COMPUTER SOFTWARE INNOVATIONS INC
Form 10-Q
May 15, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2009

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: 000-51758

COMPUTER SOFTWARE INNOVATIONS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**98-0216911**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
900 East Main Street, Suite T, Easley, South Carolina	**29640**
(Address of principal executive offices)	**(Zip Code)**

(864) 855-3900

(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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ¨ No ¨

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

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

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

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

Class	**Outstanding at May 12, 2009**
Common Stock, $0.001 par value per share	**7,181,204 shares**

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

COMPUTER SOFTWARE INNOVATIONS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	Three Months Ended	
(Amounts in thousands, except per share data)	**March 31, 2009**	**March 31, 2008**
REVENUES		
Software applications segment	$ 3,321	$ 3,058
Technology solutions segment	5,556	9,005
Net sales and service revenue	8,877	12,063
COST OF SALES		
Software applications segment		
Cost of sales, excluding depreciation, amortization and capitalization	2,124	1,666
Depreciation	29	24
Amortization of capitalized software costs	358	284
Capitalization of software costs	(248)	(296)
Total Software applications segment cost of sales	2,263	1,678
Technology solutions segment		
Cost of sales, excluding depreciation	4,805	7,332
Depreciation	27	29
Total Technology solutions segment cost of sales	4,832	7,361
Total cost of sales	7,095	9,039
Gross profit	1,782	3,024
OPERATING EXPENSES		
Research and development	91	
Selling costs	1,233	860
Marketing costs	155	39
Stock based compensation	2	5
Acquisition costs	1	24
Professional, legal compliance and litigation costs	95	96
Depreciation and amortization	164	106
Other general and administrative expenses	927	1,069
Total operating expenses	2,668	2,199
Operating (loss) income	(886)	825
OTHER INCOME (EXPENSE)		
Interest income		

Interest expense		(113)		(132)
Loss on disposal of property and equipment		(4)		
Net other income (expense)		(117)		(132)
(Loss) income before income tax (benefit) expense		(1,003)		693
INCOME TAX (BENEFIT) EXPENSE		(353)		265
NET (LOSS) INCOME	**$**	**(650)**	**$**	**428**
BASIC (LOSS) EARNINGS PER SHARE	**$**	**(0.10)**	**$**	**0.09**
DILUTED (LOSS) EARNINGS PER SHARE	**$**	**(0.10)**	**$**	**0.03**
WEIGHTED AVERAGE SHARES OUTSTANDING:				
Basic		**6,381**		**4,699**
Diluted		**6,381**		**12,451**

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

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COMPUTER SOFTWARE INNOVATIONS, INC.

CONSOLIDATED BALANCE SHEETS

(Amounts in thousands)	March 31, 2009 (Unaudited)	December 31, 2008
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$	$
Accounts receivable, net	7,430	13,862
Inventories	2,551	1,552
Prepaid expenses	170	98
Taxes receivable	638	223
Total current assets	10,789	15,735
PROPERTY AND EQUIPMENT, net	924	898
COMPUTER SOFTWARE COSTS, net	2,908	3,001
GOODWILL	2,431	2,431
OTHER INTANGIBLE ASSETS, net	2,882	2,970
Total assets	**$ 19,934**	**$ 25,035**
LIABILITIES AND SHAREHOLDERS EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 4,551	$ 3,644
Deferred revenue	5,529	6,696
Deferred tax liability	411	421
Current portion of notes payable	461	447
Subordinated notes payable to shareholders	1,950	1,950
Total current liabilities	12,902	13,158
LONG-TERM DEFERRED TAX LIABILITY, net	295	329
NOTES PAYABLE, less current portion	389	515
BANK LINE OF CREDIT	1,587	5,634
Total liabilities	15,173	19,636
SHAREHOLDERS EQUITY		
Preferred stock - $0.001 par value; 15,000 shares authorized; 6,740 shares issued and outstanding	7	7
Common stock - $0.001 par value; 40,000 shares authorized; 6,381 shares issued and outstanding	6	6
Additional paid-in capital	8,884	8,884
Accumulated deficit	(4,093)	(3,443)
Unearned stock compensation	(43)	(55)
Total shareholders equity	4,761	5,399
Total liabilities and shareholders equity	**$ 19,934**	**$ 25,035**

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

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COMPUTER SOFTWARE INNOVATIONS, INC.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY

(UNAUDITED)

(Amounts in thousands)	Common Stock	Preferred Stock	Additional Paid-In Capital	Accumulated Deficit	Unearned Stock Compensation	Total
Balances at December 31, 2008	**$ 6**	**$ 7**	**$ 8,884**	**$ (3,443)**	**$ (55)**	**$ 5,399**
Stock based compensation					12	12
Net loss for the three months ended March 31, 2009				(650)		(650)
Balances at March 31, 2009	**$ 6**	**$ 7**	**$ 8,884**	**$ (4,093)**	**$ (43)**	**$ 4,761**

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

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COMPUTER SOFTWARE INNOVATIONS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(Amounts in thousands)	**Three Months Ended March 31, 2009**	**Three Months Ended March 31, 2008**
OPERATING ACTIVITIES		
Net (loss) income	$ (650)	$ 428
Adjustments to reconcile net (loss) income to net cash provided by operating activities		
Depreciation and amortization	578	443
Stock compensation expense, net	12	22
Deferred income tax expense	(44)	5
Loss on disposal of fixed assets	4	
Changes in deferred and accrued amounts		
Accounts receivable	6,432	960
Inventories	(999)	(755)
Prepaid expenses and other assets	(72)	(32)
Accounts payable	907	939
Deferred revenue	(1,167)	(1,039)
Income taxes receivable/payable	(415)	257
Net cash provided by operating activities	4,586	1,228
INVESTING ACTIVITIES		
Purchases of property and equipment	(162)	(188)
Capitalization of computer software	(265)	(336)
Payment for acquisitions		(1,321)
Net cash used for investing activities	(427)	(1,845)
FINANCING ACTIVITIES		
Net (repayments) borrowings under line of credit	(4,047)	685
Repayments of notes payable	(112)	(68)
Net cash (used for) provided by financing activities	(4,159)	617
Net change in cash and cash equivalents		
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD		
CASH AND CASH EQUIVALENTS, END OF PERIOD	$	$
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	$ 211	$ 127
Income Taxes	$ 107	$ 3

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

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COMPUTER SOFTWARE INNOVATIONS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(Amounts in thousands, except where specifically stated)

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND ACTIVITIES

Organization

Computer Software Innovations, Inc. (formerly VerticalBuyer, Inc.) (the Company , CSI or we), a Delaware corporation, was incorporated on September 24, 1999. The Company currently trades in the over the counter market and is reported on the OTC Bulletin Board under the symbol CSWI.OB.

In the first quarter of 2005, we concluded a series of recapitalization transactions which began January 31, 2005 with a change in control due to the purchase of a majority of our common stock by Computer Software Innovations, Inc., a South Carolina corporation (CSI South Carolina). These transactions culminated on February 11, 2005 with the merger of CSI South Carolina into us (reverse merger), our issuance of preferred stock, common stock, warrants and certain subordinated notes, and the change of our name to Computer Software Innovations, Inc.

Description of business

The Company is engaged in the business of development and sales of internally developed software, sales and distribution of computers, network and communications hardware and accessories, as well as interactive collaborative classroom technologies and other hardware based solutions.

The Company s internally developed software consists of fund accounting based financial management software, standards-based lesson planning software and solutions that facilitate single sign-on application access management provisioning based on Microsoft s Identity Lifecycle Management and Microsoft SharePoint deployments. The Company s primary software product, fund accounting based financial management software, is developed for those entities that track expenditures and investments by fund, or by source and purpose of the funding. The fund accounting software is used primarily by public sector and not-for-profit entities. The Company s standards-based lesson planning software is designed to allow teachers to create lesson plans that are tied to a state s curriculum standards. These lesson plans may be reviewed by administrators and a report generated to determine the standards that have been met or need to be met. The lesson plans can be stored, shared, and retrieved for collaboration, editing and future use. The Company s solutions for single sign-on application access management provide the ability to eliminate the need for users to sign on to every application separately (thereby allowing single sign-on) and provides for other efficiencies related to setting-up and controlling user access.

In connection with its hardware-based solutions, the Company provides a wide range of technology products and services including hardware and design, engineering, installation, training and ongoing support and maintenance. Technology solutions include computers, networking, security, internet protocol (IP) telephony, interactive whiteboard solutions and integrated accessories, distance learning and video communication. The Company currently markets its products and services primarily to a wide variety of education and local government agencies, and not-for-profit entities in the southeastern United States. The majority of the Company s business is with K-12 (kindergarten through grade 12) public education and local government entities.

Basis of presentation

The consolidated financial statements include CSI Technology Resources, Inc., a wholly-owned subsidiary. CSI Technology Resources, Inc. was acquired by CSI on May 1, 2000 and became the Technology solutions segment of CSI. This subsidiary no longer has any significant operations or separate accounting, as all activities are now accounted for within CSI, except that certain vendor contracts are still in the name of CSI Technology Resources, Inc. At a future date, the name on these contracts may be converted and the subsidiary deactivated, subject to a review of any tax or legal implications. As the Company files a consolidated tax return and has been accounting for all activities through the parent, there should be no financial or tax implications related to the formal procedures which would be undertaken to deactivate the subsidiary. Intercompany balances and transactions have been eliminated. The Company uses the accrual basis of accounting.

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Use of estimates

The accounting and reporting policies conform to accounting principles generally accepted in the United States of America (generally accepted accounting principles or GAAP). GAAP requires us to make estimates, assumptions and judgments and to rely on projections of future results of operations and cash flows. Those estimates, assumptions, judgments and projections are an integral part of the financial statements. We base our estimates and assumptions on historical data and other assumptions, which include knowledge and experience with regard to past and current events and assumptions about future events that we believe are reasonable under the circumstances. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities in our financial statements. In addition, they affect the reported amounts of revenues and expenses during the reporting period.

Our judgments are based on our assessment as to the effect certain estimates, assumptions of future trends or events may have on the financial condition and results of operations reported in our financial statements. Actual results could differ materially from these estimates, assumptions, projections and judgments.

The interim consolidated balance sheet and the related consolidated statements of operations, changes in shareholders equity and cash flows are unaudited. In our opinion, all adjustments (consisting of normal recurring adjustments) necessary for fair presentation of the interim financial statements have been made. The results of the three months ended March 31, 2009 are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with the consolidated financial statements, critical accounting policies, significant accounting policies and the notes to the consolidated financial statements included in our most recent Annual Report on Form 10-K.

Certain prior period amounts have been reclassified to conform to the current presentation.

Recent accounting pronouncements

The following is a summary of recent authoritative pronouncements that could impact the accounting, reporting, and/or disclosure of financial information by the Company.

In April 2009, This FASB issued Staff Position (FSP) No. 107-1, Interim Disclosures about Fair Value of Financial Instruments. The final FSP amends FASB Statement No. 107, Disclosures about Fair Value of Financial Instruments. to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. This FSP also amends APB Opinion No. 28, Interim Financial Reporting. to require those disclosures in summarized financial information at interim reporting periods. The FSP shall be effective for interim reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. We are currently evaluating the effect the adoption of SFAS No. 161 will have on our Consolidated Financial Statements.

In May 2008, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 162, The Hierarchy of Generally Accepted Accounting Principles. SFAS No. 162 is intended to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements that are presented in conformity with generally accepted accounting principles in the United States for non-governmental entities. SFAS No. 162 is effective 60 days following approval by the U.S. Securities and Exchange Commission (SEC) of the Public Company Accounting Oversight Board s amendments to AU Section 411, The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles. The Company does not expect SFAS No. 162 to have a material impact on the preparation of its financial statements.

In April 2008, the FASB issued FASB Staff Position (FSP) No. FAS 142-3, Determination of the Useful Life of Intangible Assets. The final FSP amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, Goodwill and Other Intangible Assets. The FSP is intended to improve the consistency between the useful life of an intangible asset determined under SFAS No. 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141 (revised 2007), Business Combinations, and other US generally accepted accounting principles. The FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. We are currently evaluating the impact FSP 142-3 will have on its consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities. SFAS No. 161 is intended to improve financial reporting of derivative instruments and hedging activities by requiring enhanced disclosures to enable financial statement users to better understand the effects of derivatives and hedging on an entity s financial position, financial performance and cash flows. The provisions of SFAS No. 161 are effective for interim periods and fiscal years beginning after November 15, 2008. We are currently evaluating the effect the adoption of SFAS No. 161 will have on our Consolidated Financial Statements.

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In December 2007, the FASB issued SFAS No. 141 (revised 2007), Business Combinations. SFAS No. 141R establishes principles and requirements for recognizing and measuring assets acquired, liabilities assumed and any non-controlling interests in the acquiree in a business combination. SFAS No. 141R also provides guidance for recognizing and measuring goodwill acquired in a business combination, requires capitalization of acquired in-process research and development assets at the time of acquisition and requires the acquirer to disclose information that users may need to evaluate and understand the financial effect of the business combination. As SFAS No. 141R is effective for business combination transactions for which the acquisition date is on or after December 15, 2008. The Company will assess the impact of SFAS No. 141R if and when a future acquisition occurs.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company s financial position, results of operations or cash flows.

NOTE 2 (LOSS) EARNINGS PER SHARE

Basic (loss) earnings per share are computed by dividing net (loss) income by the weighted average number of common stock shares outstanding during the period. Diluted (loss) earnings per share is computed by dividing net (loss) income by the weighted average number of common and potential common shares outstanding, including common stock held in escrow, during the period following application of the treasury stock method. The table below presents the weighted average shares outstanding for the three months ended March 31, 2009 and 2008, both prior to and after application of the treasury stock method.

	For the Three Months Ended March 31,	
	2009	**2008**
Weighted Average Shares Outstanding Prior to Application of the Treasury Stock Method		
Common stock (excluding shares held in escrow)	6,381	4,699
Common stock held in escrow	800	
Preferred stock	7,142	6,860
Warrants	6,164	6,164
Options	385	375
Total Weighted Average Shares Outstanding	20,872	18,098
Weighted Average Shares Outstanding After Application of the Treasury Stock Method		
Common stock (excluding shares held in escrow)	6,381	4,699
Common stock held in escrow	800	
Preferred stock	7,143	6,860
Warrants		688
Options	160	204
Total Weighted Average Shares Outstanding treasury stock method	14,484	12,451

The potential common shares, including common stock held in escrow, were used in the calculation of diluted earnings per share for the three months ended March 31, 2008. The potential common shares were not used in the calculation of diluted loss per share for the three months ended March 31, 2009, as the effect is anti-dilutive due to the net loss reported for the period.

NOTE 3 ACQUISITION

Acquisition of ICS Systems, Inc.

On March 31, 2008, CSI consummated the acquisition, effective April 1, 2008, of substantially all the assets and business operations of ICS Systems, Inc. (ICS). The total purchase price was $1,370 in cash offset by $50 of liabilities, and the issuance by the Company of 209 shares of the Company s common stock. We did not assume any material liabilities of ICS. We operate ICS as a separate office from which we continue to support the existing product and expand opportunities and sales into surrounding areas. We also integrate the unique features of ICS software into our products over time, and plan to use ICS personnel to assist with these efforts and future product development needs.

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The acquisition was effectuated pursuant to an Asset Purchase Agreement with ICS and Michael Byers, its sole shareholder. The assets acquired included: certain account receivables; work in progress; all furniture, fixtures, machinery, equipment and supplies; and all software and intellectual property rights. The cash portion of the consideration was substantially funded by draw under the Company s revolving credit facility with RBC Bank (USA).

NOTE 4 STOCK-BASED COMPENSATION

The Company has a stock based compensation plan, the 2005 Incentive Compensation Plan. The Company accounts for stock based compensation using the fair value method prescribed in SFAS No. 123R, Share-Based Payment, and related interpretations, which the Company adopted in 2006 using the modified prospective method. The Company utilizes the Black-Scholes model to estimate the fair value of options granted.

In 2005, the Company assumed the stock based employee compensation plan of CSI South Carolina as a result of the reverse merger. The Company granted options to purchase 70 shares of common stock under the 2005 Incentive Compensation Plan in the first quarter of 2007 at an exercise price of $0.85 per share, as a result of the McAleer acquisition which closed on January 2, 2007, and in November 2007 granted options to purchase an additional 100 shares to key employees. In the first quarter of 2008 the Company granted options to purchase an additional 20 to other employees. The fair value of stock-based compensation was estimated at the grant date for each issuance using the Black-Scholes option-pricing model. For further information and discussion related to the weighted average assumptions used in the option pricing model, please see the Company s Annual Report on Form 10-K for the year ended December 31, 2008.

Assumptions used in calculation of fair value

	For the Three Months Ended March 31, 2009	2008
Expected term (in years)	7	7
Expected volatility	123%	123%
Expected dividend yield	0.0%	0.0%
Risk-free interest rate	3.6%	3.6%

Stock options

Detail	Number of Options	Weighted Average Exercise Price	Expiration
Options assumed in reverse merger	268	0.12	November 1, 2012
Options granted in McAleer acquisition	70	0.85	January 2, 2017
Options granted to key employees	100	1.42	November 9, 2017
Options granted to other employees	10	1.09	May 28, 2018

The following table summarizes option activity under the plans for the first three months of 2009:

Stock Options	Number of Shares	Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2008	385	$ 0.62	5.80	$ (79)
Granted				
Cancelled				
Exercised				
Forfeited/expired				
Outstanding at March 31, 2009	385	$ 0.62	5.56	$ (25)

Exercisable at March 31, 2009	285	$	0.39	4.86	$ 45

The aggregate intrinsic value represents the difference between the Company s closing stock price of $0.55 as of March 31, 2009, and the exercise price multiplied by the number of options outstanding as of that date.

As of March 31, 2009 there remained approximately $43 of unrecognized compensation cost related to non-vested stock options which is expected to be recognized over a weighted-average period of approximately two years.

No non-employee based stock awards were granted in the first three months of 2009.

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Total stock based compensation for the first three months of 2009 was $12, which was related to employee stock compensation. Total stock based compensation for the first three months of 2008 was $22, of which $5 was related to stock options granted from acquisition and $17 was related to stock options granted to key employees in November of 2007.

NOTE 5 LONG-TERM AND SHORT-TERM DEBT, INCLUDING RELATED PARTY TRANSACTIONS, AND OFF-BALANCE SHEET INSTRUMENTS

Bank Credit Facilities

The Company maintains a line of credit facility with its bank. The terms of the facility are as follows:

- the principal amount of the facility is $7.0 million;
- the latest renewal was on June 30, 2008, with a maturity date of June 30, 2010;
- permissible purposes of the funds borrowed under the revolving facility include funding short-term working capital and general corporate purposes of the Company; and
- the definition of the borrowing base includes 50% of eligible inventory (with a maximum borrowing ability against eligible inventory of $1.0 million), in addition to 80% of eligible accounts receivable.

On September 11, 2008, the Company entered into a modification of the line of credit facility. The modification temporarily increased the credit facility from $7.0 million to $8.0 million until November 30, 2008 to support the collection cycle for increased receivables generated during the summer, the seasonal high point of CSI s business. The modification increased availability by increasing the amount of inventory includable in the Credit Facility s borrowing base from $1.0 million to $2.0 million.

Under our bank facility, eligible accounts receivable balances essentially include all of our trade accounts receivable except, in most cases, those accounts which are more than 90 days past due. Certain other accounts are excluded from eligibility for borrowing including: (i) accounts due from affiliates; (ii) accounts which we have determined to be of doubtful collectability; and (iii) accounts due from any one of our customers if such accounts constitute more than 20% of the total eligible accounts. The loans bore interest at LIBOR plus 2.50% (3.00%) at March 31, 2009, and LIBOR plus 2.50% (3.59%) at December 31, 2008, payable monthly.

The Company maintains an equipment term loan which has been modified and increased from time to time with a term of three to four years. The term loan is used periodically to refinance its capital expenditures initially financed through its bank credit facility and improve its availability under its bank credit facility for working capital purposes. The latest modification was November 1, 2008. Pursuant to the modification, the equipment loan was increased from $358 to $1.0 million, and bears interest at 30-day LIBOR plus 250 basis points. Principal and interest are payable in 23 consecutive monthly payments of principal and interest of $40 continuing until November 15, 2010.

The amount outstanding on the notes payable to the bank was $850 at March 31, 2009 and $962 at December 31, 2008.

Scheduled principal payments under the Company s notes payable for the years ended are presented below:

2009	$ 461
2010	389
Total Principal Payments	$ 850

The loans under the revolving credit facility and the equipment facility, as well as all other obligations owed by the Company to the bank, are secured by a first priority security interest in substantially all of the Company s assets. Also, the Company is required to comply with certain covenants, including: providing periodic financial statements to the bank, compliance with SEC reporting requirements, allowing the bank to inspect its secured assets, and the Company maintaining its assets in good operating condition and maintaining sufficient insurance. Also, the Company is required to comply with certain financial covenants. The first financial covenant is a Debt Service Coverage Ratio, which is measured at the end of each year. This ratio is calculated by adding certain nonrecurring special items to EBITDA (Adjusted EBITDA), and then dividing by current maturities of long term debt plus interest expense. For the purposes of the amended loan agreement, EBITDA means the total of (i) net income from continuing operations (excluding extraordinary gains or losses), and to the extent deducted in determining net income (ii) interest expense, (iii) income taxes, and (iv) depreciation, depletion and amortization expenses. The Company is required to maintain a Debt Service Coverage Ratio of not less than 1.2 to 1.0. The second financial ratio is Funded Debt to EBITDA, which is also measured annually. A ratio of not greater than 2.5 to 1.0 is required.

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For the purposes of the ratio, Funded Debt generally means all obligations for borrowed money or for the deferred purchase price of property, and all capitalized lease obligations. Management believes the Company complied with these current covenants at March 31, 2009 and December 31, 2008.

The amended loan agreement also contains certain restrictive covenants. These include general prohibitions on: (i) disposing of property other than in the ordinary course of business; the Company changing its business; a change in control of the Company; mergers, acquisitions and the creation of new subsidiaries; the incurring of new indebtedness; the creation of new encumbrances or liens; investments, other than certain permitted investments in liquid investment grade paper; and the Company making loans, including loans to officers. Also, the amended loan agreement prohibits the Company from making any distributions (including any dividends on its common stock), or making any repurchases or redemptions of its capital stock, except to the extent there is no event of default either before or after any such distribution, repurchase or redemption. The bank may accelerate the Company s obligations under the amended loan agreement and the related promissory notes upon an event of default under the amended loan agreement. Events of default generally include the Company failing to make payments of principal or interest when due; defaults under loan covenants, subject to periods during which the Company may cure in certain cases; the Company becoming insolvent or being subject to certain bankruptcy proceedings, subject to certain time periods; and the occurrence of a material adverse change in the Company s business or financial condition. Upon an acceleration of the bank s loans to the Company, the bank, among other remedies, would have recourse to substantially all of the Company s assets through its security interest. There was $1,587 and $5,634 of outstanding draws under the facility as of March 31, 2009 and December 31, 2008, respectively.

Subordinated Notes

The Company has subordinated notes payable to shareholders with amounts outstanding totaling $1,950 at March 31, 2009 and December 31, 2008. Although the Company possessed adequate availability on the May 9, 2006 due date to repay the subordinated notes, management believed that cash flow from operations and remaining availability under the bank facility following such a drawdown would not be sufficient to fund ongoing working capital needs. The Company also anticipated that such a refunding of the subordinated notes with bank debt would have caused the Company to fail to comply with equity related covenants with the bank, given that the subordinated notes are treated as equity for such ratios. Accordingly, after consultation with the bank and the holders of the subordinated notes, the Company determined it was not in the best interest of all stakeholders to pay the notes at maturity, and the subordinated notes remain due and payable. We pay a default interest rate of 15%, both on the principal balance and any interest not paid quarterly. From time to time we have also deferred the payment of interest to preserve working capital. Specifically, we took this action in the first and second quarters of 2007 as a precautionary measure considering the cash requirement needed for the acquisition of the McAleer operations. Subsequently we paid this and other interest due and no interest was in arrears as of March 31, 2009 or as of the date of this report.

On April 23, 2008, we and each of the holders of the subordinated notes entered into a letter agreement which extended the maturity date of such notes until March 31, 2009. Each note holder also waived existing and past payment defaults and the notes continued to bear interest at the default rate of 15%. In exchange for the extension and waiver, we made principal payments on the subordinated notes totaling $300, paid pro-rata among the note holders. Again effective May 14, 2009, similar to the action taken at April 23, 2008, we and each of the holders of the subordinated notes entered into an informal agreement to extend the notes until August 30, 2009. In exchange for the extensions, we made a principal payment on the subordinated notes totaling $200, paid pro-rata among the note holders. Under this agreement, the Company will seek to enter into a new and separate term loan facility, preferably with its existing bank, to fund the payout of Barron, and to negotiate to restructure the notes payable to the remaining holders.

In conjunction with the Company entering into the extension with respect to the subordinated notes, it also entered into a waiver agreement (the Waiver) with the bank dated May 13, 2008. The bank had previously granted waivers with respect to cross-default and other provisions which may have been triggered by the payment default under the subordinated notes. The terms of the revolving credit facility with the bank restrict payments on the subordinated notes, and require the Company to obtain the bank s written consent prior to amending any of the terms of the subordinated notes. Accordingly, pursuant to the Waiver, the bank agreed to the terms of the extension and granted waivers of any defaults relating thereto.

Off Balance Sheet Instruments

As of March 31, 2009, for the periods reported, and through the filing date, CSI had no off-balance sheet instruments except for certain operating leases discussed in Note 7.

Related Party Transactions

During the first three months of 2009 the Company made interest payments to the five former shareholders of CSI South Carolina, all of whom are significant shareholders of the Company, and four of which are executive officers, and Barron, who owns all of the Company s preferred shares. These interest payments were made on the subordinated notes payable associated with the reverse merger transaction which occurred in 2005, and represented an annual interest rate of 15% as of March 31, 2009. In 2009, interest payments to the five original shareholders of CSI South Carolina totaled $73 and interest payments to Barron totaled $73.

NOTE 6 PREFERRED STOCK AND RELATED WARRANTS AND RETAINED EARNINGS

Warrants

On February 11, 2005, pursuant to the terms of a Preferred Stock Purchase Agreement with Barron, we issued to Barron common stock purchase warrants to purchase a total of 7,218 shares of our common stock.

Warrant exercises may be accomplished in one or a series of transactions, subject to a 4.9% beneficial ownership restriction. The terms and conditions of the warrants are identical except with respect to the exercise price.

The warrants may be exercised on a cashless basis. In such event, the Company would receive no proceeds from their exercise. So long as the Company maintains an effective registration statement for the shares underlying the warrants, a warrant holder is prohibited from utilizing a cashless exercise. The Company s registration statement was declared effective on February 14, 2006 and an updating amendment was declared effective on May 12, 2009.

Activity related to the common stock purchase warrants for the three month period ended March 31, 2009 and outstanding balances is as follows:

Common Stock Purchase Warrants

	Warrant A1	Warrant A2	Warrant B1	Warrant B2
Exercise Price	$ 1.3972	$ 0.70	$ 2.0958	$ 0.85
Expiration Date	2/10/2010	2/10/2010	2/10/2010	2/10/2010

Warrant related activity for the three months ended March 31, 2009

	Warrant A1	Warrant A2	Warrant B1	Warrant B2
Outstanding at December 31, 2008	2,000	555	2,000	1,609
Exercised first three months 2009				
Outstanding at March 31, 2009	2,000	555	2,000	1,609

Registration Rights Agreement

In conjunction with the Preferred Stock Purchase Agreement, the Company entered into a Registration Rights Agreement with Barron on February 10, 2005, whereby the Company agreed to register the shares of common stock underlying the preferred stock and warrants to be sold to Barron. Barron may also demand the registration of all or part of such shares on a one-time basis and, pursuant to piggy-back rights, may require the Company (subject to carve back by a managing underwriter) to include such shares in certain registration statements it may file. The Company is obligated to pay all expenses in connection with the registration of the shares.

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NOTE 7 COMMITMENTS, CONTINGENCIES, AND SUBSEQUENT EVENTS

Operating Leases

The Company leases certain facilities and equipment under various operating leases. At March 31, 2009, future minimum lease payments under non-cancelable leases were:

2009	$ 749
2010	978
2011	683
2012	72
Total	$ 2,482

Rent expense for the three months ended March 31, 2009 and 2008 was $102 and $51, respectively.

The Company entered into an operating lease on November 30, 2005 related to the lease of its office facility. The term of this lease is five years, beginning on April 1, 2006 and ending on March 31, 2011. The original commitment under this lease totaled $701, due on the first of each month in escalating monthly payments. The commitments under this lease are included in the future payments in the table above. If at any time the Company terminates the lease, the lessor may recover from the Company all damages approximately resulting from the termination, including the cost of recovering the premises and the worth of the balance of the lease over the reasonable rental value of the premises for the remainder of the lease term, which shall be due immediately. The Company does not anticipate terminating the lease at any time prior to its expiration.

On June 20, 2007, the Company and Chuck Yeager Real Estate amended the operating lease agreement, originally entered into on November 30, 2005, to include an additional 12,544 square feet of warehouse space. The lease of the additional warehouse space was the result of carrying additional inventory and increased monthly rent by approximately $2. While the lease on the additional space was scheduled to expire on August 31, 2007, the Company extended the lease until December 31, 2007. On April 1, 2008 the Company terminated the lease of this additional warehouse space, and entered into a one year lease with Edge Developments, LLC for 18,000 square feet of warehouse space located at 903B East Main Street, Easley, SC. The terms of this lease require monthly payments of $4, which are included in the schedule above, and are scheduled to expire on March 31, 2009, at which time the Company may choose to extend the lease.

On April 1, 2008, in connection with the acquisition of ICS (Note 3), the Company entered into a lease with Byers Properties, LLC for the lease by the Company of the former facilities of ICS. Byers Properties is controlled by Michael Byers, who is the sole shareholder of ICS. The term of the Lease begins April 1, 2008 and runs for a period of three years through March 2011. The lease calls for annual rent of $80, payable monthly. The leased property consists of a single-story brick building located on 2.57 acres in Triangle Industrial Park at 8518 Triad Drive, Colfax, North Carolina. The building comprises 7,207 square feet, with approximately 300 square feet being warehouse space. The future minimum lease payments under this lease are included in the schedule above. For further details on the acquisition of ICS, see Note 3 Acquisitions.

In August 2008, the Company entered into a corporate fleet lease program with Enterprise Fleet Services, for which individual vehicle leases are signed that may amount to a total commitment of $2.0 million over a weighted-average lease term of approximately three years. The future minimum lease payment for leases executed under the program as of March 31, 2009 is included in the schedule above.

Executive Officer Employment Agreements

The Company entered into separate employment agreements with each of the four most highly compensated executive officers on March 1, 2009. The term of all the employment agreements is three years, expiring on February 28, 2012. The agreements renew for a one year term automatically upon the expiration of the initial term or any renewal periods unless sooner terminated by any one of the parties. Such agreements provide for minimum salary levels adjusted for performance based on review by the Board of Directors. The aggregate commitment for future salaries at March 31, 2009, excluding bonuses, is approximately $2,501.

Investor Relations Firm Agreement

On May 13, 2009, we entered into an agreement with an investor relations firm, DC Consulting, LLC (DCC). DCC s experience with the retail investor market fits our goal of communicating our strategy and progress more broadly into our shareholder base. The agreement is for 90 days with options to extend for 90 day periods thereafter, or as agreed. Pursuant to the terms of the agreement, DCC will provide investor relations services for $12 per quarter and 15 shares of the Company s unregistered common stock. Also the company agreed to issue warrants for 300 shares of common stock in three blocks of 100 shares each at strike prices of $0.70, $1.00 and $1.20. The warrants expire in 2 years. Additionally, in the interim, if the stock price exceeds the warrant strike price for a period of 30 days and the warrants are not exercised the warrants expire. The common stock and warrants will be issued following the release of the Company s first quarter earnings in this Form 10-Q.

NOTE 8 SEGMENT INFORMATION

CSI is organized into the two reportable segments: Software applications and Technology solutions. Below is a description of the types of products and services from which each reportable segment derives its revenues.

Software applications segment

Through our Software applications segment, we report the results of the development, sales, and deployment and provision of ongoing support of our software applications, fund accounting based financial management software, standards based lesson planning software, solutions that facilitate single sign-on application access management provisioning based on Microsoft s Identity Lifecycle Management and Microsoft SharePoint deployments. Through this segment we also report the results of operations related to complimentary third-party applications and services we resell.

Technology solutions segment

Through our Technology solutions segment, we report the results of the technology solutions products through the sales and distribution of computers and accessories and the wide range of technology consulting services, including network and systems integration and computer support and maintenance services, that we provide.

Factors management used to identify our segments:

CSI s reportable segments are analyzed separately because of the differences in margin routinely generated by the major products within each group, and the differences in which sales and investment decisions may be made to evaluate existing or potential new products. Through its Software applications segment, the Company develops, sells, deploys and provides ongoing support of software applications. Through its Technology solutions segment, the Company provides technology solutions through the sale and distribution of computers and accessories and offers a wide range of technology consulting services, including network and systems integration and computer support and maintenance services.

There are no significant transactions between reportable segments. The total of Segment net sales and service revenue from all segments is equal to Net sales as reported in our Consolidated Statements of Operations. Sales and Cost of sales are included in each segment s (loss) income as reported in our Consolidated Statements of Operations. Accordingly, the total of the segments Gross profit is equal to Gross profit in our Consolidated Statements of Operations. Operating expenses are allocated to segment (loss) income based on estimate of sales and administrative time spent on each segment. None of the income or loss items following Operating (loss) income in our Consolidated Statements of Operations are allocated to our segments, since they are reviewed separately by management. Certain non-recurring items (those items occurring for reasons which have not occurred in the prior 2 years and are not likely to reoccur in 2 years) and compliance costs are generally excluded from management s analysis of profitability by segment and the Company s segment presentation. Accordingly, the total of Segment (loss) income from all segments, less non-recurring and compliance items, if any, is equal to Operating (loss) income as reported in our Consolidated Statements of Operations.

The total of Segment assets for all segments is equal to Total Assets as reported in our Consolidated Balance Sheets. The Company allocates shared assets related to liquidity (e.g., cash, accounts receivable and inventory) based on each segment s percent of revenues to total consolidated revenues. Capitalized computer software costs are allocated to the Software applications segment. Fixed assets, net, are allocated on the same basis as operating expenses (or by time spent on each segment as discussed above), since support equipment usage is generally tied to time utilized. All other assets are generally allocated on the same basis.

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The following tables summarize information about segment (loss) income for the three months ended March 31, 2009 and 2008, and assets allocated to segments as of March 31, 2009 and 2008.

	Software Applications	Technology Solutions	Total Company
Three months ended March 31, 2009:			
Net sales and service revenue	$ 3,321	$ 5,556	$ 8,877
Gross profit	1,058	724	1,782
Segment (loss) income	(359)	(429)	(*)
Segment assets	11,905	8,029	19,934
Three months ended March 31, 2008:			
Net sales and service revenue	$ 3,058	$ 9,005	$ 12,063
Gross profit	1,380	1,644	3,024
Segment income	377	573	(*)
Segment assets	8,722	8,557	17,279

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* See reconciliation below

Reconciliation of Segment (loss) income (non-GAAP measure) to operating (loss) income per consolidated Statements of Operations (GAAP measure):

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Segment (loss) income:		
Software applications segment	$ (359)	$ 377
Technology solutions segment	(429)	573
TOTAL SEGMENT (LOSS) INCOME	(788)	950
Less: merger-related and compliance costs		
Stock compensation non-cash	(2)	(5)
Acquisition costs	(1)	(24)
Professional and legal compliance and litigation related costs	(95)	(96)
OPERATING (LOSS) INCOME Per Consolidated Statement of Operations	$ (886)	$ 825

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

(All amounts are presented in thousands, except where specifically stated.)

A. Introduction

Unless the context requires otherwise, (1) Computer Software Innovations, Inc., CSI, we, our, us and the Company refer to the consolidat combined business of Computer Software Innovations, Inc., a Delaware corporation, and its subsidiary, CSI Technology Resources, Inc., a South Carolina corporation; (2) VerticalBuyer refers to the public Company prior to its merger with CSI South Carolina on February 11, 2005; and (3) CSI South Carolina refers to Computer Software Innovations, Inc., a South Carolina corporation, prior to the merger, which merged into VerticalBuyer in order for its operations to become publicly reported and its stock publicly traded.

Products and Services

We develop software applications and provide hardware-based technology solutions, focused primarily on the needs of organizations that employ fund accounting. Fund accounting is used by those entities that track expenditures and investments by fund, or by source and purpose of the funding (e.g., funds provided by government or grant sources), and is utilized primarily by public sector and not-for-profit entities. Our client base consists principally of K-12 (kindergarten through grade 12) public education and local government organizations including counties and municipalities. Our clients also include public libraries, disabilities boards, higher education and other non-governmental clients. While we have a significant number of non-education focused clients which represent the fastest growing sector based on increases in the number of new clients being added, our education focused customers typically generate more than 75% of our revenues in a given year.

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Organization

Our business efforts are focused on two key operating segments: internally developed software applications and related service and support (our Software applications segment), and other technology solutions and related service and support (our Technology solutions segment).

Software Applications Segment

Our Software applications segment develops accounting and administrative software applications that are designed for organizations that employ fund accounting. These organizations are primarily municipalities, school districts and local governments.

Our internally developed software consists primarily of three product focus groups:

Fund accounting based financial management software

Standards based lesson planning software

Identity lifecycle management and Microsoft SharePoint development

Our primary software, fund accounting based financial management software, is developed for those entities that track expenditures and investments by fund, or by source and purpose of the funding. Our client base for our financial management software consists principally of K-12 public education and local government organizations, including counties and municipalities. Our clients also include public libraries, disabilities boards, higher education and other non-governmental clients. In the initial state of our focus, South Carolina and that of an acquired operation, Alabama, over 90% of the K-12 education school districts run our proprietary fund accounting software. Our fund accounting software is also present in accounts in six other states in the Southeast. Specific software modules of our fund accounting based financial management software include:

General (or Fund) Ledger;

Accounts Payable;

Purchasing;

Payroll;

Personnel;

Employee Absence/Substitutes;

Inventory

Utility Billing; and