerable judgment in assessing the ultimate potential for sales returns and include consideration of the type and volume of products and services sold.

CASH AND CASH EQUIVALENTS — Cash and cash equivalents include funds in operating accounts as well as money market funds.

INVENTORIES — Inventories are stated at the lower of cost (weighted average basis) or market.

PROPERTY AND EQUIPMENT — Property and equipment are stated at cost, net of accumulated depreciation and amortization. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the related assets, which range from three to ten years.

CAPITALIZATION OF COSTS OF SOFTWARE FOR INTERNAL USE — We have capitalized certain costs for the development of internal use software under the guidelines of SOP 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." Software capitalized for internal use was \$16 thousand and \$54 thousand during three months ended June 30, 2008 and 2007, respectively, which is included in the accompanying Unaudited Condensed Consolidated Balance Sheets as a component of property and equipment—net. We had capitalized costs, net of amortization, of approximately \$1.1 million at June 30, 2008 and 1.2 million at March 31, 2008.

CAPITALIZATION OF COSTS OF SOFTWARE TO BE MADE AVAILABLE TO CUSTOMERS — In accordance with SFAS No. 86, "Accounting for Costs of Computer Software to be Sold, Leased, or Otherwise Marketed," software development costs are expensed as incurred until technological feasibility has been established. At such time such costs are capitalized until the product is made available for release to customers. For three months ended June 30, 2008 and 2007, no such costs were capitalized. We had \$526 thousand and \$572 thousand of capitalized costs, net of amortization, at June 30, 2008 and March 31, 2008, respectively.

GOODWILL AND INTANGIBLE ASSETS — In accordance with SFAS No. 142, "Goodwill and Other Intangible Assets," we perform an impairment test for goodwill at September 30th of each year and follow the two-step process prescribed in SFAS No. 142 to test our goodwill for impairment under the transitional goodwill impairment test. The first step is to screen for potential impairment, while the second step measures the amount of the impairment, if any. Intangible assets with finite lives are amortized over the estimated useful lives using the straight-line method. An impairment loss on such assets is recognized if the carrying amount of an intangible asset is not recoverable and its carrying amount exceeds its fair value.

IMPAIRMENT OF LONG-LIVED ASSETS — We review long-lived assets, including property and equipment, for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be fully recoverable. If the total of the expected undiscounted future cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and the carrying value of the asset.

FAIR VALUE OF FINANCIAL INSTRUMENTS — The carrying value of our financial instruments, which include cash and cash equivalents, accounts receivable, accounts payable and accrued expenses and other liabilities, approximates fair value due to their short maturities. The carrying amount of our non-recourse and recourse notes payable approximates its fair value. We determined the fair value of notes payable by applying the average portfolio debt rate and applying such rate to future cash flows of the respective financial instruments. The estimated fair value

and carrying amount of our recourse and non-recourse notes payable at June 30, 2008 was \$95.0 million and \$95.5 million, respectively and at March 31, 2007, they were \$93.3 million and \$93.8 million, respectively.

TREASURY STOCK — We account for treasury stock under the cost method and include treasury stock as a component of stockholders' equity.

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INCOME TAXES — Deferred income taxes are accounted for in accordance with SFAS No. 109, “Accounting for Income Taxes.” Under this method, deferred income tax assets and liabilities are determined based on the temporary differences between the financial statement reporting and tax bases of assets and liabilities, using tax rates currently in effect. Future tax benefits, such as net operating loss carryforwards, are recognized to the extent that realization of these benefits is considered to be more likely than not. In addition, on April 1, 2007, we adopted Financial Accounting Standards Board Interpretation No. 48, “Accounting for Uncertainty in Income Taxes—An Interpretation of FASB Statement No. 109” (“FIN 48”). Specifically, the pronouncement prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The interpretation also provides guidance on the related derecognition, classification, interest and penalties, accounting for interim periods, disclosure and transition of uncertain tax positions. In accordance with our accounting policy, we recognize accrued interest and penalties related to unrecognized tax benefits as a component of tax expense. This policy did not change as a result of the adoption of FIN 48. We have recorded a cumulative effect adjustment to reduce our fiscal 2008 balance of beginning retained earnings by \$491 thousand in our Unaudited Condensed Consolidated Financial Statements.

ESTIMATES — The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

COMPREHENSIVE INCOME — Comprehensive income consists of net income and foreign currency translation adjustments. For the three months ended June 30, 2008, other comprehensive income was \$11 thousand, and net income was \$3.7 million, resulting in total comprehensive income of \$3.7 million. For the three months ended June 30, 2007, other comprehensive income was \$146 thousand and net income was \$5.0 million, resulting in total comprehensive income of \$5.2 million.

EARNINGS PER SHARE — Earnings per share (“EPS”) have been calculated in accordance with SFAS No. 128, “Earnings per Share” (“SFAS No. 128”). In accordance with SFAS No. 128, basic EPS amounts were calculated based on weighted average shares outstanding of 8,253,552 for the three months ended June 30, 2008 and 8,231,741 for the three months ended June 30, 2007. Diluted EPS amounts were calculated based on weighted average shares outstanding and potentially dilutive common stock equivalents of 8,580,659 for the three months ended June 30, 2008 and 8,434,774 for the three months ended June 30, 2007. Additional shares included in the diluted EPS calculations are attributable to incremental shares issuable upon the assumed exercise of stock options and other common stock equivalents.

STOCK-BASED COMPENSATION — On April 1, 2006, we adopted SFAS No. 123 (revised 2004), “Share-Based Payment,” or SFAS No. 123R. SFAS No. 123R replaces SFAS No. 123, “Accounting for Stock-Based Compensation,” and supersedes Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees” (“APB 25”), and subsequently issued stock option related guidance. We elected the modified-prospective transition method. Under the modified-prospective method, we must recognize compensation expense for all awards subsequent to adopting the standard and for the unvested portion of previously granted awards outstanding upon adoption. We have recognized compensation expense equal to the fair values for the unvested portion of share-based awards at April 1, 2006 over the remaining period of service, as well as compensation expense for those share-based awards granted or modified on or after April 1, 2006 over the vesting period based on the grant-date fair values using the straight-line method. For those awards granted prior to the date of adoption, compensation expense is recognized on an accelerated basis based on the grant-date fair value amount as calculated for pro forma purposes under SFAS No. 123.

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RECENT ACCOUNTING PRONOUNCEMENTS — In September 2006, the FASB issued SFAS No. 157, “Fair Value Measurement” (“SFAS No. 157”). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in accordance with U.S. GAAP and expands disclosures about fair value measurements. SFAS No. 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. The provisions of SFAS No. 157 were scheduled to be effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. In February 2008, the FASB issued Staff Position No. FAS 157-2, "Effective Dates of FASB Statement No. 157," which defers the effective date of SFAS No. 157 for all nonrecurring fair value measurements of nonfinancial assets and liabilities until fiscal years beginning after November 15, 2007. We adopted SFAS No. 157 during the three months ended June 30, 2008. The adoption of SFAS No. 157 did not materially affect our financial condition and results of operations.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115” (“SFAS No. 159”). SFAS No. 159 permits an entity, at specified election dates, to choose to measure certain financial instruments and other items at fair value. The objective of SFAS No. 159 is to provide entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently, without having to apply complex hedge accounting provisions. SFAS No. 159 is effective for accounting periods beginning after November 15, 2007. We adopted SFAS No. 159 during the three months ended June 30, 2008. The adoption of SFAS No. 159 did not materially affect our financial condition and results of operations.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), “Business Combinations” (“SFAS No. 141R”), which replaces SFAS 141. SFAS No. 141R applies to all transactions in which an entity obtains control of one or more businesses, including those without the transfer of consideration. SFAS No. 141R defines the acquirer as the entity that obtains control on the acquisition date. It also requires the measurement at fair value of the acquired assets, assumed liabilities and noncontrolling interest. In addition, SFAS No. 141R requires that the acquisition and restructuring related costs be recognized separately from the business combinations. SFAS No. 141R requires that goodwill be recognized as of the acquisition date, measured as residual, which in most cases will result in the excess of consideration plus acquisition-date fair value of noncontrolling interest over the fair values of identifiable net assets. Under SFAS No. 141R, “negative goodwill,” in which consideration given is less than the acquisition-date fair value of identifiable net assets, will be recognized as a gain to the acquirer. SFAS No. 141R is applied prospectively to business combinations for which the acquisition date is on or after the first annual reporting period beginning on or after December 15, 2008. We are evaluating the impact of SFAS No. 141R, if any, to our financial position and statement of operations. We will adopt SFAS No. 141R for future business combinations that occur on or after April 1, 2009.

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2. INVESTMENT IN LEASES AND LEASED EQUIPMENT—NET

Investment in leases and leased equipment—net consists of the following:

	June 30, 2008	As of March 31, 2008
	(in thousands)	
Investment in direct financing and sales-type leases—net	\$ 123,059	\$ 124,254
Investment in operating lease equipment—net	30,507	33,128
	\$ 153,566	\$ 157,382

INVESTMENT IN DIRECT FINANCING AND SALES-TYPE LEASES—NET

Our investment in direct financing and sales-type leases—net consists of the following:

	June 30, 2008	As of March 31, 2008
	(in thousands)	
Minimum lease payments	\$ 119,841	\$ 120,224
Estimated unguaranteed residual value (1)	16,133	17,831
Initial direct costs, net of amortization (2)	1,161	1,122
Less: Unearned lease income	(12,721)	(13,568)
Reserve for credit losses	(1,355)	(1,355)
Investment in direct financing and sales-type leases—net	\$ 123,059	\$ 124,254

(1) Includes estimated unguaranteed residual values of \$1,465 thousand and \$2,315 thousand as of June 30, 2008 and March 31, 2008, respectively, for direct financing SFAS No. 140 leases.

(2) Initial direct costs are shown net of amortization of \$1,371 thousand and \$1,536 thousand as of June 30, 2008 and March 31, 2008, respectively.

Our net investment in direct financing and sales-type leases is collateral for non-recourse and recourse equipment notes, if any.

INVESTMENT IN OPERATING LEASE EQUIPMENT—NET

Investment in operating lease equipment—net primarily represents leases that do not qualify as direct financing leases or are leases that are short-term renewals on a month-to-month basis. The components of the net investment in operating lease equipment are as follows:

	June 30, 2008	As of March 31, 2008
	(in thousands)	
Cost of equipment under operating leases	\$ 61,395	\$ 62,311
Less: Accumulated depreciation and amortization	(30,888)	(29,183)
Investment in operating lease equipment—net	\$ 30,507	\$ 33,128

During the three months ended June 30, 2008 and 2007, we sold portions of our lease portfolio. The sales were reflected in our Unaudited Condensed Consolidated Financial Statements as sales of leased equipment totaling approximately \$1.3 million and \$8.6 million and cost of sales, lease equipment of \$1.2 million and \$8.2 million, for

the three months ended June 30, 2008 and 2007, respectively. There were corresponding reduction of investment in leases and lease equipment – net of \$1.2 million and \$8.2 million at June 30, 2008 and 2007, respectively.

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3. RESERVES FOR CREDIT LOSSES

As of March 31, 2008 and June 30, 2008, our activity in our reserves for credit losses is as follows (in thousands):

	Accounts Receivable	Lease-Related Assets	Total
Balance April 1, 2007	\$ 2,060	\$ 1,641	\$ 3,701
Provision for Bad Debts	55	(245)	(190)
Recoveries	40	-	40
Write-offs and other	(453)	(41)	(494)
Balance March 31, 2008	1,702	1,355	3,057
Provision for Bad Debts	(40)	-	(40)
Recoveries	-	-	-
Write-offs and other	(1)	-	(1)
Balance June 30, 2008	\$ 1,661	\$ 1,355	\$ 3,016

4. RECOURSE AND NON-RECOURSE NOTES PAYABLE

We do not have any recourse notes payable as of June 30, 2008 and March 31, 2008. Non-recourse obligations consist of the following:

	June 30, 2008	As of March 31, 2008
	(in thousands)	
Non-recourse equipment notes secured by related investments in leases with interest rates ranging from 4.65% to 8.5% for the three months ended June 30, 2008 and 4.02% to 10.77% for year ended March 31, 2008.	\$ 95,516	\$ 93,814

During the three months ended June 30, 2008 and 2007, we sold portions of our lease portfolio. The sales were reflected in our Unaudited Condensed Consolidated Financial Statements as sales of leased equipment totaling approximately \$1.3 million and \$8.6 million and cost of sales, lease equipment of \$1.2 million and \$8.2 million, for the three months ended June 30, 2008 and 2007, respectively. There is a corresponding reduction of investment in leases and lease equipment – net of \$1.2 million and \$8.2 million at June 30, 2008 and 2007, respectively.

Principal and interest payments on the recourse and non-recourse notes payable are generally due monthly in amounts that are approximately equal to the total payments due from the lessee under the leases that collateralize the notes payable. Under recourse financing, in the event of a default by a lessee, the lender has recourse against the lessee, the equipment serving as collateral, and us. Under non-recourse financing, in the event of a default by a lessee, the lender generally only has recourse against the lessee, and the equipment serving as collateral, but not against us.

There are two components of the GE Commercial Distribution Finance Corporation (“GECDF”) credit facility: (1) a floor plan component and (2) an accounts receivable component. Under the floor plan component, we had outstanding balances of \$57.1 million and \$55.6 million as of June 30, 2008 and March 31, 2008, respectively. Under the accounts receivable component, we had no outstanding balances as of June 30, 2008 and March 31, 2008. As of June 30, 2008, the facility agreement had an aggregate limit of the two components of \$125 million, and the accounts receivable component had a sub-limit of \$30 million, which bears interest at prime less 0.5%, or 4.75%. Availability

under the GECDP facility may be limited by the asset value of equipment we purchase and may be further limited by certain covenants and terms and conditions of the facility. These covenants include but are not limited to a minimum total tangible net worth and subordinated debt, and maximum debt to tangible net worth ratio of ePlus Technology, inc. We were in compliance with these covenants as of June 30, 2008. Either party may terminate with 90 days' advance notice.

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The facility provided by GECDP requires a guaranty of up to \$10.5 million by ePlus inc. The guaranty requires ePlus inc. to deliver its annual audited financial statements by certain dates. We have delivered the annual audited financial statements for the year ended March 31, 2008 as required. The loss of the GECDP credit facility could have a material adverse effect on our future results as we currently rely on this facility and its components for daily working capital and liquidity for our technology sales business and as an operational function of our accounts payable process.

Borrowings under our \$35 million line of credit from National City Bank are subject to certain covenants regarding minimum consolidated tangible net worth, maximum recourse debt to net worth ratio, cash flow coverage, and minimum interest expense coverage ratio. We are in compliance with these covenants as of June 30, 2008. The borrowings are secured by our assets such as leases, receivables, inventory, and equipment. Borrowings are limited to our collateral base, consisting of equipment, lease receivables, and other current assets, up to a maximum of \$35 million. In addition, the credit agreement restricts, and under some circumstances prohibits, the payment of dividends.

The National City Bank facility requires the delivery of our audited and unaudited financial statements, and pro-forma financial projections, by certain dates. As required by Section 5.1 of the facility, we have delivered all financial statements.

5. RELATED PARTY TRANSACTIONS

We lease approximately 55,880 square feet for use as our principal headquarters from Norton Building 1, LLC for a monthly rent payment of approximately \$93 thousand. Norton Building 1, LLC is a limited liability company owned in part by Mr. Norton's spouse and in part in trust for his children. As of May 31, 2007, Mr. Norton, our President and CEO, has no managerial or executive role in Norton Building 1, LLC. The lease was approved by the Board of Directors prior to its commencement, and viewed by the Board as being at or below comparable market rents, and ePlus has the right to terminate up to 40% of the leased premises for no penalty, with six months' notice. During the three months ended June 30, 2008 and 2007, we paid rent in the amount of \$278 thousand and \$243 thousand, respectively.

6. COMMITMENTS AND CONTINGENCIES

Litigation

We have been involved in several matters relating to a customer named Cyberco Holdings, Inc. ("Cyberco"). The Cyberco principals were perpetrating a scam, and at least five principals have pled guilty to criminal conspiracy and/or related charges, including bank fraud, mail fraud and money laundering. One lender who financed our transaction with Cyberco, Banc of America Leasing and Capital, LLC ("BoA"), filed a lawsuit against ePlus inc. in the Circuit Court for Fairfax County, Virginia on November 3, 2006, seeking to enforce a guaranty in which ePlus inc. guaranteed ePlus Group's obligations to BoA relating to the Cyberco transaction. We are vigorously defending this suit. We cannot predict the outcome of this suit. We do not believe a loss is probable, and therefore we have not accrued for this matter.

On January 18, 2007, a stockholder derivative action related to stock option practices was filed in the United States District Court for the District of Columbia. The amended complaint names ePlus inc. as nominal defendant, and personally names eight individual defendants who are directors and/or executive officers of ePlus. The amended complaint alleges violations of federal securities law, and various state law claims such as breach of fiduciary duty, waste of corporate assets and unjust enrichment. We have filed a Motion to Dismiss the plaintiff's amended complaint. The amended complaint seeks monetary damages from individual defendants and that we take certain corrective actions relating to option grants and corporate governance, and attorneys' fees. We cannot predict the outcome of this suit. We do not believe a loss is probable; therefore, we have not accrued for this matter.

We are also engaged in other ordinary and routine litigation incidental to our business. While we cannot predict the outcome of these various legal proceedings, management believes that a loss is not probable and no amount has been accrued for these matters.

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Regulatory and Other Legal Matters

In June 2006, the Audit Committee commenced an investigation of our stock option grants since our initial public offering in 1996. In August 2006, the Audit Committee voluntarily contacted and advised the staff of SEC of its investigation and the Audit Committee's preliminary conclusion that a restatement would be required. This restatement was included in our Form 10-K for the fiscal year ended March 31, 2006 and was filed with the SEC on August 16, 2007. The SEC opened an informal inquiry and we have and will continue to cooperate with the staff. No amount has been accrued for this matter.

We are currently engaged in a dispute with the government of the District of Columbia ("DC") regarding personal property taxes on property we financed for our customers. DC is seeking approximately \$508 thousand plus interest and penalties, relating to property we financed for our customers. We believe the tax is owed by our customers, and are seeking resolution in DC's Office of Administrative Hearings. We cannot predict the outcome of this matter. We do not believe a loss is probable; therefore, we have not accrued for this matter.

7. EARNINGS PER SHARE

Earnings per share ("EPS") have been calculated in accordance with SFAS No. 128, "Earnings per Share" ("SFAS No. 128"). In accordance with SFAS No. 128, basic EPS amounts are calculated based on three months weighted average shares outstanding of 8,253,552 at June 30, 2008 and 8,231,741 at June 30, 2007. Diluted EPS amounts are calculated based on three months weighted average shares outstanding and potentially dilutive common stock equivalents of 8,580,659 and 8,434,774 at June 30, 2008 and 2007, respectively. Additional shares included in the diluted EPS calculations are attributable to incremental shares issuable upon the assumed exercise of stock options and other common stock equivalents.

The following table provides a reconciliation of the numerators and denominators used to calculate basic and diluted net income per common share as disclosed in our Unaudited Condensed Consolidated Statements of Operations for the three months ended June 30, 2008 and 2007 (in thousands, except per share data).

	Three months ended June 30,	
	2008	2007
Net income available to common shareholders—basic and diluted	\$ 3,693	\$ 5,010
Weighted average shares outstanding—basic	8,254	8,232
In-the-money options exercisable under stock compensation plans	327	203
Weighted average shares outstanding—diluted	\$ 8,581	\$ 8,435
Income per common share:		
Basic	\$ 0.45	\$ 0.61
Diluted	\$ 0.43	\$ 0.59

Unexercised employee stock options to purchase 290,507 shares of our common stock were not included in the computations of diluted EPS for the three months ended June 30, 2008, because the options' exercise prices were greater than the average market price of our common stock during the applicable periods.

8. STOCK REPURCHASE

On November 18, 2005, the Board authorized a new stock repurchase program of up to 3,000,000 shares with a cumulative purchase limit of \$12.5 million, which expired on November 17, 2006. During the three months ended June 30, 2008 and 2007, we did not repurchase any shares of our outstanding common stock. Since the inception of our initial repurchase program on September 20, 2001, as of June 30, 2008, we have repurchased 2,978,990 shares of our outstanding common stock at an average cost of \$11.04 per share for a total purchase price of \$32.9 million.

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9. STOCK-BASED COMPENSATION

Contributory 401(k) Profit Sharing Plan

We provide our employees with a contributory 401(k) profit sharing plan. To be eligible to participate in the plan, employees must be at least 21 years of age and have completed a minimum service requirement. Employer contribution percentages are determined by us and are discretionary each year. The employer contributions vest over a four-year period. For the three months ended June 30, 2008 and 2007, our expense for the plan was approximately \$114 thousand and \$92 thousand, respectively.

SFAS No. 123R

On April 1, 2006, we adopted SFAS No. 123R using the modified prospective transition method. We have recognized compensation cost equal to the fair values for the unvested portion of share-based awards at April 1, 2006 over the remaining period of service, as well as compensation cost expense for those share-based awards granted or modified on or after April 1, 2006 over the vesting period based on the grant-date fair values using the straight-line method. The fair values were estimated using the Black-Scholes option pricing model.

Stock Option Plans

We issued only incentive and non-qualified stock option awards and, except as noted below, each grant was issued under one of the following five plans: (1) the 1996 Stock Incentive Plan (the "1996 SIP"), (2) Amendment and Restatement of the 1996 Stock Incentive Plan (the "Amended SIP") (collectively the "1996 Plans"), (3) the 1998 Long-Term Incentive Plan (the "1998 LTIP"), (4) Amendment and Restatement of the 1998 Stock Incentive Plan (2001) (the "Amended LTIP (2001)") or (5) Amendment and Restatement of the 1998 Stock Incentive Plan (2003) (the "Amended LTIP (2003)"). Sections of note are detailed below. All the stock option plans require the use of the previous trading day's closing price when the grant date falls on a date the stock was not traded.

In addition, at the IPO, there were 245,000 options issued that were not part of any plan, but issued under various employment agreements.

On June 25, 2008, our Board of Directors adopted the 2008 Non-Employee Director Long-Term Incentive Plan ("Non-Employee Director Plan") and the 2008 Employee Long-Term Incentive Plan ("the Employee Plan"). Both the Non-Employee Director Plan and the Employee Plan are subject to shareholder approval at the annual meeting of the shareholders to be held on September 15, 2008.

1996 Stock Incentive Plan

The allowable number of outstanding shares under this plan was 155,000. On September 1, 1996, the Board adopted this plan, and it was effective on November 8, 1996 when the SEC declared our Registration Statement on Form S-1 effective in connection with our IPO on November 20, 1996. The 1996 SIP is comprised of an Incentive Stock Option Plan, a Nonqualified Stock Option Plan, and an Outside Director Stock Option Plan. Each of the components of the 1996 Plans provided that options would only be granted after execution of an Option Agreement. Except for the number of options awarded to directors, the salient provisions of the 1996 SIP are identical to the Amended SIP, which is described below.

With regard to director options, the 1996 Outside Director Stock Option Plan provided for 10,000 options to be granted to each non-employee director upon completion of the IPO, and 5,000 options to be granted to each non-employee director on the anniversary of each full year of his or her service as a director of ePlus. As with the

other components of the 1996 Plans, the director options would be granted only after execution of an Option Agreement.

Amendment and Restatement of the 1996 Stock Incentive Plan

The 1996 SIP was amended via an Amendment and Restatement of the 1996 Stock Incentive Plan. The primary purpose of the amendment was to increase the aggregate number of shares allocated to the plan by making the shares available a percentage (20%) of total shares outstanding rather than a fixed number. The Amended SIP also modified the annual grants to directors from 5,000 options to 10,000 options.

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The Amended SIP also provided for an employee stock purchase plan, and permitted the Board to establish other restricted stock and performance-based stock awards and programs. The Amended SIP was adopted by the Board and became effective on May 14, 1997, subject to approval at the annual shareholders meeting that fall. The Amended SIP was adopted by shareholders at the annual meeting on September 30, 1997.

1998 Long-Term Incentive Plan

The 1998 LTIP was adopted by the Board on July 28, 1998, which is its effective date, and approved by the shareholders on September 16, 1998. The allowable number of shares under the 1998 LTIP is 20% of the outstanding shares, less shares previously granted and shares purchased through our employee stock purchase program. The 1998 LTIP shares many characteristics of the earlier plans. It continues to specify that options shall be priced at not less than fair market value. The 1998 LTIP consolidated the preexisting plans and made the Compensation Committee of the Board responsible for its administration. In addition, the 1998 LTIP eliminated the language of the 1996 Plans that “options shall be granted only after execution of an Option Agreement.” Thus, while the 1998 LTIP does require that grants be evidenced in writing, the writing is not a condition precedent to the grant of the award.

Another change to note is the modification of the LTIP as it relates to options awarded to directors. Under the 1998 LTIP, instead of being awarded on the anniversary of the director’s service, the options are to be automatically awarded the day after the annual shareholders meeting to all directors in service as of that day. No automatic annual grants may be awarded under the LTIP after September 1, 2006. The LTIP also permits for discretionary option awards to directors.

Amended and Restated 1998 Long-Term Incentive Plan

Minor amendments were made to the 1998 LTIP on April 1, April 17 and April 30, 2001. The amendments change the name of the plan from the 1998 Long-Term Incentive Plan to the Amended and Restated 1998 Long-Term Incentive Plan. In addition, provisions were added “to allow the Compensation Committee to delegate to a single board member the authority to make awards to non-Section 16 insiders, as a matter of convenience,” and to provide that “no option granted under the Plan may be exercisable for more than ten years from the date of its grant.”

The Amended LTIP (2001) was amended on July 15, 2003 by the Board and approved by the stockholders on September 18, 2003. Primarily, the amendment modified the aggregate number of shares available under the plan to a fixed number (3,000,000). Although the language varies somewhat from earlier plans, it permits the Board or Compensation Committee to delegate authority to a committee of one or more directors who are also officers of the corporation to award options under certain conditions. The Amended LTIP (2003) replaced all the prior plans, is our current plan, and covers option grants for employees, executives and outside directors.

As of June 30, 2008, a total of 2,202,814 shares of common stock have been reserved for issuance upon exercise of options granted under the Amended LTIP (2003).

Stock-Based Compensation Expense

In accordance with SFAS No. 123R, we recognized \$31 thousand of stock-based compensation expense for the three months ended June 30, 2008 as compared to \$1.5 million for the three months ended June 30, 2007. As previously disclosed, during the three months ended June 30, 2007, 450,000 options were cancelled which resulted in the recognition of the remaining nonvested share-based compensation expense of \$1.5 million for that period. As of June 30, 2008, there was \$27 thousand of unrecognized compensation expense related to nonvested options. This expense is expected to be fully recognized over the next three months.

Stock Option Activity

During the three months ended June 30, 2008 and 2007, there were no stock options granted to employees.

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Expected life of the option is the period of time that we expect the options granted to be outstanding. Expected stock price volatility is based on historical volatility of our stock. Expected dividend yield is zero as we do not expect to pay any dividends, nor have we historically paid any dividends. Risk-free interest rate is the five-year nominal constant maturity Treasury rate on the date of the award.

A summary of stock option activity during the three months ended June 30, 2008 is as follows:

Number of Shares	Exercise Price Range	Weighted Average Exercise Price	Weighted Average Contractual Life Remaining (in years)	Aggregate Intrinsic Value
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