ROSS SYSTEMS INC/CA
Form 10-Q
May 17, 2004

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, 2004,

or

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

Commission File Number 0-19092

ROSS SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-2170198**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)
Two Concourse Parkway, Suite 800, Atlanta, Georgia	**30328**
(Address of principal executive offices)	(Zip code)

(770) 351-9600
(Registrant s telephone number, including area code)

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 kfiling requirements for the past 90 days. YES x NO o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). YES o NO x

As of May 14, 2004, the Registrant had outstanding 2,880,496 shares of Common Stock, and 500,000 Series A 7.5% convertible preference shares, (convertible preferred stock).

ROSS SYSTEMS, INC.
QUARTERLY REPORT ON FORM 10-Q
QUARTER ENDED MARCH 31, 2004

TABLE OF CONTENTS

This Quarterly Report on Form 10-Q, including Management s Discussion and Analysis of Financial Condition and Results of Operations in Item 2, contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause the results of Ross Systems to differ materially from those expressed or implied by such forward-looking statements. All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including any projections of earnings, revenue, synergies, accretion, margins or other financial items; any statement containing the proposed merger with chinadotcom corporation; any statements of the plans, strategies and objectives of management for future operations, including the execution of integration and restructuring plans; any statement concerning proposed new products, services, developments or industry rankings; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing. The risks, uncertainties and assumptions referred to above include the performance of contracts by customers and partners; employee management issues; the challenge of managing asset levels; the difficulty of aligning expense levels with revenue changes; and other risks that are described herein and that are otherwise described from time to time in Ross Systems Securities and Exchange Commission reports. Ross Systems assumes no obligation and does not intend to update these forward-looking statements.

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ROSS SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share related data)

	March 31, 2004	June 30, 2003
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 8,751	$ 8,628
Accounts receivable, less allowance for doubtful accounts of $1,509 and $1,532, at March 31, 2004, and June 30, 2003 respectively	14,967	12,880
Prepaid and other current assets	805	731
Total current assets	24,523	22,239
Property and equipment, net	1,208	1,406
Computer software costs, net	12,617	13,573
Other assets	2,993	2,993
Total assets	$ 41,341	$ 40,211
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Short term debt	$ 5,049	$ 2,800
Accounts payable	1,436	2,978
Accrued expenses	5,055	4,940
Income taxes payable	177	261
Deferred revenues	11,944	12,203
Total current liabilities	23,661	23,182
Shareholders equity:		
Convertible Preferred stock, no par value 5,000,000 shares authorized; 500,000 shares issued and outstanding	2,000	2,000
Common stock, $0.001 par value; 15,000,000 shares	28	28

authorized; 2,879,470 and 2,815,603 shares issued and outstanding		
Additional paid-in capital	87,275	87,189
Accumulated deficit	(68,669)	(69,094)
Accumulated other comprehensive deficit	(1,834)	(1,749)
Treasury stock at cost, 133,977 and 158,973 shares	(1,120)	(1,345)
Total shareholders equity	17,680	17,029
Total liabilities and shareholders equity	$ 41,341	$ 40,211

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

Table of Contents

ROSS SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)

	Three months ended March 31, (unaudited)		Nine months ended March 31, (unaudited)	
	2004	**2003**	**2004**	**2003**
Revenues:				
Software product licenses	$ 4,244	$ 2,696	$11,594	$ 9,903
Consulting and other services	4,237	3,489	11,815	9,794
Maintenance	5,191	5,235	15,538	15,323
Total revenues	13,672	11,420	38,947	35,020
Operating expenses:				
Costs of software product licenses (inclusive of amortization of capitalized computer software costs)	1,764	1,660	5,090	4,786
Costs of consulting, maintenance and other services	5,313	4,229	15,491	12,784
Software product license sales and marketing	3,272	2,864	9,021	8,193
Product development net of capitalized computer software costs	778	605	2,417	1,893
General and administrative	812	1,016	2,807	3,420
Litigation settlement			1,896	
Provision for uncollectible accounts	188	197	418	711
Total operating expenses	12,127	10,571	37,140	31,787
Operating profit	1,545	849	1,807	3,233
Other expenses, net	(113)	(29)	(144)	(152)
Proposed merger transaction costs	(139)		(1,133)	
Income tax expense	(22)	(63)	(105)	(217)
Net income	1,271	757	425	2,864
Preferred stock dividend	(38)	(38)	(113)	(113)
Net income available to common shareholders	$ 1,233	$ 719	$ 312	$ 2,751

Net income per common share basic	$ 0.45	$ 0.27	$ 0.12	$ 1.05
Net income per common share diluted	$ 0.36	$ 0.22	$ 0.12	$ 0.87
Shares used in per share computation basic	2,728	2,638	2,707	2,616
Shares used in per share computation diluted	3,513	3,387	3,477	3,292

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

Table of Contents

ROSS SYSTEMS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Nine months ended March 31, (unaudited)	
	2004	**2003**
Cash flows from operating activities:		
Net income	$ 425	$ 2,864
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	559	556
Amortization of computer software costs	3,707	3,526
Provision for uncollectible accounts	418	711
Changes in operating assets and liabilities:		
Accounts receivable	(2,370)	(1,723)
Prepaid and other current assets	(63)	906
Income taxes recoverable/payable	(84)	235
Accounts payable	(1,510)	(374)
Accrued expenses	267	504
Deferred revenues	(226)	(701)
Cash provided by operating activities	1,123	6,504
Purchases of property and equipment, net	(302)	(551)
Computer software costs capitalized	(2,908)	(3,317)
Other		44
Cash used in investing activities	(3,210)	(3,824)
Cash flows from financing activities:		
Net cash received (paid) on line of credit activity	2,249	(169)
Repurchase of treasury stock		(1,426)
Proceeds from issuance of common stock	310	262
Preference dividend paid	(113)	
Cash provided by (used in) financing activities	2,446	(1,333)

Effect of exchange rate changes on cash	(236)	(198)
Net increase in cash and cash equivalents	123	1,149
Cash and cash equivalents at beginning of fiscal year	8,628	5,438
Cash and cash equivalents at end of fiscal quarter	$ 8,751	$ 6,587
Supplemental disclosures of cash flow information:		
Cash paid for interest charges	$ 67	$ 75
Cash paid for taxation charges	$ 79	$ 104

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

Table of Contents

ROSS SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1) BUSINESS OF THE COMPANY & BASIS OF PRESENTATION

Description of Business and Summary of Significant Accounting Policies

Business of the Company

Ross Systems, Inc. (the Company or Ross ; NASDAQ: ROSS) delivers innovative software solutions that help manufacturers worldwide fulfill their business growth objectives through increased operational efficiencies, improved profitability, strengthened customer relationships and streamlined regulatory compliance. Focused on the food and beverage, life sciences, chemicals, metals and natural products industries and implemented by over 1,000 customer companies worldwide, the company s family of Internet-architected solutions is a comprehensive, modular suite that spans the enterprise, from manufacturing, financials and supply chain management to customer relationship management, performance management and regulatory compliance.

Publicly traded on the Nasdaq National Market since 1991, Ross s global headquarters are based in the U.S. in Atlanta, Georgia, with sales and support operations around the world.

The Company operates in one business segment (software) and no individual customer accounted for more than 10% of total revenues in the quarter ended March 31, 2004. The Company does not have a concentration of credit risk in any one industry. Approximately 66% of the Company s revenues are derived from the North American market.

The accompanying unaudited condensed consolidated financial statements of the Company reflect all adjustments of a normal recurring nature which are, in the opinion of management, necessary to present a fair statement of its financial position as of March 31, 2004, and the results of its operations and cash flows for the interim periods presented. The Company s results of operations for the three months ended March 31, 2004 are not necessarily indicative of the results to be expected for the full year.

These unaudited condensed consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q, and therefore, certain information and footnote disclosures normally contained in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These financial statements should be read in conjunction with the Consolidated Financial Statements and notes thereto included in the Company s Annual Report to Stockholders on Form 10-K/A for the fiscal year ended June 30, 2003 which was filed with the Securities and Exchange Commission.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates.

Basis of Presentation

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company balances and transactions have been eliminated in consolidation.

Stock Based Compensation.

The company measures compensation cost for its stock incentive and option plans using the intrinsic value-based method of accounting.

Had the company used the fair value-based method of accounting to measure compensation expense for its stock incentive and option plans and charged compensation cost against income over the vesting periods, based on the fair value of options at the date of grant, net income or loss and the related basic and diluted per common share amounts for the three and nine months ended March 31, 2004 and 2003 would have been as follows:

Table of Contents

ROSS SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share data)

	Three months ended March 31,		Nine months ended March 31,	
	2004	**2003**	**2004**	**2003**
Net income available to common shareholders:				
As reported	$1,233	$ 719	$ 312	$2,751
Deduct: Total stock-based employee compensation expense under fair value-based method, net of tax	(235)	(56)	(763)	(341)
Pro forma net income (loss) available to common shareholders	$ 998	$ 663	$ (451)	$2,410
Basic net earnings (loss) per share:				
As reported	$ 0.45	$0.27	$ 0.12	$ 1.05
Pro forma	0.37	0.25	(0.17)	0.92
Diluted net earnings (loss) per share:				
As reported	0.36	0.22	0.12	0.87
Pro forma	0.29	0.21	(0.17)	0.77

The following weighted average assumptions for the Company s Stock Option Plan were used to determine the pro forma amounts noted above:

	Three months ended March 31,		Nine months ended March 31,	
	2004	**2003**	**2004**	**2003**
Expected life (years)	5	5	5	5
Expected volatility	30.0%	66.2%	30.0%	66.2%
Risk-free interest rate	5.0%	4.3%	5.0%	4.3%
Expected dividend yield	None	None	None	None

Revenue Recognition.

In accordance with Securities and Exchange Commission Staff Accounting Bulletin No. 101 Revenue Recognition in Financial Statements, the Company recognizes revenues from licenses of computer software up-front provided that a non-cancelable license agreement has been signed, the software and related documentation have been shipped, there are no material uncertainties regarding customer acceptance, collection of the resulting receivable is deemed probable, and no significant other vendor obligations exist. The revenue associated with any license agreements containing cancellation or refund provisions is deferred until such provisions lapse. Where the Company has future obligations, if such obligations are insignificant, related costs are accrued immediately. When the obligations are significant, the software product license revenues are deferred. Future contractual obligations can include software customization, requirements to provide additional products in the future and porting products to new platforms. Contracts which require significant software customization are accounted for on the percentage-of-completion basis. Revenues related to significant obligations to provide future products or to port existing products are deferred until the new products or ports are completed.

The Company s revenue recognition policies are designed to comply with American Institute of Certified Public Accountants Statement of Position (SOP) 97-2, Software Revenue Recognition, and with SEC Staff Accounting Bulletin (SAB) No. 101, Revenue Recognition in Financial Statements. Revenues recognized from multiple-element software license contracts are allocated to each element of the contracts based

ROSS SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

on the fair values of the elements, such as licenses for software products, maintenance, or professional services. The determination of fair value is based on objective evidence which is specific to the Company. The Company limits its assessment of objective evidence for each element to either the price charged when the same element is sold separately, or the price established by management having the relevant authority to do so, for an element not yet sold separately. If evidence of fair value of all undelivered elements exists but evidence does not exist for one or more delivered elements, then revenue is recognized using the residual method. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is recognized as revenue.

The Company utilizes distributors primarily in geographic areas where the Company does not maintain a physical presence. The Company s revenue recognition policies with respect to sales by distributors complies with SOP 97-2 and SAB 101 in that all the revenue recognition criteria listed above are met. In addition, distributors do not have rights of return, price protection, rotation rights, or other features that would preclude revenue recognition. Generally, the value of software license sales to distributors is based on list selling prices to their customer less a discount at a predetermined rate. Similarly, the Company earns revenue from distributors based on a predetermined percentage of the maintenance fees billed by the distributor to the end customer. The distributor typically retains any fees earned by them for implementation services they perform. Distributorships may or may not be geographically exclusive, and are generally subject to annual renewals by the Company.

Service revenues generated from professional consulting and training services are recognized as the services are performed. Maintenance revenues, including revenues bundled with original software product license revenues, are deferred and recognized over the related contract period, generally 12 months.

Computer Software Costs.

The Company capitalizes computer software product development costs incurred in developing a product once technological feasibility has been established and until the product is available for general release to customers. Technological feasibility is established when the Company either (1) completes a detail program design that encompasses product function, features and technical requirements and is ready for coding, and confirms that the product design is complete, that the necessary skills, hardware and software technology are available to produce the product, that the completeness of the detail program design is consistent with the product design by documenting and tracing the detail program design to the product specifications, that the detail program design has been reviewed for high-risk development issues, and that any related uncertainties have been resolved through coding and testing or (2) completes a product design and working model of the software product, and the completeness of the working model and its consistency with the product design have been confirmed by testing. The Company evaluates the expected future realizability of the capitalized amounts based on expected revenues from the product over the remaining product life. Where future projected revenue streams are not expected to cover remaining amounts to be amortized, the Company either accelerates amortization or expenses the remaining capitalized amounts. Amortization of such costs is computed as the greater of (1) the ratio of current revenues to expected future revenues from the related future product sales or (2) a straight-line basis over the estimated useful life of the product (not to exceed five years). Software costs related to the development of new products incurred prior to establishing technological feasibility or after general release are expensed as incurred.

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity date of three months or less to be cash equivalents.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable is comprised of trade receivables that are credit based and do not require collateral. Generally, the Company s credit terms are 30 days but in some instances the Company offers extended payment terms to customers purchasing software licenses. The Company has a history of offering extended payment terms from time to time for competitive reasons. These terms are not offered in connection with any contingencies related to product acceptance, implementation, or any other service obligation or

ROSS SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

contingencies post-transaction, and the Company has not offered concessions as a result of these terms. Payment arrangements in these circumstances typically require payment of a significant portion of the total contract amount within 30 days of the sale, with two to three subsequent installments typically within six months. The Company has not found collectibility to be compromised as a result of these terms. In no case have payment terms extended beyond 12 months. Based on historical results, the Company believes that its revenue recognition policies comply with all components of SOP 97-2, including that the product has been shipped and that the arrangement is fixed and determinable.

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. On an ongoing basis, the Company evaluates the collectibility of accounts receivable based upon historical collections and assessment of the collectibility of specific accounts. Ross specifically reviews the collectibility of accounts with outstanding balances in excess of 90 days. The Company evaluates the collectibility of specific accounts using a combination of factors, including the age of the outstanding balances, evaluation of the underlying company s financial condition, recent payment history, and discussions with the account executive responsible for the specific customer. Based upon this evaluation, an increase or decrease required in the allowance for doubtful accounts is reflected in the period in which the evaluation indicates that a change is necessary. Any change in the allowance for doubtful accounts could have an impact on the Company s financial condition, results of operation and cash flows.

Property and Equipment

Property and equipment are stated at cost. Depreciation is recorded using the straight-line method over the estimated useful lives of the respective assets, generally three to seven years. Leasehold improvements and equipment under capital leases are amortized using the straight-line method over the shorter of the terms of the related leases or the respective useful lives of the assets.

Long-lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the sum of the expected future undiscounted cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and the carrying value of the asset.

Fair Value of Financial Instruments

The carrying amounts reported on the balance sheet for accounts receivable, notes receivable, accounts payable and short term debt approximate their fair values.

Income Taxes

In accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* (SFAS 109), the Company utilizes the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are established to recognize the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

Foreign Operations and Currency Translation

The local currencies (typically Euros and Pounds Sterling) of the Company s foreign subsidiaries are the functional currencies. Assets and liabilities of foreign subsidiaries are translated into U.S. dollars at current exchange rates, and the resulting translation gains and losses are included as an adjustment to shareholders equity as a component of comprehensive income. Transaction gains and losses that relate to U.S. dollar denominated intercompany short-term receivables are recorded in the financial statements of the Company s foreign subsidiaries and are reflected in income. Where related intercompany balances have been designated as long-term, gains and losses are included as an adjustment to shareholders equity as a component of comprehensive income.

ROSS SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Reclassifications

It is the Company s policy to reclassify prior year amounts to conform with current year financial statement presentation when necessary.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates.

Advertising Costs

The Company generally expenses advertising costs at the time the advertisement is published, or in the case of direct mail, when mailed. Advertising costs for the three months ended March 31, 2004 and 2003 were approximately $228,000 and $125,000 respectively. Advertising costs for the nine months ended March 31, 2004 and 2003 were approximately $547,000 and $415,000 respectively

Segment Information

SFAS No. 131 Disclosures about Segments of an Enterprise and Related Information established standards for the way that public business enterprises report information about operating segments in their financial statements. The standard defines operating segments as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and assess performance. Based on these standards the Company has determined that it operates in four geographical segments: Northern Europe, Spain, the United Kingdom and North America.

The Company has no customers that represent ten percent or more of annual revenues.

For management purposes, the results of the Asian operations are included in the North American results since the costs associated with managing the Asian market place are born by the North American entities within the Group. Revenues in the Asian markets comprise less than 5% of total revenues reported for the North American segment. Selected balance sheet and income statement information pertaining to the various significant geographic areas of operation are as follows:

As of and for the quarter ended March 31, 2004 (in thousands):

	Total Assets	Revenue	Net Income Available to Common Shareholders	Depreciation and Amortization	Capital Expenditures

Northern Europe	$ 7,800	$ 1,517	$ 105	$ 15	$ 6
Spain	7,524	1,603	(152)	91	
United Kingdom	2,673	1,560	81	14	1
North America	23,344	8,992	1,199	72	91
Total	$41,341	$13,672	$1,233	$ 192	$ 98

Table of Contents

ROSS SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

As of and for the quarter ended March 31, 2003, (in thousands):

	Total Assets	Revenue	Net Income Available to Common Shareholders	Depreciation and Amortization	Capital Expenditures
Northern Europe	$ 2,622	$ 1,041	$ (34)	$ 16	$ 2
Spain	6,399	1,647	225	59	
United Kingdom	3,428	1,559	143	15	
North America	26,184	7,173	385	69	114
Total	$38,633	$11,420	$ 719	$ 159	$ 116

As of and for the nine months ended March 31, 2004 (in thousands):

	Total Assets	Revenue	Net Income Available to Common Shareholders	Depreciation and Amortization	Capital Expenditures
Northern Europe	$ 7,800	$ 3,763	$ 231	$ 43	$ 21
Spain	7,524	4,944	43	254	79
United Kingdom	2,673	4,736	509	43	10
North America	23,344	25,504	(471)	219	192
Total	$41,341	$38,947	$ 312	$ 559	$ 302

As of and for the nine months ended March 31, 2003 (in thousands):

	Total Assets	Revenue	Net Income Available to Common Shareholders	Depreciation and Amortization	Capital Expenditures
Northern Europe	$ 2,622	$ 3,479	$ 278	$ 47	$ 25
Spain	6,399	4,667	635	208	148
United Kingdom	3,428	4,171	338	40	39
North America	26,184	22,703	1,500	261	339
Total	$38,633	$35,020	$2,751	$ 556	$ 551

Ne