PRISM SOFTWARE CORP
Form 10KSB/A
April 19, 2004

U.S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Amendment No. 2
FORM 10-KSB/A

(MARK ONE)
[X] ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2003
[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

COMMISSION FILE NUMBER 0-21713

PRISM SOFTWARE CORPORATION
(Name of small business issuer in its charter)

Delaware	95-2621719
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
23696 Birtcher Lake Forest, California	92630
(Address of principal executive offices)	(Zip code)

Issuer's telephone number (including area code): (949) 855-3100

Securities registered under Section 12(b) of the Exchange Act:

None

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE EXCHANGE ACT:

Common Stock, par value $.01 per share
(Title of Class)

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

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB [ ]

The registrant's revenues for the year ended December 31, 2003 were $490,838

The aggregate market value of the voting stock held by non-affiliates of the registrant on March 31, 2004 was approximately $651,437.

The number of shares outstanding of the registrant's only class of Common Stock, par value $.01 per share was 141,591,534 on March 31, 2004. The common shares are traded on the OTC Bulletin Board under the symbol "PSOF".

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PART I

ITEM 1. DESCRIPTION OF BUSINESS.

COMPANY OVERVIEW

Prism Software Corporation (the "Company") was organized under the laws of Delaware in 1992. The Company specializes in enterprise document and content management solutions. The Company's products and expertise lie in electronic document formation, document management, and print stream conversion solutions. The Company's customer base includes organizations that use its solutions in managing high-volume, large scale document printing. These customers are in a variety of markets, such as financial services, health care, service bureau printing, government, education and manufacturing.

The Company distributes its products primarily in North America, through direct sales, resellers, value-added resellers ("VARs") and printer manufacturers.

Marketing, sales, training and technical support are provided from its Lake Forest, California corporate headquarters.

The Company's principal executive office is located at 23696 Birtcher, Lake Forest, California 92630, and its telephone number is (949) 855-3100. The Company's website is located at "www.prism-software.com."

CURRENT PRODUCTS

The following is a brief summary of the Company's two primary products: DocForm and PrintConsole Pro. More detailed information about both of these two products can be found on the company's website at www.prism-software.com. The information on the Company's website is not a part of this Report.

DOCFORM
DocForm is a powerful, low-cost and easy-to-use software tool for the design, dynamic creation, and real-time delivery of all electronic documents, forms, and reports for every industry. Its primary purposes are to (1) reduce costs by eliminating pre-printed forms, (2) enable users to dynamically create complex and personalized documents and reports, and (3) create one-to-one personalized sales and marketing messages.

PRINTCONSOLE PRO
PrintConsole Pro (1) manages corporate print and document output, and (2) can transform various print stream formats into other formats. Transforming print stream formats is of value to many organizations that want to utilize and redirect mainframe print streams designed for older and often outdated printers to newer, more modern printers.

DEPENDENCE ON MAJOR CUSTOMERS

For the fiscal years ended December 31, 2003 and December 31, 2002, the three largest customers in each year accounted for about 42% and about 34%, respectively, of the Company's sales. None of the three largest customers in either fiscal year were the same. A significant reduction in sales from any of the three largest customers from 2003 could have a material adverse effect on the Company's future operations.

The Company does not have any long-term sales contracts with any of its customers.

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RESEARCH AND DEVELOPMENT

For the fiscal years ended December 31, 2003 and December 31, 2002, research and development expenses were approximately $262,000 (about 53% of net sales) and approximately $306,000 (about 56% of net sales), respectively. None of the research and development expenses in either fiscal year were borne directly by customers.

INTELLECTUAL PROPERTY

The Company currently does not hold any patents and relies on a combination of contract, copyright, trademark and trade secret laws, licenses and confidentiality agreements and software security measures to protect its proprietary intellectual property. Despite these precautions, the Company believes that existing laws provide limited protection for the Company's technologies. However, because of the rapid pace of technological change in the Company's industry, the legal intellectual property protection for products is a less significant factor in its success than the knowledge, abilities and experience of the Company's employees, the frequency of its product enhancements, the effectiveness of its marketing activities and the timeliness and quality of its support services. There can be no assurance that the Company's means of protecting its proprietary rights will prevent others from misappropriating or otherwise gaining access to valuable information, such as software source codes, or that others will not develop technologies similar or superior to the Company's technologies. In addition, effective intellectual property protection may be unavailable or limited in certain foreign countries. The Company generally enters into confidentiality or license agreements with its employees, consultants, customers and vendors and generally controls access to and distribution of its software, documentation and other proprietary information. Despite the Company's efforts to protect its proprietary rights, unauthorized parties may attempt to copy aspects of the Company's products or to obtain and use information that the Company regards as proprietary. Policing unauthorized use of the Company's products is difficult. There can be no assurance that the steps taken by the Company will prevent misappropriation of its technology. In addition, litigation may be necessary in the future to enforce the Company's intellectual property rights, to protect the Company's trade secrets or to determine the validity and scope of the proprietary rights of others.

The Company owns, licenses or has otherwise obtained the right to use certain technologies incorporated in its products. While the Company believes that its software products and proprietary rights do not infringe the rights of others, there can be no assurance that third parties will not assert infringement claims against the Company or that any such claims will not require the Company to enter into royalty or license arrangements or result in costly litigation, regardless of the merits of the claims.

EMPLOYEES

As of March 31, 2004, the Company had 13 employees. The Company's employees are not represented by any collective bargaining organization and the Company has never experienced a work stoppage. The Company believes that its relations with its employees are good.

ITEM 2. DESCRIPTION OF PROPERTY.

The Company's principal administrative, development, manufacturing and shipping facilities are located in one facility in Lake Forest, California. The Company believes its facilities are adequate for its current needs and that suitable additional or substitute space will be available as and if needed.

ITEM 3. LEGAL PROCEEDINGS.

E. TED DANIELS

On April 21, 1995 the Company and Mr. Daniels entered into an Amended and Restated Employment Agreement and stock option agreement replacing the original agreement of September 30, 1994 which provided that during the term of the agreement, Mr. Daniels would be the President and Chief Executive Officer of the Company and would receive an annual base salary of $120,000 (subject to annual review and increases), an annual bonus equal to 10% of the Company's consolidated operating income before interest, taxes, bonus payments and certain other fringe benefits, 320,000 shares of Common Stock at no cost and a non-qualified stock option to acquire a number of shares of Common Stock equal to the greater of (i) 640,000 or (ii) the difference between 8% of the diluted Common shares outstanding from time to time and the 320,000 Common shares previously issued to Mr. Daniels (subject to certain anti-dilution adjustments) at an exercise price of $0.25 per share. The term of the employment contract went through September 30, 1998.

In December 1995, the Board of Directors approved the acceleration of the vesting of such options to become fully vested and immediately exercisable, provided that as of such date (i) the Company has not terminated Mr. Daniels for cause pursuant to the Employment Agreement and (ii) Mr. Daniels has not voluntarily resigned from the Company. Also in December 1995, the Company approved that all options granted under this Agreement are issued pursuant to Rule 701 of the Securities Act. In May 1996, the Board of Directors waived the payment by Mr. Daniels of the exercise price with respect to 1,150,430 shares issuable upon exercise of such options. In August 1996, one Board director resigned, leaving only two directors, one of them being Mr. Daniels. The third director's seat remained vacant for approximately seven years.

Mr. Daniels claims that in May 1997, the Board of Directors approved that the exercise price of all options granted to Mr. Daniels under this agreement be reduced to $0.04 per share. Mr. Daniels claims that in December 1997, the Board of Directors amended the agreement to provide for an annual increase cost of living adjustment of 10% retroactive to the date of Mr. Daniels' original contract of September 1994. The Company did not pay Mr. Daniels the full amount of salary due under this formula but at his direction accrued the unpaid balance. He also claims that in December 1997, the Board approved that all options issuable to Mr. Daniels under this agreement be exercisable at no cost and that the agreement be extended to September 30, 2000, that in October 1998, the Board extended the agreement to September 14, 2002, and that in August 2000, the Board extended the agreement to September 14, 2004.

The Company disputes the claims by Mr. Daniels because all the purported Board actions to amend or extend his Amended and Restated 1995 Employment Contract and stock options from August 1996 to October 2003 failed to be approved by a majority of the directors present and are invalid and void. Therefore his Employment Contract expired September 30, 1998 by its own terms. Mr. Daniels claims the vote of just one of two directors present was sufficient and that he is entitled to the additional salary.

In addition, except for options to purchase 2,000,000 shares of Common Stock that were subsequently exercised in 2003, as of December 31, 2002, Mr. Daniels had voluntarily cancelled all rights to such options that had previously been granted and any additional such options that would have otherwise been granted to him in the future under his agreement. However, Mr. Daniels claims that he is entitled to receive replacement options (that would expire in October 2004) on modified terms that would be similar to the ones he had previously cancelled.

Mr. Daniels has called for arbitration of the dispute, but the arbitration proceedings have not been scheduled.

Additionally, Mr. Daniels has sued the other two directors (Carl von Bibra and Conrad von Bibra) serving at the time his services as President and Chief Executive Officer terminated on January 23, 2004.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.
None

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

The Common Stock of the Company is quoted on the National Association of Securities Dealers, Inc. ("NASD") OTC Bulletin Board ("OTCBB") under the symbol "PSOF." The OTCBB is a quotation service for subscribing members and is regulated by the Securities and Exchange Commission ("SEC") and the NASD. OTCBB securities are traded by a community of market makers that enter quotes and trade reports through a closed computer network. Set forth below are the high ask and low bid prices of the Company's Common Stock during each quarter of the fiscal years ended December 31, 2002 and December 31, 2003, as reported by a member firm of the NASD that effects transactions in stocks quoted on the OTCBB and acts as one of the market makers for the Company's Common Stock. The quotations listed below reflect interdealer prices, without retail mark-up, mark-down or commissions, and may not necessarily represent actual transactions.

	High/Ask	Low/Bid
Quarter ended March 31, 2002	0.021	0.013
Quarter ended June 30, 2002	0.017	0.0051
Quarter ended September 30, 2002	0.010	0.0055
Quarter ended December 31, 2002	0.017	0.003
Quarter ended March 31, 2003	0.016	0.008
Quarter ended June 30, 2003	0.016	0.007
Quarter ended September 30, 2003	0.035	0.004
Quarter ended December 31, 2003	0.027	0.010

As of March 31, 2004, there were approximately 710 stockholders of record of the Company's Common Stock.

The Company has never paid cash dividends on its Common Stock and does not intend to pay cash dividends in the foreseeable future.

During 2003 the Company issued 2,000,000 shares of its Common Stock to E. Ted Daniels upon the exercise of stock options. The Company believes this issuance was exempt from the registration requirements of the Securities Act of 1933, as amended, by reason of Section 4(2) thereof.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

The following discussion and analysis should be read in conjunction with the Company's Consolidated Financial Statements and Notes thereto included elsewhere in this Annual Report on Form 10-KSB. Except for the historical information contained herein, the following discussion contains certain forward-looking statements that involve risks and uncertainties, such as statements of the Company's plans, objectives, expectations and intentions. The cautionary statements made in this Annual Report on Form 10-KSB should be read as being applicable to all related forward-looking statements wherever they appear in this Annual Report on Form 10-KSB. The Company's actual results may differ materially from the results discussed in the forward-looking statements.

RESULTS OF OPERATIONS

COMPARISON OF FISCAL YEARS ENDED DECEMBER 31, 2003 AND DECEMBER 31, 2002

For the fiscal year ended December 31, 2003, the Company reported a loss of approximately $5,254,000, or $0.04 per common share, compared with a loss of approximately $2,307,000, or $0.02 per share, for the fiscal year ended December 31, 2002. The loss increased approximately $2,947,000 due primarily to the following:

- Operating revenue decreased approximately $53,000. Due to the Company's focus on developing its reseller sales channel, there was a shift in the revenue mix from direct end-user sales to sales made through resellers. In addition, there was a shift in revenue to a new proprietary product line.

- The cost of sales decreased approximately $41,000 from approximately $130,000, or about 24% of revenue, to approximately $89,000, or about 18% of revenue. The decrease in the cost of sales percentage was due primarily to a different mix of products being sold.

- Total operating expenses decreased approximately $396,000 due primarily to the following:

    1. In 2002, the Company incurred a one-time loss of approximately $104,000 in writing down assets from a licensing agreement

    2. In 2002, the Company accrued a one-time expense of approximately $72,000 for minimum royalties under the aforementioned licensing agreement

    3. The remaining decrease in operating expenses was due mostly to lower expenses for personnel and professional services, resulting mainly from general cost reduction measures.

- o Interest expense increased approximately $3,332,000 due primarily to the following:

  1. An expense of about $3,172,000 was recognized in 2003 from amortizing a beneficial conversion feature on certain convertible notes. No such expense was incurred in 2002. (See "Liquidity and Capital Resources.")

  2. An increase of approximately $160,000 in aggregate face value interest expense due to an increase in the Company's indebtedness.

LIQUIDITY AND CAPITAL RESOURCES

On December 31, 2003, the Company had cash and cash equivalents of approximately $12,000. The principal source of liquidity in the fiscal year ended December 31, 2003 was approximately $1,381,000 of additional borrowings, all of which are convertible into Common Stock at the lenders' option.

When $690,000 of such borrowings were made during the fiscal year ended December 31, 2003, the conversion rate was lower than the quoted market price of the Common Stock. The value of this beneficial conversion feature (discount) on each such loan was limited to being no greater than the face value of such loan and was fully amortized when the debt was incurred.

In addition, due to the terms of a debt restructuring agreement, the conversion rate on an additional $78,000 of such borrowings made during the fiscal year ended December 31, 2003, and on $3,229,000 of borrowings made prior to the fiscal year ended December 31, 2003, was reduced to below the quoted market price of the Common Stock at the time the original debt was incurred. The value of this beneficial conversion feature (discount) on each such loan was limited to being no greater than the face value of such loan and was fully amortized when the reduced conversion rate went into effect.

As of December 31, 2003, the aggregate unamortized discount on such loans was $0 and the Company had recorded approximately $3,172,000 as additional paid-in capital for the accumulated amortization of the discount. This non-cash amortization expense is included as part of the caption "Interest expense - stockholders" in the accompanying statements of operations. For the fiscal years ended December 31, 2003 and December 31, 2002, this amortization expense was approximately $3,172,000 and $0, respectively.

Management anticipates that additional capital will be required to finance the Company's operations. The Company believes that expected cash flow from operations, borrowing, and the possible proceeds from sales of securities will be sufficient to finance the Company's operations at currently anticipated levels for a period of at least twelve months. However, there can be no assurance that the Company will not encounter unforeseen difficulties that may deplete its capital resources more rapidly than anticipated.

EFFECT OF INFLATION

The Company believes that inflation has not had a material effect on its net sales or profitability in recent years.

FORWARD-LOOKING STATEMENTS; CAUTIONARY STATEMENT

Certain of the statements contained in this report, including those under "Description of Business" and "Management's Discussion and Analysis or Plan of Operation," and especially those contained under "Liquidity and Capital Resources" may be "forward-looking statements" that involve risks and uncertainties. All forward-looking statements included in this report are based on information available to the Company on the date hereof and the Company assumes no obligation to update any such forward-looking statements. The actual future results of the Company could differ materially from those statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this Annual Report on Form 10-KSB as well as risks associated with managing the Company's growth. While the Company believes that these statements are accurate, the Company's business is dependent upon general economic conditions and various conditions specific to its industry and future trends and results cannot be predicted with certainty.

ITEM 7. FINANCIAL STATEMENTS.

The financial statements of the Company are submitted as a separate section of this Annual Report on Form 10-KSB.

ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

ITEM 8A. CONTROLS AND PROCEDURES.

Under the supervision and with the participation of our Chief Executive and Financial Officers, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-14(c) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), within 90 days of the filing date of this report. Based on this evaluation, our Chief Executive and Financial Officers concluded that the Company's disclosure controls and procedures are effective. Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports under the Exchange Act are processed and reported within the time periods specified by law. The design of any such system of controls is based in part on assumptions about the likelihood of future events, and there can be no assurance that any such system of controls will succeed in all circumstances.

Since the date of the evaluation described above, there have been no significant changes in our internal controls or in other factors that could significantly affect these controls.

PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT.

DIRECTORS AND EXECUTIVE OFFICERS:

Carl S. von Bibra	42	Director and Chairman of the Board
David Ayres	49	Director and President
Conrad von Bibra	74	Director and Secretary
E. Ted Daniels	63	Director and Past President
Michael Cheever	35	Controller

Carl S. von Bibra has served the Company as a director and Chairman since October 31, 2003. From March 1993 through May 1994, Mr. von Bibra was a board member of ADcom Information Services, Inc. and, since December 1992, has been corporate secretary of OCI Communication, Inc. Mr. von Bibra received his engineering degree from Stanford University. Carl von Bibra is the son of Conrad von Bibra and is a private investor.

David Ayres joined the Company in May 2002. He has over thirteen years of experience in the printer industry, and over twenty years in senior management positions. Prior to joining the Company he was CEO of an industry-leading supplier to the OEM printer market. He was also Sr. Product Group Manager for Canon in their Canon Computers Systems division. He has served as President of the Company since January 23, 2004 and as a director since February 13, 2004.

Conrad von Bibra was born and raised in Los Angeles, graduating from Stanford University with a degree in chemical engineering. From 1962 to 1984, he served as President of Exeter Oil Company Ltd., a drilling and production company whose stock was listed on the American Stock Exchange in 1981. He is now a private investor. He is the father of Carl S. von Bibra. He became a director and Secretary of the Company starting October 31, 2003.

E. Ted Daniels joined the Board of Directors of the Company in September 1994 and was President, Chief Executive Officer and interim Chief Financial Officer until January 23, 2004. He was employed by Eureka Capital Management from 1993 to 1994 where he was the Managing Director. Previously, he was President and Chief Operating Officer for Roberts Consolidated Industries.

Michael Cheever joined the Company in October 1993 and became an officer on October 31, 2003. He has over thirteen years of accounting experience and was formerly with the accounting firm of Deloitte & Touche LLP.

DIRECTORS' COMPENSATION

The members of the Board of Directors do not receive any cash compensation for their service as directors, but are eligible for reimbursement of their expenses incurred in connection with attendance at Board meetings in accordance with Company policy.

AUDIT COMMITTEE

The Company does not have an Audit Committee. This function is fulfilled by the Board of Directors.

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Exchange Act requires that directors and officers of the Company and persons who beneficially own more than 10% of the Common Stock file with the SEC initial reports of beneficial ownership and reports of changes in beneficial ownership of the Common Stock of the Company. Directors, officers and greater than 10% beneficial owners are required by SEC regulations to furnish the Company with copies of all Section 16(a) forms they file.

The Company received no copies of any Section 16(a) forms filed by officers, directors or 10% beneficial owners during 2003, other than the Form 4 Reports to the SEC filed during 2003 by Conrad von Bibra and Carl von Bibra and Form 3 and Form 4 Reports covering purchases in 2003 filed by David Ayres following his election to President in 2004. Based solely on its review of the copies of the Section 16(a) forms received by it, and on representations from certain reporting persons, the Company believes that, during the last fiscal year, all

Section 16(a) filing requirements applicable to its officers, directors and greater than 10% beneficial owners were complied with, except that, to the knowledge of the Company, E. Ted Daniels, its former President and a director, did not file a Form 4 with respect to the shares acquired by him during 2003 upon exercise of options.

CODE OF ETHICS

The Company is in the process of preparing a Code of Ethics for its officers and directors and will discuss it at the next meeting of its Board of Directors. It will be attached as an exhibit to the first quarterly report on Form 10-QSB that the Company will file after adopting the Code.

ITEM 10. EXECUTIVE COMPENSATION.

SUMMARY COMPENSATION TABLE

The following table sets forth certain compensation awarded or paid by the Company to its executive officers during the fiscal years ended December 31, 2003, December 31, 2002 and December 31, 2001. No other executive officer's total annual salary and bonus for services to the Company exceeded $100,000.

		Annual Compensation			A
Name and Principal Position	Fiscal Year	Salary (1) ($)	Bonus ($)	Other Annual Compen-sation (2) ($)	Stock Awards ($)
E. Ted Daniels (1)	2003	$178,435	$0	$16,203	$16,00
Past President and	2002	$172,273	$0	$14,607	$

Chief Executive Officer	2001	$224,280	$0	$12,246	$
David Ayres	2003	$137,551	$0	$0	$
President	2002	$89,640	$0	$0	$
Michael Cheever	2003	$66,054	$0	$0	$
Controller					

(1) The salary amounts shown for Mr. Daniels do not include additional amounts totalling approximately $171,000 (through his last day of employment on January 23, 2004) for past wages being claimed by Mr. Daniels and disputed by the Company. (See "Legal Proceedings")

(2) Includes auto allowances, insurance and other fringe benefits.

(3) Includes shares of Common Stock issuable upon exercise of options granted to Mr. Daniels. Prior to January 23, 2004, Mr. Daniels had exercised options to acquire an aggregate of approximately 4,130,000 shares of the Company's Common Stock, of which 2,000,000 shares were acquired at no cost by Mr. Daniels in 2003. (Also see "Legal Proceedings" and "Management Options of E. Ted Daniels")

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OPTION EXERCISES AND FISCAL YEAR-END VALUES

Show below is information with respect to the number of shares of the Company's Common Stock acquired upon the exercise of options during the fiscal year ended December 31, 2003, the value realized therefor, the number of unexercised options at December 31, 2002 and the value of unexercised in-the-money options at December 31, 2003 for the Company's executive officers in the Summary Compensation Table above. The Company's executive officers did not hold any stock appreciation rights ("SARs") during the fiscal year ended December 31, 2003.

NAME	SHARES ACQUIRED ON EXERCISE (#)	VALUE REALIZED	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS AT FISCAL YEAR-END (#) EXERCISABLE/UNEXERCISABLE	EX
E. Ted Daniels	2,000,000	$16,000	0/0	
David Ayres	0	$0	500,000/0	
Michael Cheever	0	$0	240,000/0	

EMPLOYMENT AGREEMENTS

There are currently no employment agreements between the Company and any of its directors, officers or significant employees. See "Legal Proceedings" regarding the former employment of past President and Chief Executive Officer E. Ted Daniels.

STOCK OPTION PLANS

1993 STOCK OPTION PLAN

In February 1993, the Board of Directors adopted the Company's 1993 Stock Option Plan. Due to subsequent changes to the Internal Revenue Code (the "Code") and for other reasons, the Board of Directors decided to amend many provisions of this plan. As a consequence, the Board of Directors adopted an Amended and Restated 1993 Stock Option Plan (the "1993 Plan") in May 1996. The 1993 Plan authorized the granting of options to purchase up to a maximum 630,000 shares of Common Stock to qualified officers, key employees, directors and employees of companies that do business with the Company. As of December 31, 2003, options for 62,500 shares of Common Stock available for grant under the 1993 Plan had been exercised and approximately 80,000 shares of Common Stock were reserved for issuance upon exercise of outstanding options. Except as to options previously granted and outstanding under it, the 1993 Plan terminated at midnight on February 1, 2003.

The 1993 Plan provided for the grant of both incentive stock options ("ISOs") and non-qualified stock options ("NQOs"). ISOs granted under the 1993 Plan are intended to qualify as "incentive stock options" within the meaning of Section 422 of the Code of 1986, as amended. NQOs granted under the 1993 Plan are intended not to qualify as ISOs under the Code. Options granted under the 1993 Plan generally have a term of not more that 10 years and vest no sooner than 6 months after the date of grant.

No ISO could be granted under the 1993 Plan to any person who, at the time of the grant, owned (or was deemed to own) stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or any affiliate of the Company, unless the option exercise price was at

least 110% of the fair market value of the stock subject to the option on the date of grant, and the term of the option did not exceed five years from the date of grant. For incentive stock option grants, the aggregate fair market value, determined at the time of grant, of the shares of Common Stock with respect to which such options were exercisable for the first time by an optionee during any calendar year (under all such plans of the Company and its affiliates) may not exceed $100,000.

The Company did not grant any options to its executive officers under the 1993 Plan during the fiscal year ended December 31, 2003 nor during the fiscal year ended December 31, 2002.

1996 STOCK OPTION PLAN

In May 1996, the Board of Directors adopted the 1996 Stock Option Plan (the "1996 Plan"). The 1993 Plan authorizes the granting of options to purchase up to a maximum 600,000 shares of Common Stock to qualified officers, key employees, directors and employees of companies that do business with the Company. As of December 31, 2003, none of the options available for grant under the 1996 Plan had been exercised and no shares of Common Stock were reserved for issuance upon exercise of outstanding options. The 1996 Plan terminated at midnight on February 1, 2003.

The Company did not grant any options to its executive officers under the 1996 Plan during the fiscal year ended December 31, 2003 nor during the fiscal year ended December 31, 2002.

2000 NONSTATUTORY STOCK OPTION PLAN

In May 2000, the Board of Directors adopted the Prism Software Corporation 2000 Nonstatutory Stock Option Plan (the "2000 Plan"). The 2000 Plan authorizes the granting of options to purchase up to a maximum of 3,000,000 shares of Common Stock to qualified employees and directors of the Company. As of December 31, 2003, none of the options available for grant under the 2000 Plan had been exercised, approximately 1,720,000 shares of Common Stock were reserved for issuance upon exercise of outstanding options and approximately 1,280,000 shares of Common Stock remained available for grant thereunder. Except as to options previously granted and outstanding under it, the 2000 Plan will terminate on May 4, 2010, unless sooner terminated by the Board of Directors.

The 2000 Plan provides only for the grant of non-qualified stock options. Options granted under the 2000 Plan generally have a term of not more that 10 years. Vesting periods, if any, are at the discretion of the Board of Directors at the time of grant. The exercise price of options granted under the 2000 Plan is to be at least 85% of the fair market value of the Company's Common Stock at the date of grant, as determined by the Board of Directors. The 2000 Plan provides for "cashless exercise" of the options, so the optionee has the choice of paying cash to exercise the options, surrendering Common Stock owned by him with a value equal to the exercise price, or issuing a promissory note for the exercise price.

The Company granted options to purchase 600,000 shares of its Common Stock to its executive officers under the 2000 Plan during the fiscal year ended December 31, 2003. The Company did not grant any options to its executive officers under the 2000 Plan during the fiscal year ended December 31, 2002.

MANAGEMENT OPTIONS OF E. TED DANIELS

Under his employment agreement, and distinct from the Company's other option plans, Mr. Daniels had been granted non-qualified options to purchase shares of the Company's Common Stock, such as to maintain ownership of 8% of the Company's fully-diluted Common Stock (subject to certain anti-dilution adjustments). Except for options to purchase 2,000,000 shares that were subsequently exercised in 2003, as of December 31, 2002, Mr. Daniels had voluntarily cancelled all rights to such options that had previously been granted and any additional such options that would have otherwise been granted to him in the future under his employment agreement, therefore no such options existed as of December 31, 2003. However, in February 2004, Mr. Daniels claimed that he is entitled to receive replacement options (that would expire in October 2004) on modified terms that would be similar to the ones he had previously cancelled. (Also see "Legal Proceedings")

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

The following table sets forth information regarding the beneficial ownership of the Common Stock of the Company as of March 31, 2004, by (i) each person known by the Company to beneficially own 5% or more of the outstanding Common Stock of the Company; (ii) each of the Company's directors; (iii) each of the Company's Executive Officers; and (iv) all directors and Executive Officers of the Company as a group.

NAME AND ADDRESS OF BENEFICIAL OWNER	OUTSTANDING COMMON STOCK	PERCENTAGE OF SHARES OUTSTANDING	COMMON STOCK EQUIVALENTS OF OPTIONS OR NOTES	TOTAL NUMBER OF SHARES BENEFICIALLY OWNED (1)
E. Ted Daniels 42240 Adams Street Bermuda Dunes, CA 92201	4,440,000	3%	0	4,440,000
David Ayres c/o Prism Software Corporation 23696 Birtcher Lake Forest, CA 92630	615,000	*	500,000	1,115,000
Carl S. von Bibra 1637 Spruce Street South Pasadena, CA 91030	33,607,500	24%	272,639,461	306,246,961
The Conrad von Bibra Revocable Trust 1415 Milan Ave. South Pasadena, CA 91030	60,880,856	43%	497,228,225	558,109,081
Michael Cheever c/o Prism Software Corporation 23696 Birtcher Lake Forest, CA 92630	20,000	*	240,000	260,000
All Directors and Executive Officers of the Company as a Group (5 persons)	99,563,356	70%	770,607,686	870,171,042

* Less than 0.5%

(1) Beneficial ownership is determined in accordance with the rules of the Securities and Exchange Commission and generally includes voting or investment power with respect to securities. Shares of Common Stock subject to securities currently convertible, or convertible within 60 days after March 31, 2004, are deemed to be outstanding in calculating the percentage ownership of a person or group but are not deemed to be outstanding as to any other person or group. Except as indicated by footnote, and subject to community property laws where applicable, the persons named in the table above have sole voting and investment power with respect to all shares of Common Stock shown as beneficially owned by them. Currently there are 300,000,000 shares of Common Stock authorized of which 141,591,534 are issued and outstanding. The percentage column of common stock beneficially owned shows the percent each person would own if he exercised all his conversion or option privileges and all of the others did not.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

REPURCHASE OF COMMON STOCK

In December 2002, the Company repurchased 500,000 shares of its Common Stock from Carl von Bibra for $2,500, or $0.005 per share. Mr. von Bibra is affiliate of the Company by virtue of his beneficial ownership of more than 5% of the Company's outstanding Common Stock.

CERTAIN NOTES AND NOTE CONVERSIONS

From January 2002 to February 2003, the Company borrowed approximately $1,014,000 from the Conrad von Bibra Revocable Trust ("Conrad von Bibra"), and approximately $732,000 from Carl von Bibra. All such debt was restructured under a Loan Agreement in March 2003 (see below).

In March 2003, the Company refinanced most of its debt and related accrued interest with Conrad von Bibra and Carl von Bibra under a Loan Agreement, and entered into a Credit Agreement with Conrad von Bibra. From March to December 2003, the Company borrowed approximately $1,060,000 from Conrad von Bibra under the Credit Agreement. All debt under these agreements are due upon demand, bear interest at the rate of 8% per annum and were convertible into shares of Common Stock at the initial rate of $0.05 per share (subject to certain anti-dilution adjustments) at the option of the holder. In accordance with the anti-dilution provisions of these agreements, the conversion rate on this debt was subsequently adjusted to $0.01 per share upon the issuance of a separate note in March 2003 (see below). In addition, these agreements included provisions for warrants that were subsequently waived by Conrad von Bibra and Carl von Bibra in light of the conversion rate being reduced to $0.01 per share. Borrowings made under the Credit Agreement are secured by the Company's assets in accordance with a related Security Agreement.

Also in March 2003, the Company borrowed an additional $100,000 from Conrad von Bibra under a separate Convertible Promissory Note that is secured by the Company's assets. This debt is due upon demand, bears interest at the rate of 8% per annum and is convertible into shares of Common Stock at the rate of $0.01 per share (subject to certain anti-dilution adjustments) at the option of the holder.

No commissions were paid in connection with any of these transactions. Conrad von Bibra and Carl von Bibra are affiliates of the Company by virtue of their beneficial ownership of more than 5% of the Company's outstanding Common Stock.

The Company believes that such transactions were exempt from the registration requirements of the Securities Act of 1933, as amended, by virtue of Section 4(2) thereof or Regulation D promulgated thereunder, as a transaction by an issuer not involving a public offering.

ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits

3.1. Certificate of Incorporation of Prism Software Corporation ("the Company") (1) (Exhibit 3.1)

3.2. Bylaws of the Company (1) (Exhibit 3.2)

3.3. Amendments dated February 24, 1998 and May 5, 1999 to the Company's Certificate of Incorporation (2) (Exhibit 3.3)

3.4. Amendment dated September 18, 2000 to the Company's Certificate of Incorporation (4) (Exhibit 10.1)

4.1. Specimen Common Stock certificate of the Company (1) (Exhibit 4.1)

4.2. Certificate of Designation of $5.00, 10% Class A Cumulative Convertible Preferred Stock, as amended to date (2) (Exhibit 4.3)

4.3. Form of Warrant for Common Stock, issued 2000-2001 (5) (Exhibit 4.5)

10.1. Prism Software Corporation Amended and Restated 1993 Stock Option Plan ("1993 Plan") (1) (Exhibit 10.1)

10.2. Form of Employee Installment Incentive Stock Option and Nonstatutory Stock Option Agreement pertaining to the 1993 Plan (1) (Exhibit 10.2)

10.3. Prism Software Corporation 2000 Nonstatutory Stock Option Plan ("2000 Plan") (3) (Exhibit 10.1)

10.4. Form of Stock Option Agreement pertaining to the 2000 Plan (3) (Exhibit 10.2)

10.5. Office lease dated April 21, 1994, by and between the Company and the Mort Herrmann Family Trust (1) (Exhibit 10.6)

10.6. Amendments dated April 15, 1999 to the April 21, 1994 office lease by and between the Company and the Mort Herrmann Family Trust (2) (Exhibit 10.7)

10.7. Promissory Note dated August 9, 1991, made to the order of George E.

Williams in the principal amount of $22,000 (2) (Exhibit 10.11)

10.8. Promissory Note dated December 9, 1991, made to the order of Personal Computer Products, Inc. in the principal amount of $40,000 (2) (Exhibit 10.12)

10.9. Promissory Note dated April 15, 1993, made to the order of James or Judith Bone in the principal amount of $63,031 (2) (Exhibit 10.13)

10.10. Promissory Note dated February 17, 1994, made to the order of Shirley McGarvey in the principal amount of $35,000 (2) (Exhibit 10.14)

10.11. Promissory Note dated December 31, 1994, made to the order of James Bone in the principal amount of $70,168 (2) (Exhibit 10.15)

10.12. Promissory Note dated December 31, 1994, made to the order of Allard Villere in the principal amount of $15,996 (2) (Exhibit 10.16)

10.13. Convertible Promissory Note dated July 29, 1995, made to the order of Northstar Capital Partners, LP in the principal amount of $40,000; note is currently held by Carl von Bibra (1) (Exhibit 10.15)

10.14. Amendment dated October 20, 1997 to the July 29, 1995 Convertible Promissory Note made to the order of Northstar Capital Partners, LP in the principal amount of $40,000; note is currently held by Carl von Bibra (2) (Exhibit 10.18)

10.15. Convertible Promissory Note dated July 29, 1995, made to the order of Peachtree Capital Partners, LP in the principal amount of $60,000; note is currently held by Carl von Bibra (1) (Exhibit 10.14)

10.16. Amendment dated October 20, 1997 to the July 29, 1995 Convertible Promissory Note made to the order of Peachtree Capital Partners, LP in the principal amount of $60,000; note is currently held by Carl von Bibra (2) (Exhibit 10.20)

10.17. Form of Convertible Promissory Notes dated September 25, 2000 and September 29, 2000, aggregate principal amount of $40,206; notes are currently held by Carl von Bibra and Conrad von Bibra (5) (Exhibit 10.24)

10.18. Form of Convertible Promissory Notes dated October 4, 2000, aggregate principal amount of $19,330; notes are currently held by Carl von Bibra (5) (Exhibit 10.25)

10.19. Letter Agreement dated December 31, 2002 with E. Ted Daniels to cancel all but 2,000,000 of the options under his April 21, 1995 Non-Qualified Stock Option Agreement, as amended (6) (Exhibit 10.30)

10.20. Loan Agreement dated March 13, 2003 by and between the Conrad von Bibra Revocable Trust and Carl von Bibra and Prism Software (7) (Exhibit 10.1)

10.21. Credit Agreement dated March 15, 2003 by and between the Conrad von

Bibra Revocable Trust and Prism Software (7) (Exhibit 10.3)

10.22. Promissory Note dated March 27, 2003 by and between the Conrad von Bibra Revocable Trust and Prism Software (7) (Exhibit 10.4)

10.23. Security Agreement dated March 27, 2003 by and between the Conrad von Bibra Revocable Trust and Prism Software (7) (Exhibit 10.5)

31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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(1) Incorporated by reference to the Exhibit identified in parentheses, filed as an exhibit in the Company's Registration Statement on Form SB-2 (SEC File No. 333-5450-LA).

(2) Incorporated by reference to the Exhibit identified in parentheses, filed as an exhibit in the Company's Annual Report on Form 10-KSB for the fiscal year ended December 31, 1998.

(3) Incorporated by reference to the Exhibit identified in parentheses, filed as an exhibit in the Company's Quarterly Report on Form 10-QSB for the quarter ended June 30, 2000.

(4) Incorporated by reference to the Exhibit identified in parentheses, filed as an exhibit in the Company's Quarterly Report on Form 10-QSB for the quarter ended September 30, 2000.

(5) Incorporated by reference to the Exhibit identified in parentheses, filed as an exhibit in the Company's Annual Report on Form 10-KSB for the fiscal year ended December 31, 2000.

(6) Incorporated by reference to the Exhibit identified in parentheses, filed as an exhibit in the Company's Annual Report on Form 10-KSB for the fiscal year ended December 31, 2002.

(7) Incorporated by reference to the Exhibit identified in parentheses, filed as an exhibit in the Company's Quarterly Report on Form 10-QSB for the quarter ended March 31, 2003.

(b) Reports on Form 8-K

None.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

The Company incurred Audit Fees of $38,400 with its principal accountant in the fiscal year ended December 31, 2003. The Company incurred Audit Fees of $38,400 with its principal accountant in the fiscal year ended December 31, 2002. The Company incurred no other fees with its principal accountant in either of the two fiscal years referenced.

The Company has no audit committee. The Board of Directors' policy is to pre-approve all audit and permissible non-audit services provided by the independent auditors. These services may include audit services, audit-related services, tax services and other services. Pre-approval would generally be provided for up to one year and any pre-approval would be detailed as to the particular service or category of services, and would be subject to a specific budget. The independent auditors and management are required to periodically report to the Board of Directors regarding the extent of services provided by the independent auditors in accordance with this pre-approval, and the fees for the services performed to date. The Board of Directors may also pre-approve particular services on a case-by-case basis.

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PRISM SOFTWARE CORPORATION

Dated: April 14, 2004 By: /s/ David Ayres

David Ayres, Director and President
(Principal Executive Officer)

In accordance with the Exchange Act, this report has been signed by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Dated: April 14, 2004 By: /s/ Carl S. von Bibra

Carl S. von Bibra, Director and Chairman of the Board

Dated: April 14, 2004 By: /s/ David Ayres

David Ayres, Director and President
(Principal Executive Officer)

Dated: April 14, 2004 By: /s/ Conrad von Bibra

Conrad von Bibra, Director and Secretary

Dated: April 14, 2004 By: /s/ Michael Cheever

Michael Cheever, Controller

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PRISM SOFTWARE CORPORATION

FINANCIAL STATEMENTS

DECEMBER 31, 2003

F-1

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

The Board of Directors and Stockholders
Prism Software Corporation

We have audited the accompanying balance sheet of Prism Software Corporation (the "Company") as of December 31, 2003, and the related statements of operations, stockholders' deficit and cash flows for each of the years in the two-year period ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Prism Software Corporation as of December 31, 2003 and the results of its operations and cash flows for each of the years in the two-year period ended December 31, 2003 in conformity with generally accepted accounting principles in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 12 to the financial statements, the Company's continued operating losses, limited capital and stockholders' deficit raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to this matter are also described in Note 12. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/S/ CACCIAMATTA ACCOUNTANCY CORPORATION

Irvine, California
April 12, 2004

PRISM SOFTWARE CORPORATION
Balance Sheet

	DECEMBER 31, 2003
ASSETS	
Current assets	
Cash	$ 12,024
Accounts receivable, net of allowance for doubtful accounts of $4,369	46,623
Inventory	451
Total current assets	59,098
Equipment, net	23,809
Other	9,978
	$ 92,885
LIABILITIES AND STOCKHOLDERS' DEFICIT	
Current liabilities	
Notes payable - stockholders	$ 7,389,268
Accrued interest - stockholders	688,504
Accrued expenses - stockholders	30,203
Notes payable - other	38,700
Accounts payable	404,070
Accrued expenses	435,039
Deferred revenue	105,257
Total current liabilities	9,091,041
Commitments and contingencies	--
Stockholders' deficit	
Preferred stock - 5,000,000 shares authorized, $.01 par value; Series A - 78,800 shares issued and outstanding	788
Common stock - 300,000,000 shares authorized, $.01 par value; 141,591,534 shares issued and outstanding	1,415,915
Additional paid-in capital	11,394,263
Accumulated deficit	(21,809,122)

Total stockholders' deficit	(8,998,156)
	$ 92,885

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

PRISM SOFTWARE CORPORATION
Statements of Operations

	YEAR ENDED DECEMBER 31,	
	2003	2002
Net sales		
Products	$ 220,068	$ 254,837
Services	270,770	288,659
	490,838	543,496
Cost of sales		
Products	18,023	50,566
Services	70,918	79,653
	88,941	130,219
Gross profit	401,897	413,277
Operating expenses		
Selling and administrative	1,675,957	2,027,774
Research and development	261,786	306,241
	1,937,743	2,334,015
Loss from operations	(1,535,846)	(1,920,738)
Interest expense - stockholders	(3,714,321)	(381,762)
Interest expense	(3,869)	(4,871)
Net loss	$ (5,254,036)	$ (2,307,371)
Basic and diluted net loss per common share	$ (0.04)	$ (0.02)

Basic and diluted weighted average number of common shares outstanding	140,446,000	140,089,000

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

PRISM SOFTWARE CORPORATION
Stockholders' Deficit
Years Ended December 31, 2003 and 2002

	SERIES A PREFERRED STOCK		COMMON STOCK		ADDITIONAL PAID-IN CAPITAL
	SHARES	AMOUNT	SHARES	AMOUNT	
Balance, December 31, 2001	78,800	788	140,091,534	1,400,915	8,205,130
Repurchase of common stock for cash	-	-	(500,000)	(5,000)	2,500
Issuance of stock options	-	-	-	-	34,563
Net loss	-	-	-	-	-
Balance, December 31, 2002	78,800	$ 788	139,591,534	$1,395,915	$ 8,242,193
Intrinsic value of beneficial conversion feature	-	-	-	-	3,172,070
Exercise of stock options	-	-	2,000,000	20,000	(20,000
Net loss	-	-	-	-	-
Balance, December 31, 2003	78,800	$ 788	141,591,534	$ 1,415,915	$ 11,394,263

The accompanying notes are an integral part of these financial state

PRISM SOFTWARE CORPORATION
Statements of Cash Flows

	YEAR ENDED 2003
CASH FLOWS FROM OPERATING ACTIVITIES	
Net loss	$(5,254,036)
Adjustments to reconcile net loss to net cash used by operating activities:	
Loss on disposal of assets	1,787
Depreciation	13,124
Issuance of stock options	--
Amortization of beneficial conversion feature	3,172,070
(Increase) decrease in assets	
Accounts receivable	(12,307)
Inventory	41
Licenses and other assets	1,655
Increase (decrease) in liabilities	
Accounts payable	52,898
Accrued expenses	664,149
Deferred revenue	(7,501)
Net cash used by operating activities	(1,368,120)
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of equipment	(8,634)
CASH FLOWS FROM FINANCING ACTIVITIES	
Proceeds from issuance of notes payable - stockholders	1,381,000
Payments on notes	--
Repurchase of common stock	--
Net cash provided by financing activities	1,381,000
Net increase (decrease) in cash	4,246
Cash, beginning of period	7,778
Cash, end of period	$ 12,024
Supplemental disclosures:	
Cash paid for interest	$ --
Cash paid for income tax	$ --
Non-cash investing and financing activities:	
Conversion of stockholders interest payable to notes payable	$ 737,938

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

PRISM SOFTWARE CORPORATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Prism Software Corporation (the "Company") was organized under the laws of Delaware in 1992. The Company specializes in enterprise document and content management solutions. The Company's products and expertise lie in electronic document formation, document management, and print stream conversion solutions. The Company's customer base includes organizations that use its solutions in managing high-volume, large scale document printing in a variety of markets.

Concentrations of risk

In 2003 and 2002 the three largest customers accounted for 42% and 34%, respectively, of sales. At December 31, 2003 and 2002, the three largest accounts receivable totaled 83% and 80%, respectively.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Inventory

Inventory is reported at the lower of cost (determined on the first-in-first-out method) or market and consists principally of finished goods.

Equipment

Equipment is recorded at cost. Depreciation is provided over the estimated useful lives of the related assets, generally three to five years, using the straight-line method.

Software Development Costs

Development costs related to new software products and enhancements to existing software products are expensed as incurred until technological feasibility has been established. After technological feasibility is established, any additional costs are capitalized in accordance with Statement of Financial Accounting Standards No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed." The Company believes the establishment of technological feasibility occurs concurrently with the completion of software development. Accordingly, no costs have been capitalized as of December 31, 2003.

PRISM SOFTWARE CORPORATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenue recognition

Revenues from the licensing of computer software products are recognized upon delivery of the products to customers, as there are no significant obligations remaining after the delivery date. Revenues related to service agreements are deferred and recognized over the terms of the related agreements, generally 12 months. Payments are generally due within 30 days. Management's review of collectibility is an ongoing process, and reserves are made based on the Company's historical experience with each customer and its knowledge of each receivable.

Income taxes

The Company accounts for income taxes under the asset and liability method. Deferred income taxes are recognized for the tax consequences of temporary differences by applying enacted statutory rates applicable to future years to the difference between the financial statement carrying amounts and the tax basis of existing assets and liabilities.

Stock-based compensation

The Company has elected to continue to account for stock-based compensation using the intrinsic value method, as described in Accounting Principles Board Opinion 25. Accordingly, compensation is measured as the excess, if any, of the quoted market price of the Company's common stock at the date of grant over the amount an employee is required to pay to acquire the stock. Compensation costs reported in 2003 and 2002 were $0 and $34,563, respectively. Companies using APB 25 to report stock-based compensation are required under SFAS 123 to disclose the estimated fair value of options granted.

As prescribed under SFAS 123, the Company used the Black-Scholes Option Pricing Model to estimate the fair value of the options granted in 2003 and 2002 using the following assumptions.

	2003	2002
Expected life (years)	10 years	10 years
Risk-free interest rate	1.875%	6.04%
Volatility	50%	50%

Had the Company chosen to report the stock-based compensation at its estimated fair value, net loss and net loss per share would have increased slightly.

PRISM SOFTWARE CORPORATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

	2003	2002
Net loss		
As reported	$(5,254,036)	$(2,307,371)
Estimated fair value of compensation	(7,729)	(18,149)
Pro forma	$(5,261,765)	$(2,325,520)
Basic and diluted loss per share		
As reported	$ (0.04)	$ (0.02)
Pro forma	$ (0.04)	$ (0.02)

Cash and equivalents

The Company considers all liquid investments with a maturity of three months or less from the date of purchase that are readily convertible into cash to be cash equivalents. Balances in bank accounts may, from time to time, exceed federally insured limits. The Company believes that its loss exposure is limited.

Advertising costs

Advertising costs are expensed as incurred. During 2003 and 2002, advertising costs totalled approximately $19,600 and $47,500, respectively.

Basic and diluted net loss per share

Basic net loss per share is based upon the weighted average number of common shares outstanding. Diluted net loss per share is based on the assumption that all dilutive convertible shares and stock options were converted or exercised. Dilution is computed by applying the treasury stock method. Under this method, options and warrants are assumed to be exercised at the beginning of the period (or at the time of issuance, if later), and as if funds obtained thereby were used to purchase common stock at the average market price during the period.

Fair value of financial instruments

The fair value of the notes payable to stockholders cannot be determined due to the related party nature of the obligations. The fair value of notes payable are based on interest rates available to the Company at quoted prices.

Research and development costs

Research and development costs are charged to expense as incurred.

PRISM SOFTWARE CORPORATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Recent accounting pronouncements

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations." SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This Statement is effective for financial statements issued for fiscal years beginning after June 15, 2002. The Company's reported operating results, financial position and existing financial statement disclosure have not been affected by SFAS 143.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets and broadens the definition of what constitutes a discontinued operation and how the results of a discontinued operation are to be measured and presented. The provisions of SFAS 144 became effective for financial statements issued for fiscal years beginning after December 15, 2001. The Company's reported operating results, financial position and financial statement disclosures have not been affected by SFAS 144.

In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." SFAS No. 145 requires most gains and losses on extinguishment of debt to be classified as income or loss from continuing operations rather than as extraordinary items as previously required. SFAS No. 145 also amends SFAS No. 13 "Accounting for leases", to require certain lease modifications to be treated as sale-leaseback transactions. Certain provisions of SFAS No. 145 are effective for transactions occurring after May 15, 2002, while other provisions are effective for fiscal years beginning after May 15, 2002. The Company's reported operating results, financial position and financial statement disclosures have not been affected by SFAS 145.

In July 2002, the FASB issued SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities" FAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies the Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity Including Certain Costs Incurred in a Restructuring." FAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred, whereas EITF 94-3 had recognized the liability at the commitment date to an exit plan. The provisions of SFAS 146 became effective for exit or disposal activities initiated after December 31, 2002 and did not materially impact the Company's financial position or results of operations.

PRISM SOFTWARE CORPORATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Recent accounting pronouncements (continued)

In November 2002, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others (an interpretation of FASB Statements No. 5, 57 and 107 and rescission of FASB Interpretation No. 34)". FIN 45 clarifies the requirements of FASB Statement No. 5, "Accounting for Contingencies". It requires that upon issuance of a guarantee, the guarantor must recognize a liability for the fair value of the obligation it assumes under that guarantee regardless of whether or not the guarantor receives separate identifiable consideration (i.e., a premium). The Company adopted the disclosure requirements in 2002 and the initial recognition and measurement provisions in 2003. The adoption of FIN 45 did not have a material impact on the Company's financial statements.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity". This statement establishes standards for the classification and measurement of financial instruments that possess characteristics similar to both liability and equity instruments. SFAS No. 150 also addresses the classification of certain financial instruments that include an obligation to issue equity shares. On October 29, 2003, the FASB voted to defer, for an indefinite period, the application of certain provisions of the guidance in SFAS No. 150. The FASB decided to defer the application of certain aspects of Statement 150 until it could consider some of the resulting implementation issues. The Company has adopted certain provisions of SFAS No. 150 which did not have a material impact on the Company's financial condition or results of operations. The Company does not believe the effect of the provisions of SFAS No. 150 that have been deferred to future periods will have a material impact on the Company's financial statements.

2. EQUIPMENT

Furniture and equipment	$ 28,107

Computer equipment and software	183,782
	211,889
Accumulated depreciation and amortization	(188,080)
	$ 23,809

Depreciation expense charged to operations was $13,124 and $48,013 in 2003 and 2002, respectively.

PRISM SOFTWARE CORPORATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

3. ACCRUED EXPENSES

Wages and benefits	$ 241,398
Interest other	41,157
Sales commissions	81,159
Other	71,325
	$ 435,039

4. NOTES PAYABLE

All notes are unsecured unless otherwise described.

Stockholders

9% to 10%, past due August 1996	$ 129,894
8%, convertible into common stock at $.10 per share at holders' option, past due December 1999	100,000
8%, convertible into common stock at $.05 per share at holders' option, past due December 2001	59,536
8%, convertible into common stock at $.01 per share at holders' option, due upon demand	5,939,838
8%, convertible into common stock at $.01 per share at holders' option, due upon demand, secured by the Company's assets	1,160,000

	$7,389,268
Other	$ 38,700

Certain portions of the $5,939,838 and the $1,160,000 borrowings described above contain a beneficial conversion feature equal to or less than the face value of each applicable borrowing, which is reflected in additional paid-in capital in the accompanying financial statements. During 2003 and 2002, $3,172,070 and $0, respectively, of the beneficial conversion feature was amortized and included as part of the caption "Interest expense - stockholders" in the accompanying statements of operations.

PRISM SOFTWARE CORPORATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

5. PREFERRED STOCK

The Company has authorized 5,000,000 shares of $0.01 par value preferred stock, of which 100,000 shares have been designated as $5.00 Series A 10% cumulative convertible preferred stock (Series A).

The holders of Series A are entitled to receive, when and as declared by the Company's Board of Directors (the Board), cumulative annual dividends of $0.50 per share commencing upon issuance and payable semi-annually. Series A has a liquidation preference of $5.00 per share plus any accrued but unpaid dividends. Series A is redeemable at the Company's election upon 30 days' notice at a price per share of $5.50 plus accrued but unpaid dividends thereon. The 78,800 shares of Series A outstanding at December 31, 2003 are currently convertible at the election of the holders into 3,419,920 shares of common stock. The conversion rate is subject to the adjustments set forth in the certificate of designation for Series A based on the current market price of the Company's common stock. The holders of the Series A are entitled to cast one non-cumulative vote per share of Series A in all matters presented to the shareholders, and the majority of holders of Series A, voting as a class, have certain protective rights relating to their dividends and preference rights. No amounts have been accreted in relation to the Series A redemption as the likelihood of the Company electing to repurchase is remote.

At December 31, 2003, the amount of undeclared dividends in arrears on the Series A was $454,850 ($5.77 per share).

6. COMMON STOCK

In 2003, the Company issued 2,000,000 shares of common stock to its then-current President and Chief Executive Officer upon the exercise of options.

7. STOCK OPTIONS

Financing Options

In 1994, the Company issued options to certain lenders to acquire up to 325,093 shares of the Company's common stock in connection with loans made to the Company. The options vested at issuance, were exercisable at $2.00 per share and expired in January 2004.

1993 Stock Option Plan

The Company's 1993 Stock Option Plan provides for the issuance of options to employees, directors, officers, and advisors of the Company to acquire up to 630,000 shares of the Company's common stock. Options issued under this plan are generally granted at estimated market value, vest at varying rates and expire within ten years from the date of grant or within 90 days after termination of employment. Except as to options previously granted and outstanding under it, the 1993 Stock Option Plan terminated at midnight on February 1, 2003.

7. STOCK OPTIONS (CONTINUED)

2000 Stock Option Plan

The Company's 2000 Stock Option Plan provides for the issuance of options to employees, directors, officers and advisors of the Company to acquire up to 3,000,000 shares of common stock. Options issued under this plan are generally exercisable at 85% of the market value on the date of grant, vest over three years and expire within ten years from the date of grant or within 90 days after termination of employment. Except as to options previously granted and outstanding under it, the 2000 Stock Option Plan will terminate on May 4, 2010, unless sooner terminated by the Board of Directors.

Other Management Options

Under his employment agreement, the Company's previous President and Chief Executive Officer had been granted non-qualified options to purchase shares of the Company's common stock, such as to maintain ownership of 8% of the Company's fully diluted common stock (subject to certain anti-dilution adjustments). In 2002, this executive voluntarily cancelled his rights to all but 2,000,000 options previously granted and any additional options that would have been granted to him under his employment agreement. During 2003, this executive exercised the remaining 2,000,000 options under his agreement. Therefore, no such options were outstanding at December 31, 2003. However, in February 2004, this former executive claimed that he is entitled to receive replacement options (that would expire in October 2004) on modified terms that would be similar to the ones he had previously cancelled.

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7. STOCK OPTIONS (CONTINUED)

Stock option activity for the years ended December 31, 2003 and 2002 follows:

	FINANCING OPTIONS	WEIGHTED AVERAGE OPTION PRICE	1993 PLAN	WEIGHTED AVERAGE OPTION PRICE	2000 PLAN
December 31, 2001	197,093	2.00	228,600	1.60	1,865,000
Granted	-	-	25,000	0.05	75,000
Expired or Cancelled	-	-	-	-	(1,025,000)
Exercised	-	-	-	-	-
December 31, 2002	197,093	2.00	253,600	1.45	915,000
Granted	-	-	-	-	1,000,000
Expired or Cancelled	-	-	(173,600)	1.99	(195,000)
Exercised	-	-	-	-	-
December 31, 2003	197,093	2.00	80,000	0.28	1,720,000

The following information applies to options outstanding at December 31, 2003:

	NUMBER OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE (YEARS)	WEIGHTED AVERAGE EXERCISE PRICE	EX

Financing options	197,093	1	$ 2.00
1993 stock option plan	80,000	2	$ 0.28
2000 stock option plan	1,720,000	8	$ 0.04
	1,997,093		

8. WARRANTS

The Company has outstanding warrants that were issued in 2001 in relation to a private placement offering. No value has been ascribed to the warrants as (1) the warrants were issued at exercise prices equal to or greater than the fair value of the Company's common stock on the date of issuance and (2) there is no market for the warrants. At December 31, 2003, the only warrants outstanding were the 2,500,000 warrants issued in August 2001 that expire in August 2004.

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9. BASIC AND DILUTED NET LOSS PER SHARE

The following table illustrates the reconciliation of the numerators and denominators of the basic and diluted loss per share computations.

	2003	2002
Numerator		
Net loss	$ (5,254,036)	$ (2,307,371)
Preferred dividends	(39,400)	(39,400)
Net loss	$ (5,293,436)	$ (2,346,771)
Denominator		
Basic and diluted weighted average number of common shares outstanding during the period	140,446,000	140,089,000
Basic and diluted net loss per share	$ (0.04)	$ (0.02)

The following incremental common shares associated with outstanding options, warrants and convertible debt are not included in the denominators above as their effect would be anti-dilutive:

	EQUIVALENT NUMBER OF COMMON SHARES AT DECEMBER 31, 2003	2002
Options	1,997,093	3,365,693
Warrants	2,500,000	5,940,000
Convertible debt	755,598,167	84,170,451

10. INCOME TAXES

The Company recognizes deferred tax assets and liabilities for temporary differences between the financial reporting and tax bases of its assets and liabilities. Deferred tax assets are reduced by a valuation allowance when deemed appropriate.

The Company has deferred tax assets of approximately $7,888,000 at December 31, 2003 relating to its net operating losses. The Company provided a 100% valuation allowance for these deferred tax assets. Accordingly, the Company recorded no benefit for income taxes during the periods presented. During, 2003 and 2002 the Company's valuation allowance increased approximately $2,021,000 and $916,000, respectively.

10. INCOME TAXES (CONTINUED)

At December 31, 2003, the Company has net operating loss carryforwards for federal tax purposes of approximately $17,529,000, which will expire beginning in 2004 through 2023.

11. COMMITMENTS AND CONTINGENCIES

Legal proceedings

In February 2004, the Company's previous President and Chief Executive Officer filed for arbitration in a dispute with the Company, claiming that the Company owes him unpaid back wages and interest thereon through his last day of employment (January 23, 2004), future wages through September 14, 2004, and stock options (Note 7). The Company disputes all claims. The arbitration proceedings have not been scheduled.

Leases

The Company's office lease expires March 31, 2004. A new lease is to be negotiated, and its terms are not expected to vary significantly from the current lease terms. The current lease provides for a basic rent of $8,287 per month. Rent expense was $98,433 and $95,400 in 2003 and 2002, respectively.

12. GOING CONCERN

The Company's continued operating losses, limited capital and stockholders' deficit raise substantial doubt about its ability to continue as a going concern. Management's plans to continue strengthening the Company's financial condition and operations include: restructuring the Company's debt and other liabilities, monitoring costs and cash flow activities, expanding operations through potential cooperative ventures, continuing to upgrade sales and marketing efforts and upgrading customer service and product development efforts. The Company also intends to continue raising capital to fund its operations, but no assurance can be given that such funding will be available.