ULTRADATA SYSTEMS INC
Form 10QSB
November 19, 2001

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

(MARK ONE)
[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 - FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2001

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15 (d) OF THE EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM __________TO ____________

COMMISSION FILE NUMBER 0-25380

ULTRADATA SYSTEMS, INCORPORATED
(Exact name of small business issuer as specified in its charter)

| Delaware | 43-1401158 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

| 1240 Dielman Industrial Court, St. Louis, MO | 63132 |
|---|---|
| (Address of principal executive offices) | (Zip Code) |

| 9375 Dielman Industrial Drive, St. Louis, MO | 63132 |
|---|---|
| (Former address of principal executive offices) | (Zip Code) |

Issuer's telephone number, including area code: (314) 997-2250

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date.

| Class | Outstanding as of November 8, 2001 |
|---|---|
| Common, $.01 par value | 3,249,533 |

Transitional Small Business Disclosure Format Yes [ ] No [X]

File Number
0-25380

ULTRADATA SYSTEMS, INCORPORATED
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ULTRADATA SYSTEMS, INCORPORATED

Balance Sheets

| | September 30, 2001 (unaudited) | December 31, 2000 |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 426,091 | $ 1,842,983 |
| Restricted cash | - | 767,724 |
| Trade accounts receivable, net of allowance for doubtful accounts of $117,556 | 166,102 | 673,475 |
| Inventories | 1,735,933 | 1,780,255 |
| Prepaid expenses | 211,148 | 229,637 |
| Total current assets | 2,539,274 | 5,294,074 |
| Property and equipment, net | 464,408 | 617,794 |
| Deferred compensation trust investments, available for sale | - | 84,605 |
| Investment in Talon Research and Development, Ltd. | 797,251 | 825,757 |
| Advances to affiliates | 150,000 | 150,000 |
| Advertising credits | 62,421 | 62,421 |
| Other assets | 9,444 | 8,594 |
| Total assets | $ 4,022,798 | $ 7,043,245 |

| | | |
|---|---|---|
| **Liabilities and Stockholders' Equity** | | |
| Current liabilities: | | |
| Accounts payable | $ 155,686 | $ 164,319 |
| Accrued expenses and other liabilities | 72,593 | 218,996 |
| Total current liabilities | 228,279 | 383,315 |
| Deferred rent | 622 | 6,220 |
| Deferred compensation liability | - | - |
| Note payable | 1,633,591 | 87,329 |
| Total liabilities | 1,862,492 | 476,864 |
| Stockholders' equity: | | |
| Preferred Stock, $0.01 par value, 4,996,680 shares authorized, none outstanding | - | - |
| Series A convertible preferred stock, 3,320 shares authorized, 16 shares outstanding with a stated value of $1,000 | 16,000 | 1,616,000 |
| Common stock, $.01 par value; 10,000,000 shares authorized; 3,575,704 shares issued and outstanding September 30,2001; 3,519,586 shares issued and outstanding December 31, 2000 | 35,757 | 35,196 |
| Additional paid-in capital | 9,526,093 | 9,861,970 |
| Accumulated deficit | (6,167,549) | (3,737,190) |
| Treasury stock (326,171 shares at cost) | (942,311) | (942,311) |
| Notes receivable issued for purchase of common stock | (212,833) | (205,819) |
| Accumulated other comprehensive (loss) income, net | (94,851) | (61,465) |
| Total stockholders' equity | 2,160,306 | 6,566,381 |
| Total liabilities, preferred stock, and stockholders' equity | $4,022,798 | $7,043,245 |

See accompanying summary of accounting policies and notes to financial statements.

ULTRADATA SYSTEMS, INCORPORATED

Statements of Operations

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2001 | 2000 | 2001 | 2000 |
| | (unaudited) | | (unaudited) | |
| Net sales: | $ 139,503 | $ 2,556,091 | $ 835,957 | $ 3,619,198 |
| Cost of sales: | 570,422 | 1,801,524 | 985,072 | 2,524,068 |

| | | | | |
|---|---|---|---|---|
| Gross profit | (430,919) | 754,567 | (149,115) | 1,095,130 |
| Selling expense | 96,804 | 178,900 | 302,786 | 346,348 |
| General and administrative expenses | 538,056 | 626,506 | 1,678,876 | 1,661,496 |
| Research and development expense | 81,347 | 114,448 | 306,707 | 286,538 |
| Operating loss | (1,147,126) | (165,287) | (2,437,484) | (1,199,252) |
| Other (expense) income: | | | | |
| Interest expense | (18,300) | - | (31,199) | - |
| Interest and dividend income | 215 | 47,215 | 59,157 | 131,570 |
| Equity in earnings (losses) of affiliates | 12,359 | (3,998) | 17,927 | (129,086) |
| Other, net | (16,657) | 151,031 | (38,760) | 68,762 |
| Total other income, net | (22,383) | 194,248 | 7,125 | 71,246 |
| Earnings (loss) before income taxes | (1,169,509) | 28,961 | (2,430,359) | (1,128,006) |
| Income tax | - | - | - | - |
| Net earnings (loss) | (1,169,509) | 28,961 | (2,430,359) | (1,128,006) |
| Less preferred stock dividends | (160,610) | (68,680) | (252,279) | (1,128,427) |
| Net earnings (loss) available to common shareholders | $(1,330,119) | $ (39,719) | $(2,682,638) | $ (2,256,433) |
| Earnings (loss) per share- basic and diluted | $ (0.41) | $ (0.01) | $ (0.83) | $ (0.71) |
| Weighted Average Shares Outstanding: Basic and diluted | 3,249,533 | 3,197,361 | 3,226,113 | 3,160,484 |

See accompanying summary of accounting policies and notes to financial statements.

ULTRADATA SYSTEMS, INCORPORATED

Statements of Cash Flows

Nine months ended September 30, 2001 and 2000

| | 2001 | 2000 |
|---|---|---|
| | (unaudited) | |
| Cash flows from operating activities: | | |
| Net loss | $(2,430,359) | $(1,128,006) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: | | |
| Deferred income tax provision | - | - |

| | | |
|---|---|---|
| Depreciation and amortization | 146,871 | 169,430 |
| Provision for inventory obsolescence | 613,672 | - |
| Equity in losses (earnings) of unconsolidated affiliates | (17,927) | 129,087 |
| Realized (gain) loss on investments | 13,046 | (10,602) |
| Gain on disposal of fixed asset | 18,534 | - |
| Non-cash compensation expense | 2,544 | 13,993 |
| Bad debt expense on advances to affiliates | - | 122,683 |
| Increase (decrease) in assets and liabilities: | | |
| Trade accounts receivable | 507,373 | 110,312 |
| Inventories | (569,350) | (129,678) |
| Prepaid expenses and other current assets | 10,625 | (169,268) |
| Accounts payable | (8,634) | 781,444 |
| Accrued expenses and other liabilities | (146,403) | (118,116) |
| Deferred rent | (5,598) | (5,598) |
| Deferred compensation trust liability | - | (1,183) |
| Other assets | - | 23,636 |
| Net cash used in operating activities | (1,865,606) | (211,866) |
| Cash flows from investing activities: | | |
| Investment in affiliated company | - | (200,000) |
| Deferred compensation trust investments | - | (8,748) |
| Capital expenditures | (12,017) | (124,501) |
| Restricted cash | 765,000 | (356,731) |
| Net cash provided by (used in) investing activities | 752,983 | (689,980) |
| Cash flows from financing activities: | | |
| Proceeds from issuance of redeemable preferred stock and common stock warrants | - | 1,616,000 |
| Costs related to issuance of redeemable preferred stock and common stock warrants | - | (375,625) |
| Repayment of notes payable | (126,269) | - |
| Repurchase of preferred shares | (178,000) | - |
| Exercise of employee stock options | - | 314,625 |
| Net cash provided by (used in) financing activities | (304,269) | 1,555,000 |
| Net increase (decrease) in cash and cash equivalents | (1,416,892) | 653,154 |
| Cash and cash equivalents at beginning of period | 1,842,983 | 1,220,134 |
| Cash and cash equivalents at end of period | $ 426,091 | $ 1,873,288 |
| Non-cash investing and financing | | |
| Redemption of Rabbi Trust | $ 87,329 | $ - |
| Conversion of preferred stock to common stock | $ 28,000 | $ - |
| Conversion of preferred stock to notes payable | $ 1,759,860 | $ - |

See accompanying summary of accounting policies and notes to financial statements.

ULTRADATA SYSTEMS, INCORPORATED

September 30, 2001

Summary of Significant Accounting Policies

Basis of Presentation

The accompanying interim financial statements included herein have been prepared by Ultradata Systems, Incorporated (the "Company"), without audit in accordance with generally accepted accounting principles and pursuant to the rules and regulations of the Securities and Exchange Commission for interim financial information. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures made are adequate to make the information presented not misleading. The Company's investment in Talon Research and Development, Ppty., Ltd., Auckland, NZ of 22.6% is accounted for using the equity method.

In the opinion of management, the information furnished for the three-month and nine-month periods ended September 30, 2001 and 2000, includes all adjustments, consisting solely of normal recurring accruals necessary for a fair presentation of the financial results for the respective interim periods and is not necessarily indicative of the results of operations to be expected for the entire fiscal year ending December 31, 2001. It is suggested that the interim financial statements be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2000, as filed with the Securities and Exchange Commission on Form 10-KSB (Commission File Number 0-25380).

Use of Estimates

The financial statements have been prepared in conformity with generally accepted accounting principles and, as such, include amounts based on informed estimates and adjustments by management, with consideration given to materiality. Actual results could vary from those estimates.

Reclassifications

Certain 2000 balances have been reclassified to conform to the 2001 presentation. In the fourth quarter 2000, the Company changed the way it accounts for certain sales incentives, in accordance with EITF Issue No. 00-25. Accordingly, the Company has restated the financial statements for the first and second quarters of 2000 to reflect this change. The Company reduced sales and selling expense by $8,282 in the first quarter and $37,193 in the second quarter. There was no such transaction in the third quarter.

Note 1. Nature of Operations

The principal business activity of Ultradata Systems, Incorporated (the Company), located in St. Louis, Missouri, is the design, manufacture, and sale of hand-held electronic information products.

Note 2. Inventories

Inventories consist of the following:

| | September 30, 2001 (unaudited) | December 31, 2000 |
|---|---|---|
| Raw Materials | $ 1,030,121 | $ 1,262,820 |
| Work in Process | 32,119 | 57,393 |
| Finished Goods | 1,450,422 | 1,020,803 |
| | 2,512,662 | 2,341,016 |
| Reserve for obsolescence | (776,729) | (560,761) |
| | $ 1,735,933 | $ 1,780,255 |

Note 3. Prepaid Expenses

Prepaid expenses consist of the following:

| | September 30, 2001 (unaudited) | December 31, 2000 |
|---|---|---|
| Prepaid advertising | $ 194,764 | $ 201,225 |
| Prepaid insurance | 8,005 | 5,461 |
| Other prepaid expenses | 8,379 | 22,951 |
| | $ 211,148 | $ 229,637 |

Note 4. Accrued Expenses and Other Liabilities

Accrued expenses and other liabilities consist of the following:

| | September 30, 2001 (unaudited) | December 31, 2000 |
|---|---|---|
| Accrued vacation | $ 31,052 | $ 82,990 |
| Accrued sales commissions and royalties | - | 14,758 |
| Payroll and payroll-related liabilities | 12,693 | 42,294 |
| Accrued advertising | - | 1,563 |
| Other | 28,848 | 77,391 |
| | $ 72,593 | $ 218,996 |

Note 5. Preferred Stock Redemption

During the three months ended September 30, 2001, the Company repurchased from preferred shareholders 58 shares of preferred stock for $70,000 cash.

Note 6. Preferred Stock Conversion to Note Payable

On August 13, 2001, the holders of most of the Series A Convertible Preferred Stock exchanged their shares for Senior Subordinated Secured Convertible Promissory Notes with a value of $1,748,120 and interest at 11.25%

per annum. This amount includes all accrued dividends to that date on the preferred stock plus a 10% premium on the face amount of the stock.

Note 7. Subsequent Events

On November 8, 2001, the holders of the 11.25% Senior Subordinated Secured Convertible Promissory Notes converted $9,244.97 of interest accrued under the Notes into 83,288 shares of Common Stock. On November 14, 2001, they converted $4,660 of accrued interest into 27,508 shares of Common Stock.

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

YOU SHOULD NOT RELY ON FORWARD LOOKING STATEMENTS

This quarterly report contains a number of forward-looking statements regarding our future prospects. Among the forward-looking statements are descriptions of our plans to restructure the marketing program for the Road Whiz(tm) line of products, to introduce Triplink(tm) and GPS products to the market, and to develop products based on a GPS/Internet technology. These forward-looking statements are a true statement of our present intentions, but are neither predictions of the future nor assurances that any of our intentions will be fulfilled. Many factors beyond our control could act to thwart Ultradata in its efforts to develop and market its products. Among these factors are:

* The fact that our cash resources are insufficient to fund significant growth;
* The difficulty of attracting mass-market retailers to a seasonal product like the Road Whiz(tm);
* The breadth and depth of competition in the GPS market, which will make introduction of our product with a limited marketing budget difficult;
* The difficulty of attracting qualified engineering and marketing personnel to our company.

There may also be factors that we have not foreseen which could interfere with our plans. In addition, changing circumstances may cause us to determine that a change in plans will be in the best interests of Ultradata. For this reason, you should not place undue reliance on any of the forward-looking statements in this report.

Readers are urged to carefully review and consider the various disclosures made by the Company in this report and in the Company's report Form 10-KSB filed with the Securities and Exchange Commission.

The analysis of the Company's financial condition, capital resources and operating results should be viewed in conjunction with the accompanying financial statements, including the notes thereto.

OVERVIEW

Since 1987 we have been engaged in the business of manufacturing and marketing handheld computers that provide travel information. The products are based upon a data compression technology that we developed, portions of which we have patented. Recent developments in communications technology have opened up new opportunities for us to use our technology. Therefore, we still sell our handheld computers, but over the past three years we have been expanding the scope of our operations:

* In 1998 we acquired an interest in Talon Research & Development, Ltd.,

which manufactures GPS (global positioning satellite) antennas that can be combined with our database to create a variety of travel products. We currently own 22.6% of Talon.

* Early in 2001 we introduced, in joint venture with Rand McNally, the Rand McNally Triplink(tm), a handheld computer that enables the user to download travel information from the Rand McNally Website.

* During the first quarter of 2001 we shipped the first production units of our Travel*Star 24(tm), which combines our travel information with a GPS antenna to enable a driver to obtain his location and directions to his destination while he drives. Beta tests revealed some software bugs that have since been corrected, and an updated version should be ready for delivery early in 2002.

* We started development of an enhanced version of our GPS product that will include a cellular transceiver to permit the driver to use the product to access the Internet while traveling. We have temporarily put further work on hold until the basic Travel*Star 24(tm) is in full production.

Each of our consumer products is designed to allow the consumer to access useful information stored in a convenient manner. Our handheld computers generally sell at retail prices between $19.95 and $49.95 per unit. The products are in the three largest retail mass-market chains in the country plus many other locations. The new TRAVEL*STAR 24 is offered at retail for about $400, which should make it very competitive in the auto aftermarket. Its portability and the fact that it requires no elaborate installation offer advantages over the more expensive in-car systems.

The Company is actively pursuing the sale of its 22.6% ownership in Talon. Management is seeking substantially more than its investment, as it believes the market value of Talon shares is significantly greater than the present book value ($797,251).

RESULTS OF OPERATIONS

Three and Nine Months Ended September 30, 2001 Compared to Three and Nine Months Ended September 30, 2000

Operating results for the third quarter of 2001 were significantly different from the third quarter of 2000. A large order in the third quarter of 2000 had no counterpart in 2001. On the contrary, the continuing softness in the economy, further depressed by the events of September 11, 2001, have seriously affected sales and earnings.

Sales. During the three and nine months ended September 30,2001, net sales totaled $139,503 and $835,957, respectively, compared with $2,556,091 and $3,619,198, respectively for the same periods in 2000. These figures represent decreases of 94.5% and 76.9% for the three- and nine-month periods, respectively, representing significantly reduced demand for our traditional products in the present softening US economy.

Gross Profit. Gross profit margin for the three- and nine-month periods ending September 30, 2001 were negative due to a write-off of $516,234 in obsolete inventory in September 2001. Most of this write-down consists of GPS engines the Company hopes to be able to use in 2001, at which time a portion of this loss item may be recovered. As a result, gross margins for the three- and nine-month periods were (308.9%) and (17.8%), respectively. Without the September write-down, gross margins would have been 61.2% and 43.9% for the three- and nine-month period, respectively.

SG&A Expense. Selling expenses for the three- and nine-month periods ended September 30, 2001 were $96,804 and $302,786, respectively, compared with $178,900 and $346,348, respectively, for the corresponding periods in 2000. These figures represent a decrease of 45.8% and 12.3%, respectively, for the three- and nine-month periods in 2001 versus 2000. The primary reasons for the decrease is the reduction in overall sales and the attendant commissions that go with them. As a percent of sales the current costs are much higher. General and administrative expenses were slightly lower for the three months in 2001 due to cost cutting in the corporate office, but about the same for the nine months in 2001 as compared with the same periods of 2000. Success in reducing these costs is important to the continuing survival of the Company pending improved sales due to new products.

R&D Expense. Research and development expense in the three-month period ended September 30,2001 decreased 28.9%. For the nine-month period they increased 7.0%. The quarter reduction reflect the recent cutback in personnel, whereas the nine-month slight increase reflects the fact that the capitalization of the TRAVEL*STAR 24 software tools developed over the last 21 months ended and the amortization of those costs began in the first quarter of 2001.

The Company posted a net loss from operations of ($1,147,126) and ($2,437,484) for the three- and nine-month periods ended September 30, 2001, respectively, compared to a net loss from operations of ($165,287) and ($1,199,252) for the corresponding periods in 2000.

Other Income. Other income (expense) for the three- and nine-month periods ended September 30, 2001 totaled ($22,383) and $7,125, respectively, compared with $194,248 and $71,246, respectively, for the corresponding periods of 2000. Talon's contribution was $17,927 for the nine-month period ended September 30, 2001 as compared with $136,944 for the same period in 2000. The large difference between 2000 and 2001 is attributed to the four-fold increase in R&D for 2001 over 2000. US Generally Accepted Accounting Principles differ from those in New Zealand in that most research and development costs must be expensed in the US but may be capitalized in New Zealand. The R&D activity supports Talon's new-product development and general modernization of their product line.

As a result of the foregoing, the Company posted a net loss available to common shareholders of ($1,330,119), or ($0.41) per basic and diluted common share, for the three-month period ended September 30, 2001, compared to a net loss available to common shareholders of ($39,719), or ($0.01) per basic and diluted common share, for the three-month period ended September 30, 2000. The Company posted a net loss available to common shareholders of ($2,682,638), or ($0.83) per basic and diluted common share, for the nine-month period ended September 30, 2001, compared to a net loss available to common shareholders of ($2,256,433), or ($0.71) per basic and diluted common share, for the nine-month period ended September 30, 2000. The Company was required to record an imputed dividend as a result of its sale of Series A redeemable convertible preferred stock in May of 2000 of $160,610 and $252,279 during the three- and nine-month periods ended September 30, 2001, respectively, as compared with $68,680 and $1,128,427, respectively, for the corresponding periods in 2000.

FINANCIAL CONDITION AND LIQUIDITY

At September 30, 2001`, the Company had $426,091 in cash and cash equivalents, compared to $1,842,983 at December 31, 2000. The Company's operating activities in the nine months ended September 30, 2001, used cash totaling $1,865,606, primarily due to its losses for the first nine months of the year. Accounts receivable decreased by $507,373 due to collections on sales in the first half of 2001. Inventories increased by $569,350 due to manufacturing for the deliveries in the fourth quarter, and accounts payable decreased by $8,634.

Net cash provided by investing activities for the nine-month period ended September 30, 2001 totaled $752,983 compared to ($689,980) used in investing activities for the same period in 2000, which included additional investment in Influence Data, LLC, and reduced cash outlay for capital expenditures. The 2001 total also includes the recovery of the restricted cash by the expiration of the letter of credit in favor of Talon. Net cash used in financing activities for the three-month period ended September 30, 2001 was ($304,269) compared with $1,555,000 provided in the same period of 2000. The 2001 period included cash used to repurchase 58 shares of Series A Preferred Stock. In the comparable period of 2000, the preferred shares were subscribed, providing the bulk of the cash provided by financing activities.

Our operating losses over the past three years have had an adverse effect on our working capital. Nevertheless, at September 30, 2001, we still had $2.31 million in working capital, which we believe to be substantially greater than most companies our size. There remains, however, one near-term liquidity issue: the cash needed for development of new products. The Company's $1 million credit facility with Southwest Bank expired on July 1, 2001. Management has obtained a $500,000 replacement facility with KBK Financial, an asset-based lender, which it believes will be sufficient, together with our own funds, to finance the purchase orders expected for the fourth quarter. We expect, therefore, given achievement of our fourth quarter forecast, to have sufficient capital resources to fund our operations for the next year and the foreseeable future.

We have reduced staff, office space, and consulting expenses to bring our costs of doing business more in line with revenues. The Company is now able to function on much lower sales per year and is in a position to be profitable except for repayment of the outstanding debt.

ULTRADATA SYSTEMS, INCORPORATED
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PART II - OTHER INFORMATION

Item 1. Legal Proceedings:

None

Item 2. Changes in Securities:

None

Item 3. Defaults upon Senior Securities:

None

Item 4. Submission of Matters to a Vote of Security Holders:

None

Item 5. Other Information:

None

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

Exhibits:

None

Reports on Form 8-K:

Report dated August 13, 2001, regarding the exchange of Series A Preferred Stock for 11.25% Senior Subordinated Convertible Notes.

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.

November 19, 2001

/s/ Monte Ross

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Monte Ross, CEO
(Duly authorized officer and principal financial officer)