

INTELLIGENT SYSTEMS CORP
Form 10-Q/A
December 14, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A
(Amendment No. 1)

(Mark One)

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

For the quarterly period ended March 31, 2012

OR

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

For the transition period from _____ to _____

Commission file number 1-9330

INTELLIGENT SYSTEMS CORPORATION
(Exact name of registrant as specified in its charter)

Georgia 58-1964787
(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)
organization)

4355 Shackleford Road, Norcross, Georgia 30093
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (770) 381-2900

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

Indicated by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). 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. (Check one):

Large accelerated Accelerated filer

filer

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

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

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

As of April 30, 2012, 8,958,028 shares of Common Stock of the issuer were outstanding.

Explanatory Note

The purpose of this Amendment No. 1 to this Quarterly Report on Form 10-Q is to restate the consolidated financial statements of Intelligent Systems Corporation (the "Company") to reflect adjustments related to the amounts and allocation of profits and losses to the Noncontrolling Interest of one of the Company's subsidiaries in accordance with Financial Account Standards Board ("FASB") authoritative guidance establishing accounting and reporting standards for Noncontrolling Interests in Consolidated Financial Statements. We recently determined that we have not been applying the guidance correctly in all respects because we have not been attributing to the Noncontrolling Interest (held by common shareholders of our CoreCord Software subsidiary) its share of the losses or income of the subsidiary and have not been disclosing such attributed amounts on the face of the consolidated statements of operations. Accordingly, we have restated the consolidated statements of operations for the three month periods ended March 31, 2012 and 2011 and the stockholders' equity section of the consolidated balance sheets as of March 31, 2012 and December 31, 2011 to fully comply with the standard.

For the convenience of the reader, this Amendment No. 1 amends in its entirety the original filing of the Quarterly Report on Form 10-Q. This Amendment No. 1 does not reflect events occurring after the May 15, 2012 original filing date of the Company's Quarterly Report on Form 10-Q for the period ended March 31, 2012 or modify or update those disclosures set forth in that Quarterly Report on Form 10-Q, except to reflect the restatement as noted above and in Note 12 to the Consolidated Financial Statements.

The items of the Company's Quarterly Report on Form 10-Q for the period ended March 31, 2012 that have been amended and restated herein are as follows:

1. Part I, Item 1. Financial Statements have been restated.
2. Currently dated certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 have been filed.
3. Currently dated certifications pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 have been filed.

Intelligent Systems Corporation

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**XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

Part I FINANCIAL INFORMATION

Item 1. Financial Statements

Intelligent Systems Corporation
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share amounts)

	March 31, 2012 (unaudited, restated)	December 31, 2011 (audited, restated)
ASSETS		
Current assets:		
Cash	\$3,077	\$3,152
Marketable securities	228	209
Accounts receivable, net	2,745	2,504
Notes and interest receivable, current portion	243	249
Inventories, net	885	824
Other current assets	285	284
Total current assets	7,463	7,222
Investments	1,283	1,288
Notes and interest receivable, net of current portion	--	240
Property and equipment, at cost less accumulated depreciation	1,167	1,222
Patents, net	121	133
Total assets	\$10,034	\$10,105
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$754	\$463
Deferred revenue, current portion	915	907
Accrued payroll	411	460
Accrued expenses	638	669
Other current liabilities	280	369
Total current liabilities	2,998	2,868
Deferred revenue, net of current portion	45	50
Other long-term liabilities	134	140
Commitments and contingencies (Note 8)		
Intelligent Systems Corporation stockholders' equity:		
Common stock, \$0.01 par value, 20,000,000 shares authorized, 8,958,028 issued and outstanding at March 31, 2012 and December 31, 2011	90	90
Additional paid-in capital	21,479	21,461
Accumulated other comprehensive loss	(63)	(111)
Accumulated deficit	(14,285)	(14,290)
Total Intelligent Systems Corporation stockholders' equity	7,221	7,150
Non-controlling interest	(364)	(103)
Total stockholders' equity	6,857	7,047
Total liabilities and stockholders' equity	\$10,034	\$10,105

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

Intelligent Systems Corporation

CONSOLIDATED STATEMENTS OF OPERATIONS

(restated, unaudited; in thousands, except share and per share amounts)

	Three Months Ended March 31,	
	2012	2011
Revenue		
Products	\$3,418	\$3,032
Services	676	512
Total revenue	4,094	3,544
Cost of revenue		
Products	1,686	1,548
Services	537	278
Total cost of revenue	2,223	1,826
Expenses		
Marketing	586	520
General & administrative	871	918
Research & development	668	639
Operating loss	(254)	(359)
Other income (expense)		
Interest income, net	4	11
Equity in income (loss) of affiliate company	(4)	9
Other income	10	6
Loss before income taxes	(244)	(333)
Income taxes	12	21
Net loss	(256)	(354)
Net loss attributable to noncontrolling interest	261	202
Net income (loss) attributable to Intelligent Systems Corporation	\$ 5	\$(152)
Income (loss) per share based on net income (loss) attributable to Intelligent Systems Corporation:		
Basic and diluted	\$0.00	\$(0.02)
Basic weighted average common shares outstanding	8,958,028	8,958,028
Diluted weighted average common shares outstanding	9,119,967	8,958,028

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Three Months Ended March 31,	
(unaudited, in thousands)	2012	2011
Net loss	\$(256)	\$(354)
Other comprehensive income (loss)		
Unrealized gain on available-for-sale marketable securities	19	--
Foreign currency translation adjustment	29	(2)
Comprehensive loss	\$(208)	\$(356)

The accompanying notes are an integral part of these Consolidated Financial Statements.

Intelligent Systems Corporation
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

CASH PROVIDED BY (USED FOR):	Three Months Ended March 31,	
	2012	2011
OPERATIONS:		
Net loss	\$(256	) \$(354
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation and amortization	138	61
Stock-based compensation expense	19	8
Non-cash interest income, net	(4	) (3
Equity in (income) loss of affiliate company	4	(9
Changes in operating assets and liabilities		
Accounts receivable	(241	) (98
Inventories	(61	) (80
Other current assets	(1	) (239
Accounts payable	291	177
Deferred revenue	8	156
Accrued payroll	(49	) (29
Accrued expenses	(31	) 16
Other current liabilities	(89	) (31
Other long-term liabilities	(11	) (23
Net cash used for operating activities	(283	) (448
INVESTING ACTIVITIES:		
Proceeds from notes and interest receivable	250	600
Purchases of property and equipment	(71	) (191
Net cash provided by investing activities	179	409
Effects of exchange rate changes on cash	29	(2
Net decrease in cash	(75	) (41
Cash at beginning of period	3,152	2,942
Cash at end of period	\$3,077	\$2,901
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for income taxes	\$13	\$19

The accompanying notes are an integral part of these Consolidated Financial Statements.

Intelligent Systems Corporation
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Throughout this report, the terms “we”, “us”, “ours”, “ISC” and “company” refer to Intelligent Systems Corporation, including its wholly-owned and majority-owned subsidiaries. The unaudited Consolidated Financial Statements presented in this Form 10-Q have been prepared in accordance with accounting principles generally accepted in the United States applicable to interim financial statements. Accordingly, they do not include all of the information and notes required for complete financial statements. In the opinion of ISC management, these Consolidated Financial Statements contain all adjustments (which comprise only normal and recurring accruals) necessary to present fairly the financial position and results of operations as of and for the three month periods ended March 31, 2012 and 2011. The interim results for the three months ended March 31, 2012 are not necessarily indicative of the results to be expected for the full year. These statements should be read in conjunction with our Consolidated Financial Statements and notes thereto for the fiscal year ended December 31, 2011, as filed in our Annual Report on Form 10-K.
2. Option Agreement – As disclosed in Note 17 to our 2011 Annual Report Form 10-K, on March 20, 2012, Intelligent Systems Corporation entered into an Option Agreement (the “Option Agreement”) with Central National Bank, a national banking association (“CNB”). The Option Agreement grants to CNB the option to acquire from ISC the number of shares of stock in the company’s CoreCard Software subsidiary equal to five percent (5%) of ISC’s equity ownership in CoreCard. Currently, ISC owns approximately 96 percent of the equity of CoreCard. The number of shares covered by the option may be increased, up to ten percent (10%), based on achievement of certain volumes of prepaid cards issued by CNB and processed by CoreCard, as defined in the Option Agreement. The option has an exercise price of one million dollars, expires on December 31, 2017 and can be exercised at any time before it expires. Further, at any time between September 30, 2014 and June 30, 2017, subject to certain earlier termination provisions, CNB may elect to require ISC to repurchase the option at a purchase price equal to the fair market value of the option less one million dollars. We entered into the Option Agreement in recognition of CNB’s ongoing cooperation and contribution to building CoreCard’s card processing business. During the quarter ended March 31, 2012, we recorded an expense of \$18,000 in the marketing category and recorded a long-term liability of \$18,000 to recognize the financial impact of the Option Agreement.
3. Comprehensive Income (Loss) – Comprehensive income (loss) is the total of net income (loss) and all other non-owner changes in equity in a period. A summary follows:

Consolidated Statements of Comprehensive Loss (unaudited, in thousands)	Three Months Ended March 31,	
	2012	2011
Net loss	\$ (256)	\$ (354)
Other comprehensive income (loss)		
Unrealized gain on available-for-sale marketable securities	19	--
Foreign currency translation adjustment	29	(2)
Comprehensive loss	\$ (208)	\$ (356)

4. Stock-based Compensation – At March 31, 2012, we have two stock-based compensation plans in effect. We record compensation cost related to unvested stock awards by recognizing the unamortized grant date fair value on a straight line basis over the vesting periods of each award. We have estimated forfeiture rates based on our historical experience. Stock option compensation expense for the three month periods ended March 31, 2012 and 2011 has been recognized as a component of general and administrative expenses in the accompanying Consolidated Financial Statements. We recorded \$19,000 and \$8,000 of stock-based compensation expense in the quarters ended

March 31, 2012 and 2011, respectively.

The estimated fair value of options granted is calculated using the Black-Scholes option pricing model with assumptions as previously disclosed in our 2011 Form 10-K.

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As of March 31, 2012, there is \$150,000 of unrecognized compensation cost related to stock options. No options were granted during the three months ended March 31, 2012. The following table summarizes options as of March 31, 2012:

	# of Shares	Wgt Avg Exercise Price	Wgt Avg Remaining Contractual Life in Years	Aggregate Intrinsic Value
Outstanding at March 31, 2012	342,500	\$ 1.78	5.8	\$ 12,240
Vested and exercisable at March 31, 2012	172,000	\$ 1.95	2.5	\$ 10,680

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the company's closing stock price on the last trading day of the first quarter of 2012 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on March 31, 2012. The amount of aggregate intrinsic value will change based on the fair market value of the company's stock.

5. Fair Value of Financial Instruments - The carrying value of cash, marketable securities, accounts receivable, accounts payable and certain other financial instruments (such as short-term borrowings, accrued expenses, and other current liabilities) included in the accompanying consolidated balance sheets approximates their fair value principally due to the short-term maturity of these instruments. The carrying value of the non-interest bearing note receivable beyond one year approximates its fair value and has been discounted at a rate of 4% which approximates rates offered in the market for notes receivable with similar terms and conditions.

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash, marketable securities, trade accounts and note receivable. Our available cash is held in accounts managed by third-party financial institutions. Cash may exceed the Federal Deposit Insurance Corporation, or FDIC, insurance limits. While we monitor cash balances on a regular basis and adjust the balances as appropriate, these balances could be impacted if the underlying financial institutions fail. To date, we have experienced no loss or lack of access to our cash; however, we can provide no assurances that access to our cash will not be impacted by adverse conditions in the financial markets.

6. Fair Value Measurements - In determining fair value, the Company uses quoted market prices in active markets. GAAP establishes a fair value measurement framework, provides a single definition of fair value, and requires expanded disclosure summarizing fair value measurements. GAAP 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 an asset or liability.

GAAP establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable input be used when available. Observable inputs are based on data obtained from sources independent of the company that market participants would use in pricing the asset or liability. Unobservable inputs are inputs that reflect the company's assumptions about the estimates market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The hierarchy is measured in three levels based on the reliability of inputs:

- Level 1

Valuations based on quoted prices in active markets for identical assets or liabilities that we have the ability to access. Valuation adjustments and block discounts are not applied to Level 1 instruments.

- Level 2

Valuations based on quoted prices in less active, dealer or broker markets. Fair values are primarily obtained from third party pricing services for identical or comparable assets or liabilities.

- Level 3

Valuations derived from other valuation methodologies, including pricing models, discounted cash flow models and similar techniques, and not based on market, exchange, dealer, or broker-traded transactions. Level 3 valuations incorporate certain assumptions and projections that are not observable in the market and significant professional judgment is needed in determining the fair value assigned to such assets or liabilities.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

Our available-for-sale investments are classified within level 1 of the valuation hierarchy.

The fair value of equity method and cost method investments has not been determined as it was impracticable to do so due to the fact that the investee companies are relatively small, early stage private companies for which there is no comparable valuation data available without unreasonable time and expense.

7. Concentration of Revenue – The following table indicates the percentage of consolidated revenue represented by each customer for any period in which such customer represented more than 10% of consolidated revenue.

(unaudited)	Three Months Ended March 31,			
	2012		2011	
ChemFree Customer A	13	%	11	%
ChemFree Customer B	29	%	33	%
ChemFree Customer C	10	%	11	%
ChemFree Customer D	--		11	%

8. Commitments and Contingencies – Please refer to Note 8 to our Consolidated Financial Statements included in our 2011 Form 10-K for a description of our commitments and contingencies in addition to those disclosed here.

Legal Matters – ChemFree Patent Matter – As reported in our 2011 Form 10-K, on March 12, 2012, the United States Court of Appeals issued its final ruling in the long-standing case brought by ChemFree on a patent infringement matter, affirming the invalidity findings of the lower court with respect to certain claims in four of ChemFree’s patents. As a result of the ruling, ChemFree incurred a liability for certain allowable taxable costs. Accordingly, the company accrued for the estimated amount of such costs and recorded an expense of \$75,000 reflected in the category Other Income and a corresponding liability reflected in Other Current Liabilities in its 2011 Consolidated Financial Statements. The total final amount of the liability for taxable costs was \$76,000, which ChemFree paid in April 2012.

On September 29, 2011, ChemFree filed a second patent infringement action against J. Walter in the United States District Court for the Northern District of Georgia, alleging that certain of J. Walter’s products infringe a newly issued patent held by ChemFree. The complaint seeks a ruling to compel the defendant to cease its infringing activities. The matter is in a preliminary phase.

In the ordinary course of business, from time to time we may be involved in various pending or threatened legal actions. The litigation process is inherently uncertain and it is possible that the resolution of such matters might have a material adverse effect upon our financial condition and/or results of operations. Except as noted above, other commitments and contingencies described in Note 8 to the Consolidated Financial Statements included in our 2011 Form 10-K are unchanged.

9. Industry Segments – Segment information is presented consistently with the basis described in the 2011 Form 10-K. The following table contains segment information for the three months ended March 31, 2012 and 2011.

(unaudited, in thousands)	Three Months Ended March	
	2012	2011
Information Technology		

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Revenue	\$706	\$550
Operating loss	(640) (554
Industrial Products		
Revenue	3,388	2,994
Operating income	833	582

(unaudited, in thousands)	Three Months Ended March	
	2012	31, 2011
Consolidated Segments		
Revenue	\$4,094	\$3,544
Operating income	193	29
Corporate expenses	(447)	(388)
Consolidated operating loss	\$(254)	\$(359)
Depreciation and Amortization		
Information Technology	\$52	\$40
Industrial Products	82	18
Consolidated segments	134	58
Corporate	4	3
Consolidated depreciation and amortization	\$138	\$61
Capital Expenditures		
Information Technology	\$61	\$127
Industrial Products	10	63
Consolidated segments	71	190
Corporate	--	