

DAILY JOURNAL CORP  
Form 10-Q  
May 14, 2007  
Table of Contents

---

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

---

**FORM 10-Q**

---

(Mark One)

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

For the quarterly period ended March 31, 2007

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-14665

---

**DAILY JOURNAL CORPORATION**

(Exact name of registrant as specified in its charter)

---

South Carolina  
(State or other jurisdiction of  
incorporation or organization)

915 East First Street

95-4133299  
(I.R.S. Employer

Identification No.)

90012-4050

Edgar Filing: DAILY JOURNAL CORP - Form 10-Q

**Los Angeles, California**  
(Address of principal executive offices)

(Zip code)

**(213) 229-5300**

(Registrant's telephone number, including area code)

**None**

(Former name, former address and former fiscal year, if changed since last report)

---

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes:  No:

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one)

Large Accelerated Filer:  Accelerated Filer:  Non-accelerated Filer:

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

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

Class
Common Stock, par value \$.01 per share

Outstanding at April 30, 2007
1,500,299 shares

---

**Table of Contents**

DAILY JOURNAL CORPORATION

INDEX

	<b>Page Nos.</b>
<b><u>PART I Financial Information</u></b>	
<u>Item 1. Financial Statements</u>	
<u>Consolidated Balance Sheets March 31, 2007 and September 30, 2006</u>	3
<u>Consolidated Statements of Income Three months ended March 31, 2007 and 2006</u>	4
<u>Consolidated Statements of Income Six months ended March 31, 2007 and 2006</u>	5
<u>Consolidated Statements of Cash Flows Six months ended March 31, 2007 and 2006</u>	6
<u>Notes to Consolidated Financial Statements</u>	7
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	11
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	14
<u>Item 4. Controls and Procedures</u>	14
<b><u>Part II Other Information</u></b>	
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	15
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	15
<u>Item 6. Exhibits</u>	16

**Table of Contents**

## PART I

## Item 1. FINANCIAL STATEMENTS

## DAILY JOURNAL CORPORATION

## CONSOLIDATED BALANCE SHEETS

	March 31	September 30
	2007	2006
	(Unaudited)	
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 1,091,000	\$ 617,000
U.S. Treasury Notes and Bills	10,059,000	8,953,000
Accounts receivable, less allowance for doubtful accounts of \$200,000 at March 31, 2007 and September 30, 2006	5,063,000	4,490,000
Inventories	44,000	46,000
Prepaid expenses and other assets	238,000	132,000
Deferred income taxes	1,615,000	1,710,000
<b>Total current assets</b>	<b>18,110,000</b>	<b>15,948,000</b>
Property, plant and equipment, at cost		
Land, buildings and improvements	12,941,000	12,922,000
Furniture, office equipment and computer software	3,687,000	3,868,000
Machinery and equipment	1,942,000	1,907,000
	18,570,000	18,697,000
Less accumulated depreciation	(6,906,000)	(6,780,000)
	11,664,000	11,917,000
U.S. Treasury Notes	7,094,000	6,977,000
Deferred income taxes	991,000	861,000
	<b>\$ 37,859,000</b>	<b>\$ 35,703,000</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities		
Accounts payable	\$ 4,282,000	\$ 4,156,000
Accrued liabilities	2,388,000	2,459,000
Income taxes	946,000	382,000
Notes payable - current portion	204,000	197,000
Deferred subscription revenue and other revenues	6,796,000	6,493,000
<b>Total current liabilities</b>	<b>14,616,000</b>	<b>13,687,000</b>
Long term liabilities		
Accrued liabilities	1,330,000	1,030,000
Notes payable	3,907,000	4,011,000
<b>Total long term liabilities</b>	<b>5,237,000</b>	<b>5,041,000</b>

Edgar Filing: DAILY JOURNAL CORP - Form 10-Q

Commitments and contingencies (Notes 7 and 8)

Shareholders' equity		
Preferred stock, \$.01 par value, 5,000,000 shares authorized and no shares issued		
Common stock, \$.01 par value, 5,000,000 shares authorized;		
1,500,344 and 1,500,485 shares, at March 31, 2007 and September 30, 2006, respectively, outstanding	15,000	15,000
Additional paid-in capital	1,907,000	1,908,000
Retained earnings	16,990,000	15,958,000
Less 47,445 treasury shares, at March 31, 2007 and September 30, 2006, at cost	(906,000)	(906,000)
Total shareholders' equity	18,006,000	16,975,000
	\$ 37,859,000	\$ 35,703,000

See accompanying Notes to Consolidated Financial Statements.

**Table of Contents**

DAILY JOURNAL CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	<b>Three months</b>	
	<b>ended March 31</b>	
	<b>2007</b>	<b>2006</b>
<b>Revenues</b>		
Advertising	\$ 4,765,000	\$ 4,336,000
Circulation	2,297,000	2,288,000
Information systems and services	994,000	695,000
Advertising service fees and other	835,000	746,000
	8,891,000	8,065,000
<b>Costs and expenses</b>		
Salaries and employee benefits	4,487,000	4,218,000
Newsprint and printing expenses	483,000	518,000
Other outside services	839,000	949,000
Postage and delivery expenses	383,000	417,000
Depreciation and amortization	234,000	218,000
Other general and administrative expenses	825,000	906,000
	7,251,000	7,226,000
Income from operations	1,640,000	839,000
Other income and (expense)		
Interest income	207,000	128,000
Interest expense	(171,000)	(73,000)
Income before taxes	1,676,000	894,000
Provision for income taxes	1,270,000	445,000
<b>Net income</b>	<b>\$ 406,000</b>	<b>\$ 449,000</b>
Weighted average number of common shares outstanding - basic and diluted	1,452,930	1,453,130
Basic and diluted net income per share	\$ .28	\$ .31

See accompanying Notes to Consolidated Financial Statements.

**Table of Contents**

DAILY JOURNAL CORPORATION  
 CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	Six months	
	ended March 31	
	2007	2006
<b>Revenues</b>		
Advertising	\$ 8,862,000	\$ 8,254,000
Circulation	4,507,000	4,658,000
Information systems and services	1,873,000	1,622,000
Advertising service fees and other	1,661,000	1,428,000
	16,903,000	15,962,000
<b>Costs and expenses</b>		
Salaries and employee benefits	8,709,000	8,340,000
Newsprint and printing expenses	1,042,000	1,091,000
Other outside services	1,660,000	1,818,000
Postage and delivery expenses	776,000	824,000
Depreciation and amortization	473,000	414,000
Other general and administrative expenses	1,683,000	1,713,000
	14,343,000	14,200,000
Income from operations	2,560,000	1,762,000
Other income and (expense)		
Interest income	400,000	259,000
Interest expense	(244,000)	(152,000)
Income before taxes	2,716,000	1,869,000
Provision for income taxes	1,680,000	825,000
<b>Net income</b>	<b>\$ 1,036,000</b>	<b>\$ 1,044,000</b>
Weighted average number of common shares outstanding - basic and diluted	1,452,970	1,453,142
Basic and diluted net income per share	\$ .71	\$ .72

See accompanying Notes to Consolidated Financial Statements.

**Table of Contents**

DAILY JOURNAL CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six months	
	ended March 31	
	2007	2006
Cash flows from operating activities		
Net income	\$ 1,036,000	\$ 1,044,000
Adjustments to reconcile net income to net cash provided by operations		
Depreciation and amortization	473,000	414,000
Deferred income taxes	(35,000)	93,000
Discount earned on U.S. Treasury Bills	(52,000)	(69,000)
Changes in assets and liabilities		
(Increase) decrease in current assets		
Accounts receivable, net	(573,000)	692,000
Inventories	2,000	17,000
Prepaid expenses and other assets	(106,000)	(37,000)
Increase (decrease) in current liabilities		
Accounts payable	126,000	16,000
Accrued liabilities	229,000	(341,000)
Income taxes	564,000	(673,000)
Deferred subscription and other revenues	303,000	(293,000)
Cash provided by operating activities	1,967,000	863,000
Cash flows from investing activities		
Purchases of U.S. Treasury Notes and Bills	(3,664,000)	(3,562,000)
Maturities and sales of U.S. Treasury Notes and Bills	2,493,000	3,496,000
Purchases of property, plant and equipment, net	(220,000)	(526,000)
Net cash used for investing activities	(1,391,000)	(592,000)
Cash flows from financing activities		
Payment of loan principals	(97,000)	(75,000)
Purchase of common stock	(5,000)	(1,000)
Cash used for financing activities	(102,000)	(76,000)
Increase in cash and cash equivalents	474,000	195,000
Cash and cash equivalents		
Beginning of period	617,000	471,000
End of period	\$ 1,091,000	\$ 666,000
Interest paid during period	\$ 144,000	\$ 152,000

See accompanying Notes to Consolidated Financial Statements.





**Table of Contents**

DAILY JOURNAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1 - The Corporation and Operations

The Daily Journal Corporation (the Company) publishes newspapers and web sites covering California, Arizona and Nevada, as well as the California Lawyer and 8-K magazines, and produces several specialized information services. Sustain Technologies, Inc. (Sustain), a 93% owned subsidiary as of March 31, 2007, has been consolidated since it was acquired in January 1999. Sustain supplies case management software systems and related products to courts and other justice agencies, including district attorney offices and administrative law organizations. These courts and agencies use the Sustain family of products to help manage cases and information electronically and to interface with other critical justice partners. Sustain's products are designed to help users manage electronic case files from inception to disposition, including all aspects of calendaring and accounting, report and notice generation, the implementation of standards and business rules and other corollary functions. Essentially all of the Company's operations are based in California, Arizona, Colorado and Nevada.

Note 2 - Basis of Presentation

In the opinion of the Company, the accompanying interim unaudited consolidated financial statements contain all adjustments (consisting of normal recurring accruals) considered necessary for a fair statement of its financial position as of March 31, 2007, the results of operations for the three- and six-month periods ended March 31, 2007 and 2006 and its cash flows for the six months ended March 31, 2007 and 2006. The results of operations for the three and six months ended March 31, 2007 and 2006 are not necessarily indicative of the results to be expected for the full year.

The consolidated financial statements included herein have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission. 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 are adequate to make the information presented not misleading. These financial statements should be read in conjunction with the financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2006.

Certain reclassifications of previously reported amounts have been made to conform to the current year's presentation.

Note 3 - Basic and Diluted Income Per Share

The Company does not have any common stock equivalents, and therefore the basic and diluted income per share are the same.

**Table of Contents**

## Note 4 - Operating Segments

Summarized financial information concerning the Company's reportable segments is shown in the following table:

	Reportable Segments		Total Results
	Traditional Business	Sustain	for both Segments
<b><u>Six months ended March 31, 2007</u></b>			
Revenues	\$ 15,030,000	\$ 1,873,000	\$ 16,903,000
Income (loss) before taxes	2,995,000	(279,000)	2,716,000
Total assets	34,899,000	2,960,000	37,859,000
Capital expenditures	211,000	9,000	220,000
Depreciation and amortization	457,000	16,000	473,000
Income tax benefit (provision)	(1,790,000)	110,000	(1,680,000)
Net income (loss)	1,205,000	(169,000)	1,036,000
<b><u>Six months ended March 31, 2006</u></b>			
Revenues	\$ 14,340,000	\$ 1,622,000	\$ 15,962,000
Income (loss) before taxes	2,568,000	(699,000)	1,869,000
Total assets	31,065,000	2,448,000	33,513,000
Capital expenditures	501,000	25,000	526,000
Depreciation and amortization	394,000	20,000	414,000
Income tax benefit (provision)	(1,105,000)	280,000	(825,000)
Net income (loss)	1,463,000	(419,000)	1,044,000
<b><u>Three months ended March 31, 2007</u></b>			
Revenues	\$ 7,897,000	\$ 994,000	\$ 8,891,000
Income (loss) before taxes	1,730,000	(54,000)	1,676,000
Total assets	34,899,000	2,960,000	37,859,000
Capital expenditures	117,000	9,000	126,000
Depreciation and amortization	226,000	8,000	234,000
Income tax benefit (expense)	(1,290,000)	20,000	(1,270,000)
Net income (loss)	440,000	(34,000)	406,000
<b><u>Three months ended March 31, 2006</u></b>			
Revenues	\$ 7,370,000	\$ 695,000	\$ 8,065,000
Income (loss) before taxes	1,396,000	(502,000)	894,000
Total assets	31,065,000	2,448,000	33,513,000
Capital expenditures	131,000	25,000	156,000
Depreciation and amortization	208,000	10,000	218,000
Income tax benefit (expense)	(645,000)	200,000	(445,000)
Net income (loss)	751,000	(302,000)	449,000

## Note 5 - Revenue Recognition

Proceeds from the sale of subscriptions for newspapers, court rule books and other publications and other services are recorded as deferred revenue and are included in earned revenue only when the services are provided, generally over the subscription or lease term. Advertising revenues are recognized when advertisements are published and are net of commissions.

## **Table of Contents**

The Company recognizes revenues from both the lease and sale of software products. Revenues from leases of software products are recognized over the life of the lease while revenues from software product sales are recognized normally upon delivery, installation or acceptance pursuant to a signed agreement. Revenues from annual maintenance contracts generally call for the Company to provide software updates and upgrades to customers and are recognized ratably over the maintenance period. Consulting and other services are recognized as performed or upon acceptance by the customers.

### **Note 6 - Income Taxes**

On a pretax profit of \$1,869,000 for the six months ended March 31, 2006, the Company recorded a tax provision of only \$825,000, which was lower than the amount computed under the statutory rate, because it was able to utilize the state tax benefits from Sustain-segment operating loss carry-forwards. On a pretax profit of \$2,716,000 for the six months ended March 31, 2007, the Company recorded a tax provision of \$1,680,000. This amount includes \$600,000 to establish a reserve for research and development tax credits claimed by the Company in prior years. The Internal Revenue Service is currently auditing the credits claimed by the Company in prior year tax filings, and their preliminary assessment, if upheld, would result in disallowance of \$600,000 of previously claimed credits. The Company is continuing to contest the issue, and the ultimate resolution of this dispute cannot be ascertained at this time.

In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (an interpretation of FASB Statement No. 109), which was effective for fiscal years beginning after December 15, 2006 with earlier adoption encouraged. This interpretation was issued to clarify the accounting for uncertainty in income taxes recognized in the financial statements by prescribing a recognition threshold and measurement attribute for the financial statements recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation is effective beginning on October 1, 2007, and is not expected to have a significant impact on the Company's results of operations, cash flows or financial position.

### **Note 7 - Debt and Commitments**

The Company owns its facilities in Los Angeles and leases space for its other offices under operating leases, which expire at various dates through 2010. The Company is responsible for a portion of maintenance, insurance and property tax expenses relating to certain leased property. Rental expenses for comparable six-month periods ended March 31, 2007 and 2006 were \$306,000 and \$302,000, respectively.

As of March 31, 2007, the Company had two real estate loans. One of \$1,448,000, which bears a fixed interest rate of 6.84%, is repayable in equal monthly installments of about \$18,000 through 2016. Another of \$2,663,000, which bears a fixed interest rate of 6.84%, is repayable in equal monthly installments of about \$22,000 through 2024. Each loan is secured by one of the Company's two buildings in Los Angeles and can be paid off without prepayment penalty.

### **Note 8 - Contingencies**

There has never been a resolution of the payment dispute between Sustain and a terminated outside service provider whose software development work was terminated by Sustain in April 2001 as a result of serious flaws and long delays. The terminated outside service provider filed for bankruptcy in December 2001 and stated in its filings with the U.S. Bankruptcy Court that it was considering bringing a collection action against Sustain. If it does, Sustain will assert counter-claims that completely offset the terminated outside provider's claims. Sustain will vigorously defend any litigation or action brought by the

**Table of Contents**

terminated outside service provider, although no assurances can be made as to the ultimate outcome of the dispute. It is the opinion of management that adequate provision has been made for any amounts that may become due as a result of the dispute.

Sustain received a letter in April 2003 from counsel to the Ontario, Canada Ministry of the Solicitor General, Ministry of Public Safety and Security and Ministry of the Attorney General (collectively, the Ministries ). The Ministries had entered into a contract with Sustain, dated as of April 22, 1999 (the Contract ), pursuant to which the Ministries sought to license the software product that was to be developed by the outside service provider referred to above. The Contract was formally terminated in June 2002. The letter from counsel purported to invoke the dispute resolution process set forth in the Contract and claimed damages in the amount of \$20 million. Counsel for Sustain and counsel for the Ministries engaged in preliminary discussions with respect to this matter, and the dispute resolution process set forth in the Contract was not utilized. Counsel for Sustain last communicated with counsel for the Ministries by a letter sent in April 2003. At this point, management is unable to determine whether this matter will have a material adverse effect on Sustain and the Company.

---

**Table of Contents**

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS  
Revenues were \$16,903,000 and \$15,962,000 for the six months ended March 31, 2007 and 2006, respectively. This increase of \$941,000 (6%) was primarily attributed to an increase in (i) public notice advertising revenues and (ii) Sustain's consulting revenues, partially offset by decreased commercial advertising and circulation revenues. (Revenues were \$8,891,000 and \$8,065,000 for the three months ended March 31, 2007 and 2006, respectively.)

Public notice advertising revenues increased by \$909,000 primarily resulting from an increase in trustee foreclosure sales in California. The Company's smaller newspapers, those other than the Los Angeles and San Francisco Daily Journals (The Daily Journals), accounted for about 92% of the total public notice advertising revenues. Public notice advertising revenues and related advertising and other service fees constituted about 32% of the Company's total revenues. Display advertising revenues decreased by \$42,000, and classified advertising revenues decreased by \$268,000.

Total circulation revenues decreased by \$151,000, including about \$47,000 (1%) for the Daily Journals. This is fairly consistent with recent trends. The Daily Journals accounted for about 77% of the Company's total circulation revenues. The court rule and judicial profile services generated about 14% of the total circulation revenues, with the other newspapers and services accounting for the balance. Information system and service revenues increased by \$251,000 (15%) primarily because of an increase in Sustain's consulting revenues. The Company's revenues derived from Sustain's operations constituted about 11% and 10% of the Company's total revenues for the six months ended March 31, 2007 and 2006, respectively. Other revenues increased primarily because of more small print jobs for governmental agencies.

Costs and expenses increased by \$143,000 (1%) to \$14,343,000 from \$14,200,000. Total personnel costs increased by \$369,000 (4%) to \$8,709,000. Depreciation and amortization expenses increased by \$59,000 (14%) mainly due to the amortization of the editorial/advertising software installed last year. (Costs and expenses were \$7,251,000 and \$7,226,000 for the three months ended March 31, 2007 and 2006, respectively.)

The Company's expenditures for the development of new Sustain software products are highly significant and will materially impact overall results at least through fiscal 2007. These costs are expensed as incurred until technological feasibility of the product has been established, at which time such costs are capitalized, subject to expected recovery. Sustain's internal development costs, which are primarily incremental costs for both employees and outside contractors, aggregated \$654,000 and \$765,000 for the six months ended March 31, 2007 and 2006, respectively. If Sustain's internal development programs are not successful, they will significantly and adversely impact the Company's ability to maximize its existing investment in the Sustain software, to service its existing customers, and to compete for new opportunities in the case management software business.

The Company's traditional business segment pretax profit increased by \$427,000 (17%) from \$2,568,000 to \$2,995,000 primarily resulting from increased public notice advertising revenues, partially offset by decreased commercial advertising and circulation revenues. Sustain's business segment pretax loss decreased \$420,000 from \$699,000 to \$279,000, primarily because of the increase in Sustain's consulting revenues. Projected consulting revenues are subject to uncertainty because they depend on (i) the timing of the acceptance of the completed consulting tasks and (ii) the unpredictable needs of Sustain's existing customers and its ability to secure new customers.

---

**Table of Contents**

Consolidated net income was \$1,036,000 and \$1,044,000 for the six months ended March 31, 2007 and 2006, respectively. On a pretax profit of \$1,869,000 for the six months ended March 31, 2006, the Company recorded a tax provision of only \$825,000, which was lower than the amount computed under the statutory rate, because it was able to utilize the state tax benefits from Sustain-segment operating loss carry-forwards. On a pretax profit of \$2,716,000 for the six months ended March 31, 2007, the Company recorded a tax provision of \$1,680,000. This amount includes \$600,000 to establish a reserve for research and development tax credits claimed by the Company in prior years. The Internal Revenue Service is currently auditing the credits claimed by the Company in prior year tax filings, and their preliminary assessment, if upheld, would result in disallowance of \$600,000 of previously claimed credits. The Company is continuing to contest the issue, and the ultimate resolution of this dispute cannot be ascertained at this time. Net income per share decreased to \$.71 from \$.72. But for the tax provision of \$600,000, net income per share would have increased to \$1.13 from \$.72.

**Liquidity and Capital Resources**

During the six months ended March 31, 2007, the Company's cash and cash equivalents and U.S. Treasury Note and Bill positions increased by \$1,697,000. Cash and cash equivalents were used for the purchase of capital assets of \$220,000, primarily for computer software and equipment and the purchase of the Company's common stock of \$5,000. The cash provided by operating activities of \$1,967,000 included a net increase in prepayments for subscriptions and other revenues of \$303,000. Proceeds from the sale of subscriptions from newspapers, court rule books and other publications and for software licenses and maintenance and other services are recorded as deferred revenue and are included in earned revenue only when the services are rendered. Cash flows from operating activities increased by \$1,104,000 for the six months ended March 31, 2007 as compared to the prior comparable period primarily due to the increases in accrued liabilities of \$570,000 and deferred subscription and other revenues of \$596,000. As of March 31, 2007, the Company had working capital of \$10,290,000 before deducting the liability for deferred subscription revenues and other revenues of \$6,796,000, which are scheduled to be earned within one year. In addition, the company had long-term U.S. Treasury Notes of about \$7,094,000 at March 31, 2007.

As of March 31, 2007, the Company had two real estate loans. One of \$1,448,000, which bears a fixed interest rate of 6.84%, is repayable in equal monthly installments of about \$18,000 through 2016. Another of \$2,663,000, which bears a fixed interest rate of 6.84%, is repayable in equal monthly installments of about \$22,000 through 2024. Each loan is secured by one of the Company's two buildings in Los Angeles and can be paid off without prepayment penalty.

**Critical Accounting Policies**

The Company's financial statements and accompanying notes are prepared in accordance with generally accepted accounting principles. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. These estimates and assumptions are affected by management's application of accounting policies. Management believes that revenue recognition, accounting for capitalized software costs and income taxes are critical accounting policies.

The Company recognizes revenues from both the lease and sale of software products. Revenues from leases of software products are recognized over the life of the lease while revenues from software product sales are recognized normally upon delivery, installation or acceptance pursuant to a signed agreement. Revenues from annual maintenance contracts generally call for the Company to provide software updates and upgrades to customers and are recognized ratably over the maintenance period. Consulting and other services are recognized as performed or upon acceptance by the customers. Proceeds from the sale of

## **Table of Contents**

subscriptions for newspapers, court rule books and other publications and other services are recorded as deferred revenue and are included in earned revenue only when the services are provided, generally over the subscription or lease term. Advertising revenues are recognized when advertisements are published and are net of commissions.

Pursuant to Statement of Financial Accounting Standards No. 86, *Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed*, costs related to the research and development of a new software product are to be expensed as incurred until the technological feasibility of the product is established. Accordingly, costs related to the development of new Sustain software products are expensed as incurred until technological feasibility has been established, at which time such costs are capitalized, subject to expected recoverability. In general, technological feasibility is achieved when the developer has established the necessary skills, hardware and technology to produce a product and a detailed program design has been (a) completed, (b) traced to the product specifications and (c) reviewed for high-risk development issues.

Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*, establishes financial accounting and reporting standards for the effect of income taxes. The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and the deferred tax liabilities and assets for the future tax consequences of events that have been recognized in the financial statements or tax returns. Judgment is required in assessing the future tax consequences of events that have been recognized in the Company's financial statements or tax returns. Fluctuations in the actual outcome of these future tax consequences could materially impact the Company's financial position or its results of operations.

In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (an interpretation of FASB Statement No. 109), which was effective for fiscal years beginning after December 15, 2006 with earlier adoption encouraged. This interpretation was issued to clarify the accounting for uncertainty in income taxes recognized in the financial statements by prescribing a recognition threshold and measurement attribute for the financial statements recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation is effective beginning on October 1, 2007, and is not expected to have a significant impact on the Company's results of operations, cash flows or financial position.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, codified as SAB Topic 1.N, *Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements* (SAB 108). SAB 108 describes the approach that should be used to quantify the materiality of a misstatement and provides guidance for correcting prior year errors. This interpretation was effective for fiscal years ending on or before November 15, 2006. The adoption of SAB 108 has not had a material impact on the Company's consolidated financial statements.

The above discussion and analysis should be read in conjunction with the unaudited consolidated financial statements and the notes thereto included in this report.

## **Disclosure Regarding Forward-Looking Statements**

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Certain statements contained in this document, including but not limited to those in Management's Discussion and Analysis of Financial Condition and Results of Operations, are forward-looking statements that involve risks and uncertainties that may cause actual future events or results to differ materially from those described in the forward-looking statements. Words such as



---

**Table of Contents**

expects, intends, anticipates, should, believes, will, plans, estimates, may, variations of such words and similar expressions are in order to identify such forward-looking statements. We disclaim any intention or obligation to revise any forward-looking statements whether as a result of new information, future developments, or otherwise. There are many factors that could cause actual results to differ materially from those contained in the forward-looking statements. These factors include, among others: risks associated with the functionality and resources required for new and existing case management software projects; the success or failure of Sustain's internal software development efforts; Sustain's reliance on the time and materials professional services engagement with the California Administrative Office of the Courts for a substantial portion of its consulting revenues; the ultimate resolution, if any, of the dispute with the Ontario, Canada Ministries; material changes in the costs of materials; a further decline in subscriber and classified revenues; an inability to continue borrowing on current terms; possible changes in tax laws; collectibility of accounts receivable; potential increases in employee and consultant costs; attraction, training and retention of employees; changes in accounting guidance; and competitive factors in both the case management software business and the publishing business. In addition, such statements could be affected by general industry and market conditions and growth rates, general economic conditions (particularly in California) and other factors. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Important factors that could cause actual results to differ materially from those in the forward-looking statements are disclosed in this Form 10-Q, including in conjunction with the forward-looking statements themselves. Additional information concerning factors that could cause actual results to differ materially from those in the forward-looking statements is contained from time to time in documents filed by the Company with the Securities and Exchange Commission, including in Item 1A "Risk Factors" in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2006.

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company does not use derivative financial instruments. The Company does maintain a portfolio of cash equivalents maturing in three months or less and a portfolio of U.S. Treasury Bills and Notes maturing within three years. Given the nature of the investments and the fact that the Company had no outstanding borrowing except for the two real estate loans, which bear a fixed interest rate, the Company was not subject to significant interest rate risk. As of March 31, 2007, the Company had two real estate loans. One of \$1,448,000, which bears a fixed interest rate of 6.84%, is repayable in equal monthly installments of about \$18,000 through 2016. Another of \$2,663,000, which bears a fixed interest rate of 6.84%, is repayable in equal monthly installments of about \$22,000 through 2024. Each loan is secured by one of the Company's two buildings in Los Angeles and can be paid off without prepayment penalty.

**Item 4. CONTROLS AND PROCEDURES**

An evaluation was performed under the supervision and with the participation of the Company's management, including Gerald L. Salzman, its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of March 31, 2007. Based on that evaluation, Mr. Salzman concluded that the Company's disclosure controls and procedures are effective in ensuring that information required to be disclosed by the Company in reports it files or submits under the Securities Exchange Act of 1934, as amended, is (1) recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities Exchange Commission and (2) accumulated and communicated to the Company's management, including Mr. Salzman, in such a way as to allow timely decisions regarding required disclosure. There have been no material changes in the Company's internal controls over financial reporting or in other factors reasonably likely to affect its internal controls over financial reporting during the quarter ended March 31, 2007.

**Table of Contents**

## PART II

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS  
ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
1/1/07 - 1/31/07	51	\$ 36.00	(a)	Not applicable
2/1/07 - 2/28/07	30	\$ 36.00	(a)	Not applicable
3/1/07 - 3/31/07			(a)	Not applicable
Total	81	\$ 36.00	(a)	Not applicable

- (a) The Company's common stock repurchase program was implemented in 1987 in combination with the Company's Deferred Management Incentive Plan, and therefore the Company's per share earnings have not been diluted by grants of units under the Deferred Management Incentive Plan. Each unit entitles the recipient to a designated share of the pre-tax earnings of the Company on a consolidated basis, or a designated share of the pre-tax earnings attributable to only Sustain or the Company's traditional business, depending on the recipient's responsibilities. All shares purchased were made in privately negotiated transactions. The Company's stock repurchase program remains in effect, and the Company plans to repurchase shares from time to time as it deems appropriate (including, if necessary, to prevent any additional dilution that may be caused by the Deferred Management Incentive Plan).

## Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company's annual meeting was held on February 7, 2007. The matters submitted to a vote of security holders were the election of directors and the ratification of the appointment of Ernst & Young LLP as independent accountants for the Company for the current fiscal year.

Each of the nominees to the board of directors was elected. The following votes were received as to the election of the board of directors:

Nominee's Name	Votes		Broker
	For	Withheld	
Charles T. Munger	1,419,525	8,946	0
J. P. Guerin	1,401,896	26,575	0
Gerald L. Salzman	1,419,585	8,886	0
Peter D. Kaufman	1,401,653	26,818	0
George C. Good	1,402,393	26,078	0

Ernst & Young LLP was ratified as the Company's independent accountants with 1,421,975 votes in favor, 2,560 votes against, 7,310 abstentions and no broker non-votes.

**Table of Contents**

Item 6. EXHIBITS

- 31 Certification by Chief Executive Officer and Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32 Certification by Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURE

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.

DAILY JOURNAL CORPORATION  
(Registrant)

/s/ Gerald L. Salzman  
Gerald L. Salzman  
Chief Executive Officer  
President  
Chief Financial Officer  
Treasurer

DATE: May 11, 2007