COTELLIGENT INC
Form 10-Q
January 07, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For The Quarterly Period Ended June 30, 2002

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

For the Transition Period from _____ to ____

Commission File Number 0-27412

COTELLIGENT, INC.
(Exact name of registrant as specified in its charter)

Delaware	94-3173918
(State of incorporation)	(I.R.S. ID)

100 Theory, Suite 200, Irvine, California 92612
(Address of principal executive offices)

(949) 823-1600
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [ ] No [X]

At January 2, 2003, there were 14,801,354 shares of common stock outstanding.

COTELLIGENT, INC.

INDEX

Item 1. Financial Statements

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	June 30, 2002	December 3 2001 (Restated
ASSETS		
Current assets:		

Cash and cash equivalents	$ 20,555	$ 18,778
Refundable income taxes	7,695	7,008
Accounts receivable, including unbilled accounts of $627 and $1,627 and net of allowance for doubtful accounts of $610 and $533, respectively	2,753	5,693
Current assets of discontinued operations	122	151
Notes receivable from officers and stockholder, net of valuation allowance of $1,703	--	--
Current portion of note receivable from acquirer of discontinued operation	1,000	835
Prepaid expenses and other current assets	1,039	806
Total current assets	33,164	33,271
Property and equipment, net	81	--
Note receivable from acquirer of discontinued operation	1,089	1,564
Equity investment in alliance partner	561	847
Other assets	349	398
Total assets	$ 35,244	$ 36,080

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:		
Accounts payable	$ 937	$ 1,651
Accrued compensation and related payroll liabilities	1,761	2,144
Restructuring liabilities	132	331
Deferred revenue	476	874
Other accrued liabilities	2,567	2,074
Total current liabilities	5,873	7,074
Restructuring liabilities, net of current portion	854	959
Other long-term liabilities, net of current portion	257	465
Income tax payable	2,618	2,618
Total liabilities	9,602	11,116
Stockholders' equity:		
Preferred Stock, $0.01 par value; 500,000 shares authorized, no shares issued or outstanding	--	--
Common Stock, $0.01 par value; 100,000,000 shares authorized, 15,545,954 and 15,514,757 shares issued, respectively	155	155
Additional paid-in capital	86,666	86,662
Notes receivable from stockholders	(6,193)	(6,193
Accumulated deficit	(54,486)	(55,160
Treasury Stock	(500)	(500
Total stockholders' equity	25,642	24,964
Total liabilities and stockholders' equity	$ 35,244	$ 36,080

See accompanying notes to condensed consolidated financial statements.

3

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share data)

	Three Months Ended June 30,		Six Mon
	2002	2001	2002
		(Restated)	
Revenues	$ 4,302	$ 12,460	$ 10
Cost of services	2,675	9,443	6
Gross profit	1,627	3,017	3
Research and development costs	599	209	
Selling, general and administrative expenses	5,008	9,533	9
Operating loss	(3,980)	(6,725)	(6
Other income (expense):			
Interest expense	(24)	(30)	
Interest income	85	273	
Other	(129)	(294)	
Total other income (expense)	(68)	(51)	
Loss from continuing operations before income taxes	(4,048)	(6,776)	(6
Benefit for income taxes	96	--	7
Income (loss) from continuing operations	(3,952)	(6,776)	
Gain (loss) on sale of discontinued operations, net of income tax expense of $0, $0, $0, $0	82	1	
Net income (loss)	$ (3,870)	$ (6,775)	$
Earnings (loss) per share:			
Basic -			
Income (loss) from continuing operations	$ (0.26)	$ (0.44)	$
Income (loss) from discontinued operations	--	--	
Net income (loss)	$ (0.26)	$ (0.44)	$
Diluted -			
Income (loss) from continuing operations	$ (0.26)	$ (0.44)	$
Income (loss) from discontinued operations	--	--	
Net income (loss)	$ (0.26)	$ (0.44)	$
Weighted average number of shares outstanding			
Basic	14,901,054	15,273,716	14,895
Diluted	14,901,054	15,273,716	17,387

See accompanying notes to condensed consolidated financial statements.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Six Months 2002
Cash flows from operating activities:	
Income (loss) from continuing operations	$ 592
Adjustments to reconcile income (loss) from continuing operations to net cash provided by (used for) operating activities:	
Equity loss from investment in alliance partner	286
Depreciation and amortization	3
Provision for doubtful accounts	77
Deferred taxes, net	(7,496)
Changes in current assets and liabilities:	
Accounts receivable	2,863
Prepaid expenses and other current assets	(233)
Income taxes, net	6,809
Accounts payable and accrued liabilities	(1,116)
Deferred revenue	(398)
Other assets	49
Cash provided by (used for) operating activities	1,436
Cash flows from investing activities:	
Payments received on note from acquirer of discontinued operations	310
Purchases of property and equipment	(84)
Cash provided by (used for) investing activities	226
Cash flows from financing activities:	
Payments on capital lease obligations	--
Net proceeds on issuance of common stock	4
Purchase of treasury stock	--
Cash provided by (used for) financing activities	4
Cash flows provided by discontinued operations	111
Net increase (decrease) in cash	1,777
Cash at beginning of period	18,778
Cash at end of period	$20,555
Supplemental disclosures of cash flow information:	
Interest paid	$ 47
Income taxes paid (refunded)	$(6,809)
Return of common stock previously issued to employee for note receivable	$ --

See accompanying notes to condensed consolidated financial statements.

5

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands)

Note 1 - Business Organization and Basis of Presentation

Cotelligent, Inc. ("Cotelligent" or the "Company"), a Delaware corporation, provides software consulting services to businesses with complex information technology ("IT") operations and also provides maintenance, support and contract services on software products it licenses. These financial statements include the accounts of Cotelligent, Inc. and its subsidiaries.

During the fiscal year ended March 31, 2000, the Company was organized in two practice groups, Technology Solutions and Professional Services (also known as its IT staff augmentation business), and operated across the United States along with international consultant recruiting offices in Brazil and the Philippines. Prior to March 31, 2000, the Company entered into a plan to divest its IT staff augmentation business. Accordingly, the accompanying consolidated financial statements and related footnotes have been prepared to present as discontinued operations the Company's IT staff augmentation business for all periods presented.

The Company has suffered significant operating losses as well as negative operating cash flows in the last three fiscal periods and continues to be subject to certain risks common to companies in this industry. These uncertainties include the availability of financing, the retention of and dependence on key individuals, the effects of intense competition, the ability to develop and successfully market new product and service offerings, and the ability to streamline operations and increase revenues. There can be no assurance the Company will be profitable in the future.

Note 2 - Restatement

The Company has restated its consolidated balance sheets as of December 31, 2001 and 2000 and its consolidated statements of operations, stockholders' equity and cash flows for the year ended December 31, 2001 and the nine months ended December 31, 2000. Additionally, the Company restated the quarterly financial data for each three month period within the year ended December 31, 2001 and nine months ended December 31, 2000. The restated consolidated financial statements and quarterly financial data, along with a description of the items causing the restatement, appear in the Company's Amendment No. 3 to Annual Report on Form 10-K/A for the year ended December 31, 2001, filed with the Securities and Exchange Commission on December 9, 2002.

6

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands)

The following tables present the changes that have been made to the condensed consolidated statements of operations and cash flows for the three and six months ended June 30, 2001:

	As Previously Reported	Restated
	Three Months Ended June 30, 2001	
Consolidated Statement of Operations:		
Revenues	$ 12,460	$ 12,460
Cost of services	9,443	9,443
Gross profit	3,017	3,017
Research and development costs	--	209
Selling, general and administrative expenses	9,326	9,533

Operating loss	(6,309)	(6,725)
Other income (expense):		
Interest expense	(1)	(30)
Interest income	396	273
Other	(103)	(294)
Total other income (expense)	292	(51)
Loss from continuing operations before income taxes	(6,017)	(6,776)
Benefit for income taxes	--	--
Loss from continuing operations	(6,017)	(6,776)
Operating income (loss) from discontinued operations	23	--
Gain on sale of discontinued operations	--	1
Income (loss) from discontinued operations	23	1
Net loss	$ (5,994)	$ (6,775)
Earnings (loss) per share:		
Basic -		
Income (loss) from continuing operations	$ (0.39)	$ (0.44)
Income (loss) from discontinued operations	--	--
Net income (loss)	$ (0.39)	$ (0.44)
Diluted -		
Income (loss) from continuing operations	$ (0.39)	$ (0.44)
Income (loss) from discontinued operations	--	--
Net income (loss)	$ (0.39)	$ (0.44)
Weighted average number of shares outstanding:		
Basic	15,273,716	15,273,716
Diluted	15,273,716	15,273,716

7

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands)

	As Previously Reported	Restated
	Six Months Ended June 30, 2001	
Revenues	$ 29,056	$ 29,056
Cost of services	21,299	21,299
Gross profit	7,757	7,757
Research and development costs	--	315
Selling, general and administrative expenses	18,861	19,259

Operating loss	(11,104)	(11,817)
Other income (expense):		
Interest expense	(2)	(60)
Interest income	881	635
Other	(57)	(439)
Total other income (expense)	822	136
Income (loss) from continuing operations before income taxes	(10,282)	(11,681)
Benefit for income taxes	--	3,454
Income (loss) from continuing operations	(10,282)	(8,227)
Operating income (loss) from discontinued operations	17	--
Gain (loss) on sale of discontinued operations	--	(119)
Income (loss) from discontinued operations	17	(119)
Net income (loss)	$ (10,265)	$ (8,346)
Earnings (loss) per share:		
Basic -		
Income (loss) from continuing operations	$ (0.67)	$ (0.54)
Income (loss) from discontinued operations	--	(0.01)
Net income (loss)	$ (0.67)	$ (0.55)
Diluted -		
Income (loss) from continuing operations	$ (0.67)	$ (0.54)
Income (loss) from discontinued operations	--	(0.01)
Net income (loss)	$ (0.67)	$ (0.55)
Weighted average number of shares outstanding:		
Basic	15,316,705	15,311,180
Diluted	15,316,705	15,311,180

	As Previously Reported	Restated
	Six Months Ended June 30, 2001	
Consolidated Statement of Cash Flows:		
Net cash used in operating activities	$(3,849)	$(3,957)
Net cash used in investing activities	(559)	(32)
Net cash used in financing activities	(445)	(201)
Cash provided by discontinued operations	684	21

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands)

Note 3 - Summary of Significant Accounting Policies

The accompanying interim financial statements do not include all disclosures included in the financial statements in Cotelligent's Amendment No. 3 to Annual Report on Form 10-K/A for the year ended December 31, 2001 ("Form 10-K/A"), and therefore these financial statements should be read in conjunction with the financial statements included in Cotelligent's Form 10-K/A.

In the opinion of management, the interim financial statements filed as part of this Quarterly Report on Form 10-Q reflect all adjustments necessary for a fair presentation of the financial position and the results of operations and of cash flows for the interim periods presented. Certain balances of the prior year have been reclassified to conform to the current presentation.

Note 4 - Changes in Stockholders' Equity

	Common Stock		Additional Paid-In Capital	Notes Receivable From Stockholders	Accum. Deficit	T
	Shares	Amount				S
Balance at December 31, 2001...	15,514,757	$155	$86,662	$(6,193)	$(55,160)	64
Issuance of common stock.......	31,197	--	4	--	--	
Net income....................	--	--	--	--	674	
Balance at June 30, 2002.......	15,545,954	$155	$86,666	$(6,193)	$(54,486)	64

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands)

Note 5 - Discontinued Operations

On June 30, 2000, the Company sold the majority of its IT staff augmentation business and on July 14, 2000 and October 31, 2000 sold other components of the IT staff augmentation business. During the quarter ended June 30, 2001, the Company held one remaining component of its discontinued operations. During the fourth quarter of fiscal 2001, the Company abandoned its plan to divest of this operation and consequently closed this business.

The following financial data reflects a summary of operating results for the Company's discontinued operations for the three and six months ended June 30, 2001.

Summary of Operating Results of Discontinued Operations:

	Three Months Ended	Six Months Ended
	June 30, 2001	June 30, 2001

Revenues	$1,426	$3,503
Cost of services	1,055	2,727
Gross profit	371	776
Selling, general and administrative expenses	370	895
Operating income (loss)	1	(119)
Other income (expense)	--	--
Operating income (loss) before provision for taxes	1	(119)
Provision for income taxes	--	--
Operating income (loss)	1	(119)
Reclassification to gain (loss) on sale of discontinued operations	(1)	119
Operating income from discontinued operations	$ --	$ --

Gain on Sale of Discontinued Operations in 2002:

The gain on the sale of discontinued operations for the three and six months ended June 30, 2002 is the result of recoveries of trade accounts receivable in 2002 previously written off as bad debt.

Note 6 - Income Taxes

On March 9, 2002, Congress approved the Job Creation and Worker Assistance Act of 2002 allowing net operating losses for the Company's fiscal tax year ending March 31, 2002 to be carried back five years. In accordance with SFAS No. 109, the effect of this change in tax law was reflected in the March 31, 2002 financial statements as changes in tax law must be reflected in the period of enactment. Consequently, the Company recorded a $7,496 tax benefit during the six months ended June 30, 2002, which reflects the release of a valuation allowance against a deferred tax asset previously written down to zero due to the uncertainty of its realization. The Company received a $7,496 refund of taxes on August 10, 2002.

Note 7 - Weighted Average Number of Shares Outstanding

	Three Months Ended June 30,		Six
	2002	2001	2002
Basic weighted average number of shares outstanding	14,901,054	15,273,716	14,895,
Effect of stock options issued to employees and directors	--	--	2,491,
Diluted weighted average number of shares outstanding	14,901,054	15,273,716	17,387,

Options to purchase 4,646,094 and 1,956,386 shares of common stock were outstanding at June 30, 2002 and 2001, respectively, but were not included in EPS for the three months ended June 30, 2002 and 2001 because the Company had a loss from continuing operations making the options antidilutive. Options to purchase 422,402 shares of common stock were outstanding for the six months ended June 30, 2002 but were not included in the computation of diluted EPS because the options' exercise price was greater than the average market price of the common shares. Options to purchase 1,956,386 shares of common stock were outstanding at June 30, 2001, but were not included in EPS for the six months ended June 30, 2001 because the Company had a loss from continuing operations making the options antidilutive.

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

Except for statements of historical fact contained herein, any statements contained in this report may be deemed to be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. For example, words such as "may," "will," "should," "estimates," "predicts," "potential," "continue," "strategy," "believes," "anticipates," "plans," "expects," "intends" and similar expressions are intended to identify forward-looking statements. All such forward-looking statements are based upon current expectations that involve risks and uncertainties. Cotelligent's actual results and the timing of certain events may differ significantly from the results discussed in the forward-looking statements. Factors that might cause or contribute to such a discrepancy include, but are not limited to, those discussed under "Risk Factors" in Cotelligent's Annual Report on Form 10-K for the fiscal year ended December 31, 2001, other filings made with the Securities and Exchange Commission and Cotelligent's press release announcing earnings for the quarter ended March 31, 2002, which was issued on April 30, 2002. The following discussion is qualified in its entirety by, and should be read in conjunction with, the more detailed information set forth in our financial statements and the notes thereto included elsewhere in this filing. All forward-looking statements included in this report are based upon information available to Cotelligent as of the date thereof, and Cotelligent assumes no obligation to update any of such forward-looking statements.

OVERVIEW

Cotelligent provides software consulting services to businesses with complex information technology ("IT") operations and also provides maintenance, support and contract services on software products it licenses. These activities are provided under time and materials billing arrangements or on a fixed-fee basis. For time and materials billing arrangements, revenues are recorded as work is performed. Revenues are directly related to the total number of hours billed to clients and the associated hourly billing rates. Hourly billing rates are established for each service provided and are a function of the type of work performed and the related skill level of the consultant. For fixed-fee arrangements, work is performed in line with established deliverables and revenue is calculated on a percentage of completion basis. In addition, the Company has developed complete mobile workforce management solutions for industries that have medium to large transient sales, field or delivery personnel. A component of these solutions may be software that has been developed by the Company. Revenues earned for software license sales and service contracts are recorded based on the provisions of AICPA SOP 97-2, "Software Revenue Recognition," which shares the basic criteria of SAB No. 101.

The Company's principal costs are professional compensation directly related to the performance of services and related expenses. Gross profits (revenues after professional compensation and related expenses) are primarily a function of hours billed to clients per professional employee or consultant, hourly billing rates of those employees or consultants and employee or consultant compensation relative to those billing rates. Gross profits can be adversely impacted if services provided cannot be billed, if the Company is not effective in managing its service activities, if fixed-fee engagements are not properly priced, if consultant cost increases exceed bill rate increases or if there are high levels of unutilized time (work activities not chargeable to clients or unrelated to client services) of full-time salaried service professional employees.

Operating income can be adversely impacted by increased administrative staff compensation and expenses related to streamlining or expanding the Company's business, which may be incurred before revenues or economies of scale are generated from such investment. Solution development activities require a higher level of selling, general and administrative activities as well as investment in research and development activities.

As a service and software organization, the Company responds to service demands from its clients. Accordingly, the Company has limited control over the timing and circumstances under which its services are provided. Therefore, the Company can experience volatility in its operating results from quarter to quarter. The operating results for any quarter are not necessarily indicative of the results for any future period.

RESTATEMENT

The Company has restated the condensed consolidated statements of operations and cash flows for the three and six months ended June 30, 2001 included in this Quarterly Report on Form 10-Q. For additional information regarding the restatement, please refer to Note 2 to the condensed consolidated financial statements included in Item 1.

CONSOLIDATED RESULTS OF OPERATIONS
(In thousands)

Three Months Ended June 30, 2002 Compared to Three Months Ended June 30, 2001

Revenues

Revenues decreased $8,158, or 65%, to $4,302 in the three months ended June 30, 2002, from $12,460 in the three months ended June 30, 2001. The decrease was due to a general reduction in demand for its services due to softening in the market coupled with a shift away from general IT consulting services towards offering mobile workforce management and Web services solutions.

Gross Profit

Gross profit decreased $1,390, or 46%, to $1,627 in the three months ended June 30, 2002, from $3,017 in the three months ended June 30, 2001. The decrease was due to lower revenues following a general reduction in demand for its services due to softening in the market coupled with a shift away from general IT consulting services towards offering mobile workforce management and Web services solutions. The gross profit margin increased to 38% from 24% due to better pricing, a mix shift to higher margin projects, caused in part by the end of some long-term, lower margin, legacy system development engagements and an increase in utilization of billable staff.

Research and Development Costs

Research and development costs were $599 for the three months ended June 30, 2002 compared to $209 for the three months ended June 30, 2001. The Company has a dedicated team of people solely focused on research and development activities associated with mobile workforce management and Web services solutions. The increase of $390 results from research and development costs related to the development of a software solution for a prospective business partner.

Selling, General and Administrative Expenses

Selling, general and administrative expenses decreased $4,525, or 47%, to $5,008 in the three months ended June 30, 2002 from $9,533 in the three months ended June 30, 2001. The decrease was primarily due to reductions in operating staff and associated spending in order to streamline operations in line with revenues, offset by increased spending in the June 2002 quarter in legal and proxy solicitation costs in connection with the 2002 Annual Meeting of Stockholders.

Other Income (Expense)

Other income (expense) primarily consists of interest income, interest expense and losses on an investment in an alliance partner accounted for under the equity method of accounting. Interest income net of interest expense was $61 for the three months ended June 30, 2002 compared to net interest income of $243 for the three months ended June 30, 2001. The decrease in interest income was due to lower cash and cash equivalents on hand during the three months ended June 30, 2002 and lower interest rates available on cash equivalents. The equity method losses on the investment in an alliance partner also decreased between the periods.

Benefit for Income Taxes

The Company recognized a tax benefit of $96 which represented a true-up of the estimated tax benefit recognized in the quarter ended March 31, 2002. The benefit was based on the carryback claim actually filed in the quarter ended June 30, 2002.

Gain on Sale from Discontinued Operations

Discontinued operations is comprised of the Company's IT staff augmentation business. During the quarter ended June 30, 2001, the Company held one remaining component in discontinued operations. During the fourth quarter fiscal 2001, the Company abandoned its plan to divest of this operation and consequently closed the business.

The gain from the sale of discontinued operations for the three months ended June 30, 2002 of $82 was the result of cash collected on trade accounts receivable written off to bad debt expense in prior years.

CONSOLIDATED RESULTS OF OPERATIONS
(In thousands)

Six Months Ended June 30, 2002 Compared to Six Months Ended June 30, 2001

Revenues

Revenues decreased $18,881, or 65%, to $10,175 in the six months ended June 30, 2002 from $29,056 in the six months ended June 30, 2001. The decrease was due to a general reduction in demand for its services due to softening in the market, coupled with a shift away from general IT consulting services towards offering mobile workforce management and Web services solutions.

Gross Profit

Gross profit decreased $4,025, or 52%, to $3,732 in the six months ended June 30, 2002 from $7,757 in the six months ended June 30, 2001. The decrease was due to a general reduction in demand for its services due to softening in the market, coupled with a shift away from general IT consulting services towards offering mobile workforce management and Web services solutions. The gross profit margin increased to 37% from 27%, due to better pricing, a mix shift to higher margin projects, caused in part by the end of some long-term, lower margin, legacy system development engagements and an increase in utilization of billable staff.

Research and Development Costs

Research and development costs were $818 for the six months ended June 30, 2002 compared to $315 for the six months ended June 30, 2001. The Company has created a dedicated team of people solely focused on research and development activities associated with mobile workforce management and Web services solutions and has increased the number of people assigned to this area in 2002. Also, the Company incurred $400 of research and development costs related to the development of a software solution for a prospective business partner during the three months ended March 31, 2002.

Selling, General and Administrative Expenses

Selling, general and administrative expenses decreased $9,638, or 50%, to $9,621 in the six months ended June 30, 2002 from $19,259 in the six months ended June 30, 2001. The decrease was primarily due to the reductions in operating staff and associated spending in order to streamline operations in line with revenue, offset by increased spending in the June 2002 quarter in legal and proxy solicitation costs in connection with the 2002 Annual Meeting of Stockholders.

Other Income (Expense)

Other income (expense) primarily consists of interest income, interest expense and losses on an investment in an alliance partner accounted for under the equity method of accounting. Interest income net of interest expense was $90 for the six months ended June 30, 2002 compared to net interest income of $575 for the six months ended June 30, 2001. The decrease in interest income was due to lower cash and cash equivalents on hand during the six months ended June 30, 2002 and lower interest rates available on cash equivalents. The equity method losses on the investment in an alliance partner also decreased between the periods.

Benefit for Income Taxes

The income tax benefit of $7,496 for the six months ended June 30, 2002 was the result of the Job Creation and Worker Assistance Act of 2002, approved by Congress on March 9, 2002, allowing net operating losses for the Company's fiscal tax year ending March 31, 2002 to be carried back five years. In accordance with SFAS No. 109, the effect of this change in tax law was reflected in the six months ended June 30, 2002 financial statements as changes in tax law must be reflected in the period of enactment. The Company recorded a further income tax benefit of $3,454 for the six months ended June 30, 2001 due to the deduction of goodwill associated with an abandoned operating location.

Gain on Sale from Discontinued Operations

Discontinued operations was comprised of the Company's IT staff augmentation business. During the six months ended June 30, 2001, the Company held one remaining component in discontinued operations which resulted in a loss from discontinued operations of $119. During the fourth quarter of fiscal 2001, the Company abandoned its plan to divest this operation and consequently closed the business. The gain on sale of discontinued operations in the six months ended June 30, 2002 was the result of recovering trade accounts receivable written off in prior years.

LIQUIDITY AND CAPITAL RESOURCES
(In thousands)

The Company has financed itself principally through cash flows from operations, net proceeds from its public offerings, net proceeds from the sale of its IT staff augmentation business and tax refunds from the carry back of net operating losses.

The Company previously maintained a credit facility with a consortium of banks under which it borrowed to fund working capital needs. On June 30, 2000, the Company used a portion of the cash proceeds from the sale of its IT staff augmentation business to pay off all obligations under the credit facility and to pay existing earn-out obligations to sellers of an acquired business. Upon settlement of all obligations under the credit facility, the credit facility was terminated. Since June 30, 2000, the Company has not maintained a credit facility.

Cash provided by operating activities was $1,436 for the six months ended June 30, 2002, and the average cash balance during the quarter was $21,833. The Company's primary sources of liquidity for the Company going forward include the collection of accounts receivable and federal and state income tax refunds resulting from the carry-back of net operating losses. In addition, the Company continues to utilize the cash proceeds generated from the sales of its IT staff augmentation businesses. Total receivables were 72 days of quarterly revenues at June 30, 2002 and 74 days at December 31, 2001. In the first quarter of 2002, Congress approved the Job Creation and Worker Assistance Act of 2002 allowing fiscal tax year end March 31, 2002 net operating losses to be carried back five years. The effect of this change in tax law resulted in a $7,496 tax refund received by the Company on August 10, 2002. The Company's management believes that the remaining cash on hand will provide adequate cash to fund its anticipated cash working capital needs at least through next year.

The following table reflects our contractual cash obligations, excluding interest, due over the indicated periods.

	Payments Due by Period				
Contractual Cash Obligations:	Total	Less than 1 Year	1 to 3 Years	4 to 5 Years	After Year
Obligations due sellers of an acquired business	$ 578	$ 360	$ 218	$ --	$--
Operating leases	$5,439	$1,703	$3,279	$457	$--
Total contractual obligation	$6,017	$2,063	$3,497	$457	$--

RECENT ACCOUNTING PRONOUNCEMENTS

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. Examples of costs covered by the standard include lease termination costs and certain employee severance costs that are associated with a restructuring, discontinued operations, plant closing, or other exit or disposal activities. SFAS No. 146 is effective prospectively for exit or disposal activities initiated after December 31, 2002, with earlier adoption encouraged. As the provisions of SFAS No. 146 are required to be applied prospectively after the adoption date, we cannot determine the potential effects that adoption of SFAS No. 146 will have on our consolidated financial statements.

CRITICAL ACCOUNTING POLICIES

Allowance for Doubtful Accounts

The Company provides an allowance for potentially uncollectible accounts receivable under the provisions of SFAS No. 5, "Accounting for Contingencies," in the ordinary course of business. The allowance is derived as the result of periodic and thorough reviews of aged and known problem accounts during each quarter. In addition, the Company reserves for unknown issues in its receivables at the balance sheet date using a formula consistent from quarter to quarter. Management believes that its approach is appropriate to reserve for potentially uncollectible receivables. Should management have taken another approach to developing its reserve, the allowance for doubtful accounts may have been different than that reported.

Revenue Recognition

The Company accounts for time and materials revenue under the provisions of SAB 101, "Staff Accounting Bulletin No. 101: Revenue Recognition in Financial Statements", which requires revenue to be recorded when there is evidence of an agreement, a fixed or determinable fee, collectibility is reasonably assured, and delivery has occurred. Revenues include reimbursable expenses charged to and collected from clients. Revenues pursuant to fixed-fee contracts are generally recognized as services are rendered on

the percentage-of-completion method of accounting based on hours incurred to total estimated labor hours to complete. Revenues earned for software license sales and service contracts are recorded based on the provisions of AICPA SOP 97-2, "Software Revenue Recognition", which shares the basic criteria of SAB No. 101.

Restructuring Liabilities

As part of the Company's efforts to streamline its operations commensurate with its revenue base, the Company identified opportunities to reduce its cost structure by reducing headcount and closing certain operating facilities to conform to the Company's changing operating structure in June 1999, December 2000, and September 2001. These restructuring obligations were calculated using information known at the date of the respective accruals based on the provisions of EITF 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity." Management has adjusted these obligations over the payment periods of each restructuring plan as liabilities have been settled and payments have been made. Management periodically reviews the accuracy of the restructuring liabilities, and accounts for any necessary adjustments due to changes in estimates in the statement of operations as originally provided.

Accounting for Income Taxes

The Company accounts for income taxes under SFAS No. 109, "Accounting for Income Taxes." This pronouncement requires using an asset and liability approach to recognize deferred tax assets and liabilities for the tax consequences of temporary differences by applying enacted statutory tax rates to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. The Company has not given benefit to any deferred tax assets or net operating losses in the previous two fiscal years due to uncertainty of realizing these assets in future periods, except a) in the first quarter of 2001, the Company recognized an income tax benefit related to a net operating loss generated through March 31, 2001 that was carried back to early years and for which a refund of taxes was received and b) in the first quarter of 2002, Congress approved the Job Creation and Worker Assistance Act of 2002, allowing March 31, 2002 net operating losses to be carried back five years. Under SFAS No. 109, the effect of this change in tax law was reflected in the March 31, 2002 financial statements as changes in tax law must be reflected in the period of enactment. In addition, the financial statements have provided reserves for certain tax positions taken by the Company in the March 31, 1999, 2000 and 2001 tax returns based on enacted tax laws during those periods.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Cotelligent has invested its existing cash in highly liquid money market accounts and does not use derivative financial instruments, derivative commodity instruments or other market risk sensitive instruments, positions or transactions. Accordingly, the Company believes that it is not subject to any material risks arising from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices or other market changes that affect market risk sensitive instruments. Cotelligent's policy is to invest its cash in a manner that provides Cotelligent with the appropriate level of liquidity to enable it to meet its current obligations, primarily accounts payable, capital expenditures and payroll, recognizing that it does not currently have outside bank funding available.

Item 4. Controls and Procedures

There have not been any significant changes in the Company's internal controls or in other factors that could significantly affect these controls and there have been no corrective actions taken with regard to significant deficiencies and material weaknesses subsequent to the date of their evaluation.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

We are, from time to time, a party to litigation arising in the normal course of our business. We are not presently subject to any material litigation.

Item 2. Changes in Securities and Use of Proceeds

None

Item 3. Defaults upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

The Company solicited proxies for an annual meeting of stockholders held on June 11, 2002 at which one director was to be elected. The Board of Directors nominated Debra J. Richardson to serve as a director for a term expiring at the 2005 annual meeting of stockholders. The terms of directors James R. Lavelle and Anthony M. Frank continued after the annual meeting. Skiritai Capital LLC, a stockholder of the Company, solicited proxies in opposition to the Board's nominee for the purpose of electing its nominee, Russell Silvestri, as director.

On June 18, 2002, the independent inspector of elections certified the final results of the voting at Cotelligent's annual meeting held on June 11, 2002. Stockholders elected Debra J. Richardson and approved a non-binding stockholder proposal recommending that the Board of Directors redeem the rights issued and outstanding under the Company's shareholder rights plan. The final results are as follows:

1. Election of one director to serve for a three-year term expiring at the annual meeting in 2005.

For	
Debra J. Richardson	7,229,844
Russell Silvestri	3,127,647
Authority Withheld	1,389,804

2. Approve the adoption of a non-binding stockholder proposal recommending that the Board of Directors redeem the rights issued and outstanding under the Company's shareholder rights plan.

For	5,106,532
Against	4,145,605
Abstain	53,296
Broker Non-Vote	2,441,862

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

99.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

99.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K

Cotelligent, Inc. filed with the Securities and Exchange Commission on May 9, 2002, a current report on Form 8-K in connection with the adoption of Amended and Restated By-laws of Cotelligent, Inc and certain changes to Cotelligent Inc.'s Board of Directors.

Cotelligent, Inc. filed with the Securities and Exchange Commission on June 13, 2002, a current report Form 8-K regarding Amendment No. 1 to Rights Agreement, amending the Rights Agreement dated September 24, 1997, between Cotelligent, Inc. and BankBoston, N.A.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COTELLIGENT, INC.

Date: January 6, 2003

/s/ Curtis J. Parker

Curtis J. Parker
Executive Vice President,
Chief Financial Officer and Treasurer

Certifications Pursuant to Section 302
of the Sarbanes-Oxley Act of 2002

I, James R. Lavelle, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cotelligent, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report; and

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report.

Date: January 6, 2003

/s/ James R. Lavelle

James R. Lavelle
Chairman of the Board and Chief Executive Officer

Certifications Pursuant to Section 302
of the Sarbanes-Oxley Act of 2002

I, Curtis J. Parker, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cotelligent, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report; and

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report.

Date: January 6, 2003

/s/ Curtis J. Parker

Curtis J. Parker
Executive Vice President and Chief Financial Officer