

Edgar Filing: SmartPros Ltd. - Form 10QSB

SmartPros Ltd.
Form 10QSB
August 12, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2005

Commission File Number 001-32300

SMARTPROS LTD.

(Exact name of small business issuer as specified in its charter)

Delaware

13-4100476

(State or other jurisdiction
of incorporation or organization)

(I.R.S. Employer
Identification No.)

12 Skyline Drive, Hawthorne, New York 10532

(Address of principal executive office)

(914) 345-2620

(Issuer's telephone number, including area code)

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

Yes No

Number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: As of August 1, 2005, there were 5,085,340 shares of common stock outstanding.

Transitional Small Business Disclosure Format.

Yes No

SMARTPROS LTD.
FORM 10-QSB REPORT

June 30, 2005

TABLE OF CONTENTS

PAGE

Edgar Filing: SmartPros Ltd. - Form 10QSB

PART I - FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements (Unaudited)	
Balance Sheets - June 30, 2005 and December 31, 2004	3
Statements of Operations for the three- and six-month periods ended June 30, 2005 and 2004	4
Statements of Cash Flows for the six-month period ended June 30, 2005 and 2004	5
Notes to Interim Condensed Consolidated Financial Statements	6
Item 2. Management's Discussion and Analysis or Plan of Operation	8
Item 3. Controls and Procedures	17

PART II - OTHER INFORMATION

Item 1. Legal Proceedings	17
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	17
Item 3. Defaults Upon Senior Securities	18
Item 4. Submission of Matters to a Vote of Security Holders	18
Item 5. Other Information	18
Item 6. Exhibits	18

SIGNATURES	19
------------	----

FORWARD-LOOKING STATEMENTS

Certain statements made in this Quarterly Report on Form 10-QSB are "forward-looking statements" within the meaning of Section 21E of the Securities and Exchange Act of 1934 regarding the plans and objectives of management for future operations and market trends and expectations. Such statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The forward-looking statements included herein are based on current expectations that involve numerous risks and uncertainties. Our plans and objectives are based, in part, on assumptions involving the continued expansion of our business. Assumptions relating to the foregoing involve judgments with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Although we believe that our assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this report will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved. The terms "we", "our", "us", or any derivative thereof, as used herein refer to SmartPros Ltd., a Delaware corporation, and its predecessors.

Edgar Filing: SmartPros Ltd. - Form 10QSB

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SMARTPROS LTD. AND SUBSIDIARY CONDENSED CONSOLIDATED BALANCE SHEETS

	JUNE 30, 2005 (UNAUDITED)	DECEMBER 31, 2004
<hr/>		
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 3,228,463	\$ 1,756,991
Investment securities available-for-sale	3,750,000	5,000,000
Accounts receivable, net of allowance for doubtful accounts of \$71,000	1,095,864	985,259
Prepaid expenses and other current assets	176,116	175,270
	<hr/>	<hr/>
TOTAL CURRENT ASSETS	8,250,443	7,917,520
	<hr/>	<hr/>
Property and equipment, net	567,381	544,176
Goodwill	53,434	53,434
Other intangible, net	2,314,565	2,482,653
Other assets, including restricted cash of \$150,000	150,000	167,196
	<hr/>	<hr/>
TOTAL ASSETS	\$ 11,335,823	\$ 11,164,979
	<hr/> <hr/>	<hr/> <hr/>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 265,232	\$ 358,867
Accrued expenses	355,488	373,993
Current portion of capital lease and equipment financing obligations	44,491	56,119
Deferred revenue	3,631,449	3,741,466
	<hr/>	<hr/>
TOTAL CURRENT LIABILITIES	4,296,660	4,530,445
	<hr/>	<hr/>
Long-Term Liabilities:		
Capital lease and equipment financing obligations	43,094	64,020
Other liabilities	162,729	164,907
	<hr/>	<hr/>
TOTAL LONG-TERM LIABILITIES	205,823	228,927
	<hr/>	<hr/>
Commitments and Contingencies		
Stockholders' Equity:		
Convertible preferred stock, \$.001 par value, authorized 1,000,000 shares, no shares issued and outstanding	--	--
Common stock, \$.0001 par value, authorized 30,000,000 shares, 5,143,346 issued and 5,085,340 outstanding at June 30, 2005;		

Edgar Filing: SmartPros Ltd. - Form 10QSB

5,140,545 issued and 5,082,539 outstanding at December 31, 2004	514	514
Common stock in treasury, at cost - 58,006 shares	(220,000)	(220,000)
Additional paid-in capital	16,413,517	16,407,495
Accumulated (deficit)	(9,064,691)	(9,454,902)
	-----	-----
	7,129,340	6,733,107
Deferred compensation	(96,000)	(127,500)
Note receivable from stockholder	(200,000)	(200,000)
	-----	-----
TOTAL STOCKHOLDERS' EQUITY	6,833,340	6,405,607
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 11,335,823	\$ 11,164,979
	=====	=====

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3

SMARTPROS LTD. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	SIX MONTHS ENDED JUNE 30,		THREE
	2005	2004	2005
	-----	-----	-----
Net Revenues	\$ 5,555,992	\$ 4,592,296	\$ 2,707,04
Cost of Revenues	2,240,944	1,686,988	1,158,23
	-----	-----	-----
Gross Profit	3,315,048	2,905,308	1,548,80
	-----	-----	-----
Operating Expenses:			
Selling, general and administrative	2,710,830	2,355,409	1,275,67
Depreciation and amortization	285,899	346,226	144,65
	-----	-----	-----
	2,996,729	2,701,635	1,420,32
	-----	-----	-----
Operating Income	318,319	203,673	128,48
	-----	-----	-----
Other Income (Expense):			
Interest income	77,022	7,318	47,46
Interest expense	(5,130)	(36,775)	(1,82
	-----	-----	-----
	71,892	(29,457)	45,63
	-----	-----	-----
Income before provision for income taxes	390,211	174,216	174,11
Provision for Income Taxes	--	--	--
	-----	-----	-----
Net Income	\$ 390,211	\$ 174,216	\$ 174,11
	=====	=====	=====

Edgar Filing: SmartPros Ltd. - Form 10QSB

Net Income Per Common Share:			
Basic net income per common share	\$.08	\$.07	\$.0
	=====	=====	=====
Diluted net income per common share	\$.08	\$.05	\$.0
	=====	=====	=====
Weighted Average Number of Shares Outstanding			
Basic	5,083,576	2,580,478	5,084,60
	=====	=====	=====
Diluted	5,118,075	3,244,262	5,118,84
	=====	=====	=====

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

4

SMARTPROS LTD. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	SIX MONTHS ENDED JUNE 30,	
	2005	2004
	-----	-----
Cash Flows from Operating Activities:		
Net income	\$ 390,211	\$ 174,216
	-----	-----
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	285,899	346,226
Reduction in deferred compensation	31,500	--
Changes in operating assets and liabilities:		
(Increase) decrease in operating assets:		
Accounts receivable	(110,605)	(95,306)
Prepaid expenses and other current assets	(845)	(313,073)
Other assets	17,196	--
(Decrease) increase in operating liabilities:		
Accounts payable and accrued expenses	(112,140)	(158,536)
Deferred revenue	(110,017)	500,734
Other liabilities	(2,178)	--
	-----	-----
Total adjustments	(1,190)	280,045
	-----	-----
Net Cash Provided by Operating Activities	389,021	454,261
	-----	-----
Cash Flows from Investing Activities:		
Reduction in investment securities available-for-sale	1,250,000	--
Acquisition of property and equipment	(141,017)	(37,062)
	-----	-----
Net Cash Provided by (Used in) Investing Activities	1,108,983	(37,062)
	-----	-----

Edgar Filing: SmartPros Ltd. - Form 10QSB

Cash Flows from Financing Activities:		
Proceeds from exercise of stock option	6,022	--
Payments on note payable - treasury stock	--	(36,000)
Proceeds from issuance of long-term debt	--	10,135
Payments on long-term debt	--	(136,002)
Payments under capital lease obligations	(32,554)	(43,318)
	-----	-----
Net Cash Used in Financing Activities	(26,532)	(205,185)
	-----	-----
Net Increase in Cash and Cash Equivalents	1,471,472	212,014
Cash and Cash Equivalents, beginning of period	1,756,991	546,993
	-----	-----
Cash and Cash Equivalents, end of period	\$ 3,228,463	\$ 759,007
	=====	=====
Supplemental Disclosure:		
Cash paid for interest	\$ 5,130	\$ 36,775
	=====	=====
Supplemental Disclosure of Non Cash Investing and Financing Activities:		
Equipment purchased under capital leases	\$ --	\$ 10,135
	=====	=====

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

5

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of SmartPros Ltd. ("SmartPros" or the "Company"), included herein have been prepared by the Company in accordance with generally accepted accounting principles for interim financial information and with instructions to Form 10-QSB. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. However, in the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2004 and the notes thereto included in the Company's Annual Report on Form 10-KSB filed with the United States Securities and Exchange Commission on March 25, 2005. Results of consolidated operations for the interim periods are not necessarily indicative of the operating results to be attained for the entire fiscal year. The unaudited condensed consolidated financial statements herein include the accounts of the Company and its wholly owned subsidiary, Working Values, Ltd. All material inter-company accounts and transactions have been eliminated.

NOTE 2. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company, a Delaware corporation, was organized in 1981 as Center for Video Education, Inc. for the purpose of producing educational videos primarily directed to the accounting profession. SmartPros' primary products today are

Edgar Filing: SmartPros Ltd. - Form 10QSB

periodic video and Internet subscription services directed to corporate accountants, financial managers and accountants in public practice. In addition, the Company also produces a series of continuing education courses directed to the engineering profession as well as a series of courses designed for candidates for the professional engineering exam. Through its Working Values subsidiary, the Company also develops various programs on governance, compliance and ethics for corporations. SmartPros also produces custom videos and rents out its studios. SmartPros is located in Hawthorne, New York, where it maintains its corporate offices, new media lab, video production studios and tape duplication facilities. While the Company's management monitors the revenue streams of the various products and services, operations are managed and financial performance is evaluated on a company wide basis. Accordingly, all of the Company's operations are considered by management to be aggregated in one reportable segment.

USE OF ESTIMATES

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 the 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.

REVENUE RECOGNITION

The Company recognizes revenues from its subscription services as earned. Video subscriptions are generally billed on an annual basis, while on-line subscriptions are paid by credit card at point of sale. Both of these types of sales are deferred at the time of billing or payment and amortized into revenue on a monthly basis over the term of the subscription, which is generally one year. Engineering products are non-subscription based and revenue is recognized upon shipment or, in the case of on-line sales, payment. Revenues from non-subscription services provided to customers, such as website design, video production, consulting services and custom projects are generally recognized on a proportional performance basis where sufficient information relating to project status and other supporting documentation is available. The contracts may have different billing arrangements resulting in either unbilled or deferred revenue. The Company obtains either signed agreements or purchase orders from its non-subscription customers outlining the terms and conditions of the sale or service to be provided. Otherwise, such services are recognized as revenues after completion and delivery to the customer. Duplication and related services are generally recognized upon shipment or, if later, when the Company's obligations are complete and realization of receivable amounts is assured.

6

NOTE 2. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

CAPITALIZED COURSE COSTS

Capitalized course costs include the direct cost of internally developing proprietary educational products and materials that have extended useful lives. Amortization of these capitalized course costs commences with the realization of course revenues. The amortization period is three years. Other course costs incurred in connection with any of the Company's monthly subscription products or custom work are charged to expense as incurred. Included in other intangible assets at June 30, 2005 are capitalized course costs of \$204,177, net of accumulated amortization of \$90,657.

Edgar Filing: SmartPros Ltd. - Form 10QSB

DEFERRED REVENUE

Deferred revenue related to subscription services represents the portion of unearned subscription revenue, which is amortized on a monthly, straight-line basis, as earned. Deferred revenue related to website design and video production services represents that portion of amounts billed by the Company, or cash collected by the Company, for which services have not yet been provided or earned in accordance with the Company's revenue recognition policy.

CAPITAL STOCK

On September 10, 2004, the Company filed an amendment to its Certificate of Incorporation, effecting a reverse stock split in which each issued share of its Common Stock was converted into 0.5169925 new shares. The financial statements reflect this reverse split.

EARNINGS (LOSS) PER SHARE

Basic earnings or loss per common share is net income or loss, as the case may be, divided by the weighted average number of common shares outstanding during the year. Basic earnings or loss per share exclude any dilutive effects of options, warrants and convertible securities. Diluted earnings per common share include the dilutive effect of shares of Common Stock issuable under stock options, warrants and the Company's Series A Convertible Preferred Stock. Diluted earnings per share are computed using the weighted average number of Common Stock and Common Stock equivalent shares outstanding during the period. Common Stock equivalent shares of 34,242 and 663,784 for the six- and three-month periods ended June 30, 2005 and 2004 respectively, include the Company's stock options and warrants that are dilutive.

STOCK-BASED COMPENSATION

Employee compensation expense under stock options is reported using the intrinsic value method. No stock-based compensation cost is reflected in net income, as all options granted had an exercise price equal to or greater than the market price of the underlying Common Stock at date of grant.

The following table illustrates the effect on net earnings per share if expense was measured using the fair value recognition provisions of FASB Statement No. 123 "Accounting for Stock-Based Compensation":

7

NOTE 2. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS EN JUNE 30,	
	2005	2004	2005	
Net income as reported	\$ 174,119	\$ 181,576	\$ 390,211	\$
Add: Stock-based employee compensation expense included in reported net income (loss), net of related tax effects	--	--	--	

Edgar Filing: SmartPros Ltd. - Form 10QSB

Deduct: Stock-based compensation expense determined under fair value-based method	(7,606)	(39,038)	(15,212)	
	-----	-----	-----	-----
Pro forma net income	\$ 166,513	\$ 142,538	\$ 374,999	\$
	=====	=====	=====	=====
Basic earnings per share, as reported	\$.03	\$.07	\$.08	\$
	=====	=====	=====	=====
Diluted earnings per share, as reported	\$.03	\$.06	.08	\$
	=====	=====	=====	=====
Pro forma basic earnings per share	\$.03	\$.05	.07	\$
	=====	=====	=====	=====
Pro forma diluted earnings per share	\$.03	\$.04	.07	\$
	=====	=====	=====	=====

The fair value of options granted in 2004 were estimated on the date of grant using the Black-Scholes Option Pricing model with an average assumed risk-free interest rate of 4.0%, an average expected life of 10 years, an expected volatility of close to zero and the assumption that no dividends will be paid. The weighted average fair value per option of options granted in 2004 was \$1.40. In October 2004, subsequent to the Company's initial public offering, the Company granted 22,925 options to employees at an exercise price of \$4.27. On May 10, 2005 the Compensation Committee awarded a grant of 10,000 options to the Chairman of the Audit Committee of which 2,500 vested immediately and 2,500 will vest on each May 10, 2006 - 2008. The options have an exercise price of \$4.00 each. In April 2005, an option to purchase 2,801 shares was exercised at a price of \$2.15 per share.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS

THE FOLLOWING DISCUSSION OF OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS SHOULD BE READ IN CONJUNCTION WITH THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND RELATED NOTES INCLUDED ELSEWHERE IN THIS REPORT. CERTAIN STATEMENTS IN THIS DISCUSSION AND ELSEWHERE IN THIS REPORT CONSTITUTE FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF SECTION 21E OF THE SECURITIES AND EXCHANGE ACT OF 1934. SEE THE "FORWARD LOOKING STATEMENT" IMMEDIATELY FOLLOWING THE TABLE OF CONTENTS. BECAUSE THIS DISCUSSION INVOLVES RISK AND UNCERTAINTIES, OUR ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE ANTICIPATED IN THESE FORWARD-LOOKING STATEMENTS.

We provide learning solutions for accounting/finance and engineering professionals, as well as ethics and compliance training for the general corporate community. We offer "off-the-shelf" courses and custom designed programs with delivery methods suited to the specific needs of our clients. Our customers include approximately half of the Fortune 500 companies and a large number of midsize and small companies.

Our learning solutions for professionals are designed to meet the initial and ongoing licensing and continuing professional education requirements imposed by state licensing agencies and professional standards organizations. Most of the courses in our accounting/finance library are designed to meet these standards and adhere to the requirements of all state boards of accountancy as well as those of the American Institute of Certified Public Accountants, Institute of Management Accountants, Institute of Internal Auditors, the Association of Finance Professionals, and the Association of Government

Edgar Filing: SmartPros Ltd. - Form 10QSB

Accountants. In the engineering area, most of our courses have been approved for continuing professional

8

development credit by one or more organizations, including the American Society of Civil Engineers, the National Society of Professional Engineers, the American Council of Engineering Companies, the American Society of Mechanical Engineers and the Project Management Institute. Our corporate ethics and compliance training programs are designed to align corporate behavior with applicable laws and regulations, as well as generally accepted codes of conduct. So, for example, our programs may deal with issues prompted by the Sarbanes-Oxley Act of 2002 and the U.S. Federal Sentencing Guidelines, as well as laws addressing workplace misconduct such as harassment.

Our products are available in one or more of the following formats: print, videotapes and digital. Digital format can be delivered on CD-ROM, DVD or over the Internet. The Internet has become our fastest growing delivery channel, attracting new and existing subscribers. This has had a positive effect on our revenue as well as our gross margins since online sales eliminate the cost for materials, i.e., videotapes, packaging and shipping.

We believe that our learning solutions effectively address the needs of professionals and companies seeking comprehensive learning resources for themselves and their employees. Our solutions are flexible, cost-efficient and easy to use. They alleviate many of the inefficiencies associated with traditional classroom training, such as travel costs, scheduling difficulties and opportunity costs. In addition, we also offer our clients a learning content management system, which allows the professionals and their employers to track usage and performance.

Accounting/finance continuing professional education was our original market. This market covers corporate accountants and financial managers as well as accountants in public practice. Initially, our accounting/finance programs were delivered on videotape. In 1998, we recognized that, to remain competitive, we would have to make our products available in digital format for distribution over the Internet and corporate intranets. Towards that end, we hired information technology professionals to build a new media department that, among other things, would convert our programs to digital format for online delivery and who would oversee the development of a learning content management system.

To take advantage of financing opportunities that were then available to technology companies, we were advised to pursue an acquisition strategy that focused on building revenues and diversifying into new markets. Based on assurances we received from a specific financing source, we identified several viable acquisition targets, including Virtual Education Corporation, or VEC, a provider of license preparation and continuing professional development programs for engineers. However, the dynamics of the capital markets changed and our financing source was unable to raise any funds. At that point, we had already consummated our acquisition of VEC.

The acquisition of VEC put a tremendous strain on our internal capital resources. Although our accounting division continued to grow and generate operating profits, overall we began losing money. In the four-year period beginning in 2000 and ending in 2003 we generated over \$10 million of losses. In 2001, we hired a new chief executive officer, Allen S. Greene, who had been the chief operating officer of a publicly traded specialty finance company. Mr. Greene successfully refocused on our core competencies, cut overhead, substantially reduced debt and raised additional equity capital. In 2004, we recorded our first annual profit since 1999 and completed our initial public

Edgar Filing: SmartPros Ltd. - Form 10QSB

offering.

Since 2001, we have successfully completed two key acquisitions. First, in May 2001, we acquired substantially all of the assets of Pro2Net. In so doing, we acquired a library of "how to" programs, a functional learning content management system that we could market with our programs, customer lists, trade names and computer hardware. As a result, we were able to terminate a contract with a third party to develop a learning content management system, saving us approximately \$2 million in development costs. Our ability to provide the value-added services represented by the learning management system is, we believe, key to our recent revenue growth and future success.

Second, in April 2003, we acquired a library of custom-designed integrity-based courses and other assets from Working Values Group Ltd., a company that specialized in building custom-designed learning solutions for the general corporate community using traditional and alternative instructional techniques. As part of the transaction, we also hired the development team from Working Values Group. With the increased focus on corporate governance and ethics and the passage of the Sarbanes-Oxley Act of 2002 along with new rules and regulations adopted by the national stock exchanges and markets, we believe that there is a significant growth opportunity in supplying training that addresses corporate culture as a significant risk factor.

9

The aggregate purchase price for the Pro2Net and Working Values Group assets was \$1.1 million in cash, stock (based on the value at the time of the acquisition) and assumption of liabilities. In comparison, the sellers of these assets had collectively raised more than \$30 million to develop these assets and fund their operations.

We measure our operations using both financial and other metrics. The financial metrics include revenues, gross margins, operating expenses and income from continuing operations. Other key metrics include (i) revenues by sales source, i.e., accounting/finance, engineering, Working Values and video production and e-commerce. (ii) online sales, (iii) cash flows and (iv) EBITDA.

Some of the most significant trends affecting our business are the following:

- o The increasing recognition by professionals and corporations that they must continually improve their skills and those of their employees in order to remain competitive.
- o The plethora of new laws and regulations affecting the conduct of business and the relationship between a corporation and its employees.
- o The increased competition in today's economy for skilled employees and the recognition that effective training can be used to recruit and train employees.
- o The development and acceptance of the Internet as a delivery channel for the types of products and services we offer.

In October 2004 we successfully completed our initial public offering. The net proceeds to us from the offering were \$6.0 million of which we immediately used \$500,000 to repay our outstanding indebtedness other than capital leases. The remaining proceeds from the public offering are invested in either money markets or short-term interest bearing securities. We intend to use the remaining net proceeds, \$5.5 million, cash from operations and our publicly

Edgar Filing: SmartPros Ltd. - Form 10QSB

traded stock to execute our growth strategy, which contemplates acquiring other companies and businesses that provide learning solutions. We intend to focus on acquisitions that will allow us to increase the breadth and depth of our current product offerings, including the general corporate market for compliance, governance and ethics. We will also consider acquisitions that will give us access to new market segments such as insurance, health care and financial services. We prefer acquisitions that are accretive in the short term, as opposed to those that are dilutive, but ultimately the decision will be based on maximizing shareholder value rather than short-term profits. The size of the acquisitions will be determined, in part, by our size, the capital available to us and the liquidity and price of our stock. We may use debt to enhance or augment our ability to consummate larger transactions.

There are many risks involved with acquisitions. These risks include integrating the acquired business into our existing operations and corporate structure, retaining key employees and minimizing disruptions to our existing business. We cannot assure you that we will be able to identify appropriate acquisitions opportunities or negotiate reasonable terms or that any acquired business or assets will deliver the shareholder value that we anticipated at the outset. At the present time, we have no agreements or commitments for any acquisitions. We cannot assure you that we will successfully complete any acquisitions.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The discussion and analysis of our financial condition and results of operations is based on our condensed consolidated financial statements that have been prepared according to accounting principles generally accepted in the United States. In preparing these financial statements, we are required to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures of contingent assets and liabilities. We evaluate these estimates on an ongoing basis. We base these estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions. We consider the following accounting policies to be the most important to the portrayal of our financial condition.

10

REVENUES

Most of our revenue is in the form of subscription fees for one of our monthly accounting update programs or our course library. Other sources of revenue include direct sales of programs on a non-subscription basis, fees for various services, including website design, software development, tape duplication, video production, video conversion, course design and development, ongoing maintenance of our clients' online learning content management system and licensing fees. Subscriptions are billed on an annual basis, payable in advance and deferred at the time of billing. Sales made over the Internet are by credit card only. Renewals are usually sent out 60 days before the subscription period ends. We usually obtain either a signed agreement or purchase orders from our non-subscription customers outlining the terms and conditions of the sale or service to be provided. Larger transactions are usually dealt with by contract, the financial terms of which depend on the services being provided. The contracts may have different billing arrangements resulting in either unbilled or deferred revenue. Contracts for development and production services typically provide for a significant upfront payment and a series of payments based on deliverables specifically identified in the contract.

Edgar Filing: SmartPros Ltd. - Form 10QSB

Revenues from subscription services are recognized as earned, deferred at the time of billing or payment and amortized into revenue on a monthly basis over the term of the subscription. Engineering products are non-subscription based and revenue is recognized upon shipment of the product or, in the case of on-line sales, payment. Revenues from non-subscription services provided to customers, such as website design, video production, consulting services and custom projects, are generally recognized on a proportional performance basis where sufficient information relating to project status and other supporting documentation is available. Otherwise, these services are recognized as revenues after completion and delivery to the customer. Duplication and related services are generally recognized upon shipment or, if later, when our obligations are complete and realization of receivable amounts is assured. Working Values recognizes revenue on a proportional performance basis.

EQUIPMENT, INTANGIBLE ASSETS AND LEASEHOLD IMPROVEMENTS

Fixed and intangible assets are carried at cost less their respective accumulated depreciation/amortization and are depreciated/amortized using the straight-line method over their estimated useful lives, which range from three to ten years. Leasehold improvements are amortized over the lesser of their estimated lives or the life of the lease. Major expenditures for renewals and improvements are capitalized and amortized over their useful lives.

IMPAIRMENT OF LONG-LIVED ASSETS

We review long-lived assets and certain intangible assets annually for impairment whenever circumstances and situations change such that there is an indication that the carrying amounts may not be recovered.

STOCK-BASED COMPENSATION

We have adopted the disclosure only requirements of SFAS No. 123. As a result, no compensation costs are recognized for stock options granted to employees. Options and warrants granted to non-employees are recorded as an expense at the date of grant based on the then estimated fair value of the security in question.

RESULTS OF OPERATIONS

COMPARISON OF THREE MONTHS ENDED JUNE 30, 2005 AND 2004

The following table compares our statement of operations data for the three months ended June 30, 2005 and 2004. The trends suggested by this table may not be indicative of future operating results, which will depend on various factors including the relative mix of products sold (accounting/finance, engineering or corporate training) and the method of sale (video or online).

11

	THREE MONTHS ENDED JUNE 30,			
	2004		2005	
	AMOUNT	PERCENTAGE	AMOUNT	PERCENTAGE
Net revenues	\$ 2,373,945	100.0%	\$ 2,707,041	100.0%

Edgar Filing: SmartPros Ltd. - Form 10QSB

Cost of revenues	833,514	35.1%	1,158,235	42.8%

Gross profit	1,540,431	64.9%	1,548,806	57.2%

Selling, general and administrative	1,170,219	49.3%	1,275,670	47.1%
Depreciation and amortization	175,255	7.4%	144,656	5.3%

Total operating expenses	1,345,474	56.7%	1,420,236	52.4%

Operating income	194,957	8.2%	128,480	4.8%
Other (expense), net	(13,381)	(0.6) %	45,639	1.6%

Net income	\$ 181,576	7.6%	\$ 174,119	6.4%

NET REVENUES

Net revenues for the quarter ended June 30, 2005 increased 14.0% compared to net revenues for the three months ended June 30, 2004. This increase was primarily due to the development fee and usage charges relating to a custom designed course for one client. Online sales continue to be an important factor contributing to our overall revenue growth, a trend that began in 2003. In the 2005 period, net revenues from online sales accounted for approximately \$816,000, or 30% of net revenues. In the 2004 period, net revenues from online sales accounted for \$479,000, or 20% of net revenues.

In the second quarter of 2005, net revenues from our accounting/finance and related products were \$2.0 million, compared to \$1.7 million in the comparable 2004 period. This increase is due to various factors, including converting a number of our existing video customers to our online services, partnering with more professional organizations and our continued marketing efforts to increase sales and the one large sale referred to above. For the second quarter of 2005, net revenues from accounting/finance products, which includes both subscription-based revenue and direct sales of course material on a non-subscription basis, was \$1.85 million. Net revenues from custom work and advertising were \$171,000. For the comparable 2004 period, subscription-based revenue and direct sales of course material on a non-subscription basis was \$1.6 million, and net revenues from custom work and advertising was \$119,000.

Net revenues from sales of our engineering products, which are not subscription-based, were \$77,000 in the second quarter of 2005 compared to \$64,000 in the second quarter of 2004. This increase is due to our continual sales and marketing efforts in this area.

Net revenues from video production, duplication, consulting and e-commerce services for the second quarter of 2005 were \$489,000 compared to \$259,000 for the second quarter of 2004. This increase is primarily attributable to the growth in custom work in both the technology and video production areas. Under our long-standing policy, revenue is credited to the originating department regardless of the type of service that is performed. For example, a contract to convert videotapes to digital format is credited to the accounting education department if that is where the sale originated, even if the project has nothing to do with accounting. Custom work is non-repetitive and subject to market conditions and can vary from quarter to quarter.

For the second quarter of 2005 Working Values contributed \$116,000 to net revenues compared to \$363,000 in the second quarter of 2004. In 2004, the Company had two large consulting contracts for ethics-based training that it completed during the year. In 2005, the Company began concentrating on

Edgar Filing: SmartPros Ltd. - Form 10QSB

developing its newest product, Learning Moments. Custom work is non-repetitive and subject to market conditions and can vary from quarter to quarter.

COST OF REVENUES

Cost of revenues includes production costs - I.E., the salaries, benefits and other costs related to personnel, whether our employees or independent contractors, who are used directly in production, including producing our educational programs; royalties paid to third parties; the cost of materials, such as videotape and packaging supplies; and shipping costs. There are many different types of expenses that are characterized as production costs and many of them vary from period to period depending on many factors.

12

Compared to the second quarter of 2004, cost of revenues in the second quarter of 2005 increased by \$325,000. The increase was primarily attributable to additional personnel and the cost of sub-contracted labor related to various projects in the technology department. The expenses that showed the greatest variations from 2004 to 2005 and the reasons for those variations were as follows:

- o OUTSIDE LABOR AND DIRECT PRODUCTION COSTS. Outside labor includes the cost of hiring actors and production personnel such as directors, producers and cameramen and the out-sourcing of non-video technology. The cost of actors increased \$7,000; the cost of video production and technology personnel increased \$188,000. This increase is directly related to the outsourcing of labor associated with the completion of a number of custom technology and video projects. The higher than anticipated cost of such personnel reduced our margins during the quarter. Direct production costs, are costs related to producing videos other than labor costs, such as the cost of renting equipment and locations, decreased \$4,000. These variations are related to the type of video production and other projects and do not reflect any trends in our business. As our business grows we may be required to hire additional production personnel, increasing our cost of revenues.
- o ROYALTIES. Royalty expense increased in the 2005 period compared to the 2004 period by \$32,000. This increase was due to a growth of sales in our accounting and engineering products. During the first quarter of 2004 the Company had over-accrued its royalty expense because some of our partners were behind in providing us with the necessary sales information. The adjustment for this over-accrual is reflected in lower costs for the second quarter of 2004.
- o SALARIES. Overall, payroll and related costs attributable to production personnel increased by \$115,000. Most of the increase - I.E., \$105,000 - was attributable to our technology group.
- o TRAVEL AND ENTERTAINMENT; SHIPPING. Travel and entertainment and shipping expenses increased only \$1,000, reflecting our continuing effort to control costs.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses include corporate overhead such as compensation and benefits for administrative, sales and marketing and finance personnel, rent, insurance, professional fees, travel and entertainment and office expenses. While general and administrative expenses in the second quarter

Edgar Filing: SmartPros Ltd. - Form 10QSB

of 2005 were \$105,000 higher than they were in 2004, as a percentage of net revenues they decreased by 2%. Part of the increase is attributable to the costs of being a public company, such as legal, accounting, investor relations, insurance and regulatory expenses, which we did not have in the second quarter of 2004. The increase in these expenses was \$68,000. In addition, personnel costs increased by \$28,000, which is primarily due to increases in our accounting department necessary to our being a public company. Selling costs, which includes advertising, promotion, travel and entertainment, increased by \$9,000. Although, we make every effort to control our costs, we anticipate that general and administrative expenses will continue to increase primarily as a result of increased accounting, legal and insurance costs, attributable to the fact that we are now a public company.

DEPRECIATION and AMORTIZATION

Depreciation and amortization expenses decreased in the second quarter of 2005 compared to the second quarter of 2004 as a number of our assets became fully depreciated. We expect our depreciation and amortization expenses on our current assets to decrease in 2005 as many of our older assets are either fully or almost fully depreciated and we do not anticipate replacing them at the same rate.

INCOME FROM OPERATIONS

For the three months ended June 30, 2005 net income from operations was \$128,000 compared to \$195,000 in the comparable period of 2004. This is primarily attributable to the fact that the increase in net revenues was offset by an increase in sub-contracted labor, additional personnel required for some of our consulting jobs and the additional costs incurred related to being a public company. Our quarterly earnings are effected by the mix of custom projects compared to subscription and education-based sales.

13

OTHER INCOME/EXPENSES

Other income and expense items consist of interest paid on indebtedness and interest earned on deposits. As a result of the successful completion of our initial public offering, we were able to retire all of our debt (other than capital lease obligations), reducing our interest expense. At the same time, since we have not yet used the balance of the net proceeds from our initial public offering, our interest income has increased. As a result, for the second quarter of 2005 we had net interest income compared to a net interest expense for the second quarter of 2004.

NET INCOME

For the three months ended June 30, 2005, we recorded a net profit of \$174,119, or \$.03 per share, basic and diluted, compared to a net income of \$181,576 or \$.07 and \$.06 per share, basic and diluted, for the three months ended June 30, 2004. The decrease in net profit is attributable to increased revenue offset by an increase in operating costs. The decrease in earnings per share is a result of the additional shares issued in October 2004 in connection with our public offering.

COMPARISON OF SIX MONTHS ENDED JUNE 30, 2005 AND 2004

The following table compares our statement of operations data for the six months ended June 30, 2005 and 2004. The trends suggested by this table may not be indicative of future operating results, which will depend on various

Edgar Filing: SmartPros Ltd. - Form 10QSB

factors including the relative mix of products sold (accounting/finance, engineering or corporate training) and the method of sale (video or online).

	SIX MONTHS ENDED JUNE 30,			
	2004		2005	
	AMOUNT	PERCENTAGE	AMOUNT	PERCENTAGE
Net revenues	\$ 4,592,296	100.0%	\$ 5,555,992	100.0%
Cost of revenues	1,686,988	36.7%	2,240,944	40.3%
Gross profit	2,905,308	63.3%	3,315,048	59.7%
Selling, general and administrative	2,355,409	51.3%	2,710,830	48.8%
Depreciation and amortization	346,226	7.5%	285,899	5.1%
Total operating expenses	2,701,635	58.8%	2,996,729	53.9%
Operating income	203,673	4.4%	318,319	5.8%
Other (expense), net	(29,457)	(.6)%	71,892	1.2%
Net income	\$ 174,216	3.8%	\$ 390,211	7.0%

NET REVENUES

Net revenues for the six months ended June 30, 2005 increased 21.0% compared to net revenues for the six months ended June 30, 2004. Online sales continue to be an important factor contributing to our overall revenue growth, a trend that began in 2003. In the 2005 period, net revenues from online sales accounted for approximately \$1.44 million, or 26% of net revenues. In the 2004 period, net revenue from online sales accounted for \$1.15 million, or 25% of net revenues.

For the six months ended June 30, 2005, net revenues from sales of accounting and finance products grew in real dollars but was relatively flat as a percentage of total net revenues compared to the six months ended June 30, 2004. In the first six months of 2005, net revenues from sales of accounting/finance products were \$4.07 million, or 73% of net revenues. For the first six months of 2004, net revenues from sales of accounting/finance products were \$3.32 million, or 72% of net revenues. These increases are due in part to an increased level of sales in the subscription-based products and a development fee and usage charge related to a custom designed course for one customer. For the first six months of 2005, net revenues from sales of accounting/finance products, which includes subscription-based revenue and direct sales of course material on a non-subscription basis, was \$3.5 million. Net revenues primarily from custom work and advertising was \$584,000. For the first six months of 2004, subscription-based revenue and direct sales of course material on a non-subscription basis was \$3.1 million, and net revenues from custom work and advertising was \$191,000 in the aggregate.

Net revenues from sales of engineering products, which are not subscription-based, increased in absolute terms but were relatively flat as a percentage of total net revenues. For the six months ended June

Edgar Filing: SmartPros Ltd. - Form 10QSB

30, 2005, net revenues from sales of engineering products were \$323,000 or 5.8% of net revenues. For the six months ended June 30, 2004, net revenues from sales of engineering products were \$251,000, or 5.5% of net revenues. The increase in net revenue from sales of engineering products is primarily attributable to our continuing effort to market existing products.

For the first six months of 2005, Working Values contributed \$186,000 to net revenues compared to \$375,000 for the first six months of 2004. The decrease in revenues from Working Values in 2005 can be attributed to several factors. In 2004, the Company had two large consulting contracts for ethics-based training courses. In addition, Working Values has been concentrating on adding scalable products to its course library.

Net revenues from video production, duplication, consulting and e-commerce services for the first six months of 2005 were \$972,000 compared to \$657,000 for the first six months of 2004. Of this increase, approximately \$61,000 was attributable to video production and duplication. Consulting revenues increased by \$254,000 over the comparable period of last year as a result of completing two custom projects. In addition to doing custom work for clients, the technology department provides services to the entire company.

COST OF REVENUES

Compared to the first six months of 2004, cost of revenues in the first six months of 2005 increased in absolute terms and as a percent of net revenues, resulting in lower gross margins. In the case of the first six months of 2004 and 2005, the expenses that showed the greatest variations and the reasons for those variations were as follows:

- o OUTSIDE LABOR AND DIRECT PRODUCTION COSTS. While the cost of actors decreased by \$5,000, the cost of outsourced production personnel related to custom video and technology projects increased by \$339,000. Direct production costs, other than labor, decreased \$24,000.
- o SALARIES. Overall, payroll and related costs attributable to production personnel increased by \$200,000. Most of this increase was attributable to the fact that we added additional personnel to Working Values and to our consulting group to meet the demands of a number of custom projects and to design new products. In addition, the technology group has been redesigning and making continual improvements to our learning management system.
- o ROYALTIES. Royalty expense for both periods was constant at \$297,000. If sales volume increases, we expect the actual royalty payments in 2005 will be higher than they were in 2004.

As our business grows we may be required to hire additional production personnel, increasing our cost of revenues.

GENERAL AND ADMINISTRATIVE EXPENSES

While general and administrative expenses in the first six months of 2005 increased in absolute terms compared to the first six months of 2004, as a percentage of net revenues they decreased by 2%. The increase is primarily attributable to the costs of being a public company, increased marketing and product development costs and an increase in staffing and related costs, which offset reductions in our communication costs and other operating expenses. We anticipate that general and administrative expenses will continue to increase as

Edgar Filing: SmartPros Ltd. - Form 10QSB

a result of increased accounting, legal and insurance costs resulting from the fact that we are now a public company.

DEPRECIATION and AMORTIZATION

Depreciation and amortization expenses were lower in the six months ended June 30, 2005 than they were in the comparable 2004 period, and as a percentage of net revenues they decreased from 7.5% to 5.1%. The decrease is attributable to the fact that although we continue to purchase additional computer hardware many of our older assets are now fully depreciated. Through June 2005 we acquired \$141,000 of depreciable and amortizable assets compared to \$37,000 in the same period of 2004. In addition, many of our older assets are either fully or almost fully depreciated. We expect our depreciation and amortization

15

expenses to decrease as we realize the full effect of the asset acquisitions and capitalized costs that were made before 2004.

INCOME FROM OPERATIONS

For the first six months of 2005 net income from operations was \$318,000 compared to \$204,000 in the comparable period of 2004. This increase is primarily attributable to approximately \$1 million increase in sales in the 2005 period, offset by the additional costs (i) for outside labor and personnel necessary to complete custom projects and (ii) related to being a public company.

OTHER INCOME/ EXPENSES

Other income and expense items consist of interest paid on indebtedness and interest earned on deposits. The decrease in our net interest expense is due primarily to the reduction in debt in the fourth quarter of 2004 following the completion of our public offering. In addition, the approximately \$5.5 million of net proceeds from the offering (after repaying debt) and cash generated from operations are invested in various money market funds and interest bearing securities. This resulted in \$72,000 of net income for the first six months of 2005 as compared to a net expense of \$29,000 in the same period of 2004.

NET INCOME

For the six months ended June 30, 2005, we recorded a net profit of \$390,000 compared to \$174,000 for the six months ended June 30, 2004. This increase is attributable to increased revenues of almost \$1 million, net interest income of \$72,000 and our continuing efforts to control our costs and expenses.

CONTRACTUAL OBLIGATIONS, COMMITMENTS AND CONTINGENCIES

Historically, we have financed our working capital requirements through internally generated funds, sales of equity and debt securities and proceeds from short-term bank borrowings. In October 2004 we completed our initial public offering, which resulted in net proceeds to us of approximately \$6 million.

Our working capital as of June 30, 2005 was approximately \$3.95 million compared to \$3.39 million at December 31, 2004. Our current ratio at June 30, 2005 was 1.92 to 1 compared to 1.75 to 1 at December 31, 2004. The current ratio is derived by dividing current assets by current liabilities and is a measure used by lending sources to assess our ability to repay short-term liabilities.

Edgar Filing: SmartPros Ltd. - Form 10QSB

The largest component of our current liabilities, \$3.63 million at June 30, 2005 compared to \$3.74 million at December 31, 2004, was deferred revenue, which is revenue collected or billed but not yet earned under the principles of revenue recognition. Most of this revenue is in the form of subscription fees and will be earned over the next 12 months. The cost of fulfilling our monthly subscription obligation does not exceed this revenue and is booked to expense as incurred. For some of our products, there are no additional costs, other than shipping costs, required to complete our obligations, as the material already exists.

The primary components of our operating cash flows are net income adjusted for non-cash expenses, such as depreciation and amortization, and the changes in accounts receivable, accounts payable and deferred revenues. For the six months ended June 30, 2005, net cash generated by operating activities was \$389,000 and we had a net cash increase of \$1.47 million, which includes a \$1.25 million transfer from investment securities held for sale. Exclusive of that transfer, net cash increased by \$221,000 after purchasing \$141,000 of fixed assets and debt reduction of \$33,000 during the first half of the year.

Capital expenditures for the six months ended June 30, 2005 were approximately \$141,000, which consisted primarily of computer equipment purchases and the capitalization of internally produced courses for Working Values. Although, we continually upgrade our technology hardware, we do not anticipate any significant capital expenditures relating to equipment purchases over the next 12 months.

At June 30, 2005 our only indebtedness consisted of capital lease obligations, the balance of which was \$88,000 compared to \$121,000 at December 31, 2004. We have three leases with IDB Leasing, which had an aggregate outstanding balance at June 30, 2005 of \$63,000. One lease has a 48-month term that expires in 2007, an imputed interest rate of 7.0% and monthly payments of \$2,055. A second lease has a 36-month term that expires in 2006, an imputed interest rate of 7.5% and monthly payments of \$996. The

16

third lease has a 36-month term that expires in 2007, an imputed interest rate of 6.05% and a monthly payment of \$313. In addition, we have outstanding balances on other capital leases of approximately \$10,000. In August 2004 we financed the purchase of a van. The loan is for a term of 36 months, bears interest at 4.99% per annum and requires 35 monthly payments of \$358 and a final payment of approximately \$13,800 due in August 2007. The lender has agreed to repurchase the vehicle at our option for the amount of the final payment less any applicable expenses, at the end of the term. At June 30, 2005, the balance on the loan was \$21,000.

As of June 30, 2005 we had commitments under two operating leases - the leases for executive offices in Hawthorne, New York and the Working Values executive offices in Sharon, Massachusetts - aggregating \$1.6 million through February 2010. In May 2004 we paid \$92,000 in connection with our termination of a sublease in Irvine, California.

We believe that the net proceeds of our initial public offering in October 2004 together with cash flow from operations will be sufficient to meet our working capital and capital expenditure requirements from the next 12 months.

In the future, we may issue additional debt or equity securities to satisfy our cash needs. Any debt incurred or issued may be secured or unsecured, at a fixed or variable interest rates and may contain other terms and conditions

Edgar Filing: SmartPros Ltd. - Form 10QSB

that our board of directors deems prudent. Any sales of equity securities may be at or below current market prices. We cannot assure you that we will be successful in generating sufficient capital to adequately fund our liquidity needs.

ITEM 3. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES. Management, with the participation of the chief executive officer and the chief financial officer, carried out an evaluation of the effectiveness of our "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934, as amended (the "Exchange Act") Rules 13a-15(e) and 15-d-15(e)) as of the end of the period covered by this quarterly report (the "Evaluation Date"). Based upon that evaluation, the chief executive officer and the chief financial officer concluded that, as of the Evaluation Date, our disclosure controls and procedures are effective, providing them with material information relating to us as required to be disclosed in the reports that we file or submit under the Exchange Act on a timely basis.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING. There were no changes in our internal controls over financial reporting, known to the chief executive officer or the chief financial officer that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1: LEGAL PROCEEDINGS.

We are not currently a party to any legal proceeding that we deem material.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

RECENT SALES OF UNREGISTERED SECURITIES

There were no sales of unregistered securities during the period covered by this Report.

USE OF PROCEEDS

On October 19, 2004, our registration statement on Form SB-2, commission file number 333-115454 (the "Registration Statement") registering the offer and sale of units (each a "Unit" and collectively the "Units"), each Unit consisting of three shares of our common stock, par value \$.0001 per share, and one and one-half common stock purchase warrants, was declared effective by the U.S. Securities and Exchange Commission. The warrants included in the Units have a term of five years and an exercise price of \$7.125

per share. We sold all 600,000 Units covered by the Registration Statement. Paulson Investment Company, Inc. was the representative of the underwriters of the offering. The gross proceeds to us from the offering were \$7.65 million and the net proceeds were \$6.0 million. As of the date hereof, we used \$490,000 of the net proceeds to repay indebtedness. The remaining \$5.5 million will be used for working capital and general corporate purposes, including acquisitions.

Edgar Filing: SmartPros Ltd. - Form 10QSB

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

On Thursday, June 9, 2005 at 10:00 A.M. eastern time we held our 2005 Annual Meeting of Stockholders for the purposes of electing two (2) Class I directors and obtaining advisory approval of the appointment of our independent registered public accounting firm for the fiscal year ending December 31, 2005.

In connection with the Annual Meeting, proxies were solicited pursuant to Regulation 14A under the Exchange Act and there was no solicitation in opposition to any of the director-nominees. At the Annual Meeting, all of the director-nominees were re-elected for three-year terms. Each director-nominee received at least 3,790,068 votes, which represented 75% of the shares voted. In addition, advisory approval of the appointment of Holtz Rubenstein Reminick LLP as our independent registered public accounting firm for the fiscal year ended December 31, 2005 was ratified with 3,778,677 votes in favor, representing 74% of the shares voted.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS.

a. Exhibits:

Exhibit No. -----	Description -----
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Smartpros Ltd.

(Registrant)

Date: August 12, 2005

/s/ Allen S. Greene

Chief Executive Officer

Edgar Filing: SmartPros Ltd. - Form 10QSB

Date: August 12, 2005

/s/ Stanley P. Wirtheim

Chief Financial Officer
(Principal Financial Officer)