

SIMPLETECH INC  
Form 10-Q  
August 14, 2001

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**FORM 10-Q**

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

**For the quarterly period ended June 30, 2001**

**or**

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

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

**Commission File Number 000-31623**

**SIMPLETECH, INC.**

(Exact name of Registrant as specified in its charter)

**CALIFORNIA**

(State or other jurisdiction of incorporation or organization)

**33-0399154**

(I.R.S. EmployerIdentification No.)

**3001 Daimler Street**

**Santa Ana, CA**

(Address of principal executive offices)

**92705-5812**

(Zip Code)

**(949) 476-1180**

(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 filing requirements for the past 90 days. Yes  No

The number of shares outstanding of the Registrant's common stock, par value \$0.001, as of June 30, 2001 was 38,262,961.



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Except as otherwise noted in this report, SimpleTech, the company, we, us and our collectively refer to SimpleTech, Inc.

### PART I. FINANCIAL INFORMATION

#### Item 1. Financial Statements

SimpleTech, Inc.  
Consolidated Balance Sheets  
(in thousands, except share amounts)

	<u>June 30, 2001</u>	<u>December 31, 2000</u>
	(unaudited)	
<b>ASSETS:</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	\$ 41,091	\$ 33,747
Accounts receivable, net of allowances of \$1,183 at June 30, 2001 and \$972 at December 31, 2000	11,121	28,103
Inventory, net	17,281	31,052
Deferred income taxes	2,060	2,060
Other current assets	3,507	1,069
	<u>75,060</u>	<u>96,031</u>
Furniture, fixtures and equipment, net	7,508	6,926
Deferred income taxes	329	329
	<u>82,897</u>	<u>103,286</u>
	\$	\$
	82,897	103,286
<b>LIABILITIES AND SHAREHOLDERS' EQUITY:</b>		
<b>Current Liabilities:</b>		
Accounts payable	\$ 4,541	\$ 25,950
Current maturities of long-term debt	794	761
Current maturities of capital lease obligations	562	801
Accrued and other liabilities	3,115	4,219
	<u>9,012</u>	<u>31,731</u>
Total current liabilities	9,012	31,731
Long-term debt	677	1,083
Capital lease obligations	338	560
	<u>10,027</u>	<u>33,374</u>
Total liabilities	10,027	33,374
<b>Shareholders' Equity:</b>		
Preferred stock, \$0.001 par value, 20,000,000 shares authorized, no shares issued and outstanding	---	---
	38	38

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Common stock, \$0.001 par value, 100,000,000 shares authorized,  
38,262,961 shares issued and outstanding as of June 30, 2001;  
37,572,667 shares issued and outstanding as of December 31, 2000

Additional paid-in capital	64,820	63,911
Unearned stock-based compensation	(38)	(63)
Retained earnings	8,050	6,026
	<hr/>	<hr/>
Total shareholders' equity	72,870	69,912
	<hr/>	<hr/>
Total liabilities and shareholders' equity	\$ 82,897	\$ 103,286
	<hr/>	<hr/>

See accompanying notes to unaudited consolidated financial statements.

SimpleTech, Inc.  
Consolidated Statements of Operations  
(in thousands, except per share amounts)  
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	2000	2001	2000
	<hr/>	<hr/>	<hr/>	<hr/>
Net revenues	\$ 36,768	\$ 74,812	\$ 95,483	\$ 132,647
Cost of revenues	31,149	58,224	74,402	103,237
	<hr/>	<hr/>	<hr/>	<hr/>
Gross profit	5,619	16,588	21,081	29,410
	<hr/>	<hr/>	<hr/>	<hr/>
Sales and marketing	4,625	5,114	9,905	9,461
General and administrative	3,377	3,479	6,353	6,265
Research and development	1,206	994	2,263	1,512
	<hr/>	<hr/>	<hr/>	<hr/>
Total operating expenses	9,208	9,587	18,521	17,238
	<hr/>	<hr/>	<hr/>	<hr/>
Income (loss) from operations	(3,589)	7,001	2,560	12,172
Interest expense	54	520	117	806
Interest income	(435)	-	(914)	(1)
	<hr/>	<hr/>	<hr/>	<hr/>
Income (loss) before provision (benefit) for income taxes	(3,208)	6,481	3,357	11,367
Provision (benefit) for income taxes	(1,274)	231	1,333	175
	<hr/>	<hr/>	<hr/>	<hr/>
Net income (loss)	\$ (1,934)	\$ 6,250	\$ 2,024	\$ 11,192
	<hr/>	<hr/>	<hr/>	<hr/>
Pro forma data:				
Income before provision for income taxes		\$ 6,481		\$ 11,367

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Provision for income taxes		2,462		4,319	
Pro forma net income	\$	4,019	\$	7,048	
Net income (loss) per share (pro forma in 2000):					
Basic	\$	(0.05)	\$ 0.13	\$ 0.05	\$ 0.23
Diluted	\$	(0.05)	\$ 0.12	\$ 0.05	\$ 0.21
Weighted average shares outstanding:					
Basic		38,241	30,601	37,968	30,601
Diluted		38,241	33,077	39,377	33,361

See accompanying notes to unaudited consolidated financial statements.

SimpleTech, Inc.  
Consolidated Statements of Cash Flows  
(in thousands)  
(unaudited)

	Six Months Ended June 30,	
	2001	2000
Cash flow from operating activities:		
Net income	\$ 2,024	\$ 11,192
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,684	1,361
Loss on sale of furniture, fixtures and equipment	4	1
Accounts receivable provisions	1,518	1,249
Inventory excess and obsolescence expense	918	365
Deferred income taxes	-	171
Compensation related to stock options vesting	25	23
Change in operating assets and liabilities:		
Accounts receivable	15,464	(2,122)
Inventory	12,853	(23,211)
Other assets	(2,438)	(8)
Accounts payable	(21,409)	4,813
Accrued and other liabilities	(1,104)	1,764
Net cash provided by (used in) operating activities	9,539	(4,402)

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Cash flows from investing activities:		
Purchase of furniture, fixtures and equipment	(2,437)	(1,044)
Proceeds from sale of furniture, fixtures and equipment	167	228
Net cash used in investing activities	(2,270)	(816)
Cash flows from financing activities:		
Deferred offering costs	-	(937)
Borrowings under line of credit, net	-	10,796
Repayment of borrowings from banks	(373)	(341)
Payment on capital lease obligations	(461)	(456)
Repayment of loans to related parties, net	-	40
Distributions to shareholders	-	(7,640)
Proceeds from exercise of stock options	909	-
Net cash provided by financing activities	75	1,462
Net increase (decrease) in cash	7,344	(3,756)
Cash and cash equivalents at beginning of period	33,747	3,779
Cash and cash equivalents at end of period	\$ 41,091	\$ 23

See accompanying notes to unaudited consolidated financial statements.

**SIMLETECH, INC**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**Note 1 - Basis of Presentation**

The accompanying interim consolidated financial statements are unaudited and have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal and recurring accruals) considered necessary for a fair presentation of the consolidated financial position of the Company at June 30, 2001 and the consolidated results of operations and cash flows for the three and six months ended June 30, 2001 and 2000 have been included. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes contained in the Annual Report on Form 10-K filed with the SEC. The December 31, 2000 balances reported herein are derived from the audited consolidated financial statements included in the Annual Report on Form 10-K for the fiscal year ended December 31, 2000. The results for the interim periods are not necessarily indicative of results to be expected for the full fiscal year.

The consolidated financial statements of the Company include the accounts of the Company's subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

**Note 2 - 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 certain estimates and assumptions that affect the reported amounts of assets and liabilities (e.g., bad debt reserves and inventory reserves), disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Note 3 - Net Income Per Share**

Basic earnings per share is computed by dividing net income by the weighted average number of shares outstanding. In computing diluted earnings per share, the weighted average number of shares outstanding is adjusted to additionally reflect the effect of potentially dilutive securities. For the quarter ended June 30, 2000, and the six months ended June 30, 2001 and 2000, potentially dilutive securities consisted solely of options and resulted in potential common shares of 2,475,832, 1,409,006 and 2,759,555, respectively. No potential common shares were included in the diluted per share amount for the three months ended June 30, 2001, as the effect would have been anti-dilutive.

For the three and six months ended June 30, 2000, pro forma net income was computed using an effective tax rate of 38% to reflect the estimated income tax expense of the Company as if it had been subject to C corporation federal and state income taxes during the period, instead of S corporation income taxes.

**Note 4 - Supplemental Balance Sheet Information**

Inventory consists of the following:

(In thousands)	June 30, 2001		December 31, 2000	
Raw materials	\$	15,898	\$	24,768
Work-in-progress		361		759
Finished goods		5,447		9,652
		21,706		35,179
Reserve for excess and obsolescence		(4,425)		(4,127)
Inventory, net	\$	17,281	\$	31,052

Furniture, fixtures and equipment consist of the following:

(In thousands)	June 30, 2001		December 31, 2000	
Furniture and fixtures	\$	298	\$	294
Equipment		18,806		16,769
		19,104		17,063
Accumulated depreciation		(11,596)		(10,137)
Furniture, fixtures and equipment, net	\$	7,508	\$	6,926

**Note 5 Dense-Pac Microsystems, Inc. Litigation**

On February 7, 2001, the Court ruled on pending summary judgment motions in the lawsuit the Company filed in September 1998 against Dense-Pac Microsystems, Inc. In this lawsuit filed in Federal Court in Santa Ana, the Company alleged that Dense-Pac infringed the Company's IC Tower stacking patent, U.S. Patent No. 5,514,907. Dense-Pac counterclaimed for infringement of its stacking patent, U.S. Patent No. 4,956,694. The Company sought damages and an injunction against infringement of its patent by Dense-Pac. Dense-Pac denied the infringement and asserted a defense of patent invalidity and a counterclaim against the Company alleging infringement of its stacking patent.

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In the Court's summary judgment rulings, the Court found non-infringement by Dense-Pac as to the Company's patent and non-infringement by the Company as to Dense-Pac's patent. The Company has appealed the adverse summary judgment ruling to U.S. Court of Appeals for the Federal Circuit in Washington, D.C. Dense-Pac has not appealed the Court's ruling that the Company did not infringe the Dense-Pac patent, and that ruling is now final.

On February 21, 2001, the Company filed a new lawsuit against Dense-Pac in Federal Court in Santa Ana for infringement of its IC Tower stacking patent, U.S. Patent No. Re. 36,916 (a reissue of U.S. Patent No. 5,514,907 referenced above). The Company is seeking damages, an injunction against further infringement, and related costs. Dense-Pac filed its answer on March 13, 2001, denying infringement, asserting a defense of patent invalidity, and alleging technology misappropriation by the Company. Trial has been set for October 22, 2002.

### Note 6 Segment Information:

The Company designs, manufactures and markets a comprehensive line of memory, storage and connectivity products used in high performance computing, networking and communications, consumer electronics and industrial applications. The Company provides technology solutions for two reportable operating segments, Industrial (formerly termed Original Equipment Manufacturer or OEM) and Commercial (formerly termed Aftermarket), based on DRAM, SRAM and Flash memory technologies.

Beginning in 1999, after completion of management information system enhancements, the Company used net sales and gross profit as the basis for evaluating the performance of its operating segments. The Company does not allocate operating expenses, interest or income taxes to operating segments. Due to the similarity of products manufactured for customers within each operating segment, the Company does not maintain separate records to identify assets by operating segment.

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

(in thousands)	Three Months Ended June 30, 2001			Three Months Ended June 30, 2000		
	Industrial	Commercial	Consolidated	Industrial	Commercial	Consolidated
Net revenues	\$ 7,738	\$ 29,030	\$ 36,768	\$ 28,662	\$ 46,150	\$ 74,812
Cost of revenues	5,938	25,211	31,149	20,594	37,630	58,224
Gross profit	\$ 1,800	\$ 3,819	\$ 5,619	\$ 8,068	\$ 8,520	\$ 16,588

  

	Six Months Ended June 30, 2001			Six Months Ended June 30, 2000		
	Industrial	Commercial	Consolidated	Industrial	Commercial	Consolidated
Net revenues	\$ 32,625	\$ 62,858	\$ 95,483	\$ 47,690	\$ 84,957	\$ 132,647
Cost of revenues	21,686	52,716	74,402	34,155	69,082	103,237
Gross profit	\$ 10,939	\$ 10,142	\$ 21,081	\$		\$