

Edgar Filing: VFINANCE INC - Form 10QSB/A

VFINANCE INC  
Form 10QSB/A  
August 18, 2003

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

FORM 10-QSB/A  
(Mark One)

QUARTERLY REPORT UNDER SECTION 13 or 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2002

or

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the transition period \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-11454-03

VFINANCE, INC.

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

Delaware

58-1974423

-----  
(State or other jurisdiction of  
incorporation or organization)

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

3010 North Military Trail, Suite 300, Boca Raton, FL 33431

-----  
(Address of principal executive offices)

(561) 981-1000

-----  
(Issuer's telephone number)

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

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 registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

State the number of shares outstanding of each of the issuer's classes of common equity, as of June 30, 2002:

23,187,097 - shares of Common Stock \$0.01 par value

Transitional Small Business Disclosure Format (Check one): Yes ; No

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INDEX  
VFINANCE, INC.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets - December 31, 2001 and  
June 30, 2002 (Unaudited) .....4

Consolidated Statements of Operations for the three and  
six months ended June 30, 2001 and 2002 (Unaudited) .....5

Consolidated Statements of Cash Flows for the three and  
six months ended June 30, 2001 and 2002 (Unaudited) .....6

Notes to Consolidated Financial Statements (Unaudited) .....7

Item 2. Management's Discussion and Analysis of Financial Condition  
and Results of Operations .....13

PART II. OTHER INFORMATION

Item 1. Legal Proceedings .....15

Item 2. Changes in Securities .....15

Item 5. Other Information .....16

Item 6. Exhibits and Reports on Form 8-K .....16

Signatures

FORWARD-LOOKING STATEMENTS

The following information provides cautionary statements under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 (the Reform Act). We identify important factors that could cause our actual results to differ materially from those projected in forward-looking statements we make in this report or in other documents that reference this report. All statements that express, or involve discussions as to, expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, identified through the use of words or phrases such as we or our management believes, expects, anticipates, hopes, words or phrases such as will result, are expected to, will continue, is anticipated, estimated, projection and outlook, and words of similar import) are not statements of historical facts and may be forward-looking. These forward-looking statements are based largely on our

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expectations and are subject to a number of risks and uncertainties including, but not limited to, economic, competitive, regulatory, growth strategies, available financing and other factors discussed elsewhere in this report and in the documents filed by us with the Securities and Exchange Commission ("SEC"). Many of these factors are beyond our control. Actual results could differ materially from the forward-looking statements we make in this report or in other documents that reference this report. In light of these risks and uncertainties, there can be no assurance that the results anticipated in the forward-looking information contained in this report or other documents that reference this report will, in fact, occur.

These forward-looking statements involve estimates, assumptions and uncertainties, and, accordingly, actual results could differ materially from those expressed in the forward-looking statements. These uncertainties include, among others, the following: (i), the inability of our broker-dealer operations to operate profitably in the face of intense competition from larger full service and discount brokers; (ii) a general decrease in merger and acquisition activities and our potential inability to receive success fees as a result of transactions not being completed; (iii) increased competition from business development portals; (iv) technological changes; (v) our potential inability to implement our growth strategy through acquisitions or joint ventures; and (vi) our potential inability to secure additional debt or equity financing.

Any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time and it is not possible for our management to predict all of such factors, nor can our management assess the impact of each such factor on the business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

3

### vFINANCE, INC. CONDENSED CONSOLIDATED BALANCE SHEETS

	(AUDITED) December 31, 2001 -----	(UNAUDITED) June 30, 2002 -----
<b>Assets:</b>		
Cash and cash equivalents .....	\$ 1,826,474	\$ 1,959,639
Restricted cash .....	203,106	201,722
Due from clearing broker .....	588,222	-
Investments in trading securities .....	1,077,815	1,023,991
Accounts receivable, net of allowance for doubtful accounts of \$63,528 and \$359,537, respectively .....	93,719	194,574
Forgivable loans - employees, current portion .....	307,452	218,952
Notes receivable - employees, net of allowance for		

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doubtful accounts of \$60,550 and \$0, respectively .....	107,600	89,676
Prepaid expenses and other current assets .....	133,085	93,589
	-----	-----
Total current assets .....	4,337,473	3,782,143
Furniture and equipment, at cost:		
Furniture and equipment .....	940,537	372,848
Internal use software .....	146,835	158,500
	-----	-----
	1,087,372	531,348
Less accumulated depreciation .....	(403,970)	(243,219)
	-----	-----
Net furniture and equipment .....	683,402	288,129
Forgivable loans - employees .....	577,760	499,073
Goodwill .....	420,000	420,000
Other assets .....	387,177	172,483
	-----	-----
Total Assets .....	\$ 6,405,812	\$ 5,161,828
	=====	=====
Liabilities and Shareholders' Equity:		
Accounts payable .....	\$ 1,093,662	\$ 688,456
Accounts payable - employees .....	66,407	22,708
Due to clearing broker .....	-	106,476
Accrued payroll.....	1,264,081	856,013
Accrued interest.....	239,469	-
Other accrued liabilities .....	815,960	817,258
Securities sold, not yet purchased .....	53,981	90,998
Lines of credit .....	297,656	-
Subordinated promissory notes .....	650,000	-
Note payable, net of discount .....	1,162,429	482,375
Capital lease obligations, current portion .....	12,627	-
Other .....	-	22,892
	-----	-----
Total current liabilities .....	5,656,272	3,087,176
Letter of credit and promissory note .....	268,500	-
Capital lease obligations .....	56,641	-
Note payable - long term .....	-	1,500,000
Series A Convertible Preferred Stock, \$0.01 par value; 122,500 shares authorized; 122,500 shares issued and outstanding (liquidation preference of \$1,556,050 at December 31, 2001) .....	1,225	1,225
Series B Convertible Preferred stock, \$0.01 par value; 50,000 shares authorized; 50,000 issued and outstanding (liquidation preference of \$46,450 at December 31, 2001) .....	500	500
Common stock, \$0.01 par value, 75,000,000 shares authorized; 25,964,395 and 26,398,608 shares issued, and 22,952,885 and 23,187,097 outstanding, respectively .....	259,644	263,986
Additional paid-in-capital on preferred stock .....	1,565,775	1,487,025
Additional paid-in-capital on common stock .....	22,515,699	24,856,437
Deferred compensation .....	(82,657)	(82,657)
Accumulated deficit .....	(21,666,359)	(23,780,436)
	-----	-----
	2,593,827	2,746,080
Less treasury stock .....	(2,169,428)	(2,171,428)
	-----	-----

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Total Shareholders' Equity .....	424,399	574,652
	-----	-----
Total Liabilities and Shareholders' Equity .....	\$ 6,405,812	\$ 5,161,828
	=====	=====

See accompanying notes

4

vFINANCE, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

	Three Months Ended June 30,		Six Months End
	2001	2002	2001
	-----	-----	-----
Revenues:			
Commissions - agency .....	\$ 1,455,546	\$ 2,225,366	\$ 3,394,475
Commissions - principal .....	1,005,158	767,778	2,599,121
Success fees .....	170,337	455,531	1,939,335
Consulting and retainers .....	163,406	425,500	436,206
Other brokerage related income .....	139,088	148,145	303,715
Other .....	86,401	100,688	235,695
	-----	-----	-----
Total revenues .....	3,019,936	4,123,008	8,908,547
	-----	-----	-----
Cost of revenues:			
Commissions .....	1,578,979	1,687,119	3,691,719
Clearing and transaction costs .....	355,975	222,554	758,928
Success .....	-	362,557	651,976
Consulting and retainers .....	9,000	79,365	46,000
Other .....	11,376	9,445	27,210
	-----	-----	-----
Total cost of revenues .....	1,955,330	2,361,040	5,175,833
	-----	-----	-----
Gross profit .....	1,064,606	1,761,968	3,732,714
	-----	-----	-----
Other expenses:			
General and administrative .....	2,186,376	2,303,944	4,787,911
Net loss (gain) on trading securities .....	67,029	(995)	84,408
Professional fees .....	246,534	327,921	578,849

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Provision for bad debts .....	73,715	176,086	123,715
Legal settlements.....	22,605	61,860	39,210
Net unrealized loss (gain) on investments held for trading and stock purchase warrants .....	354,893	316,353	1,149,648
Depreciation and amortization .....	477,195	74,653	721,339
Amounts forgiven under forgivable loans .....	-	69,375	107,151
Stock based compensation expense .....	89,500	-	89,500
	-----	-----	-----
Total other expenses .....	3,517,847	3,329,197	7,681,731
	-----	-----	-----
Loss from operations .....	2,453,241	1,567,229	3,949,017
Loss on sale of property .....	14,071	-	16,180
Interest and dividend (income) expense .....	(86,763)	85,663	(204,929)
	-----	-----	-----
Pre-tax net loss .....	2,380,549	1,652,892	3,760,268
Income tax expense .....	-	139,513	-
	-----	-----	-----
Net loss .....	2,380,549	1,792,405	3,760,268
Less: Preferred stock dividend .....	30,625	48,125	61,250
	-----	-----	-----
Loss available to common stockholders .....	\$ 2,411,174	\$ 1,840,530	\$ 3,821,518
	=====	=====	=====
Loss per share:			
Basic .....	\$ 0.12	\$ 0.08	\$ 0.20
	=====	=====	=====
Weighted average number of common shares used in computing basic loss per share .....	19,514,421	23,220,430	19,297,313
	=====	=====	=====
Diluted .....	\$ 0.12	\$ 0.08	\$ 0.20
	=====	=====	=====
Weighted average number of common shares used in computing diluted loss per share .....	19,514,421	23,220,430	19,297,313
	=====	=====	=====

See accompanying notes

VFINANCE, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

Six Months Ended June 30,

-----	-----
2001	2002
-----	-----

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OPERATING ACTIVITIES		
Net loss .....	\$ (3,760,268)	\$ (2,114,076)
Adjustments to reconcile net loss to net cash used in operating activities:		
Non-cash fees received .....	-	(687,187)
Depreciation and amortization .....	721,339	148,013
Provision for doubtful accounts .....	120,881	235,460
Income tax receivable write off .....	-	139,513
Accretion of debt discount .....	-	121,875
Unrealized loss (gain) on sale of investments, net	839,558	167,244
Unrealized loss (gain) on stock purchase warrants	18,950	88,780
Loss (gain) on sale of investments, net .....	95,723	(13,648)
Proceeds from sale of investments .....	-	177,298
Amount forgiven under forgiveable loan .....	359,568	144,188
Repayment of Notes Receivable, employees .....	92,445	-
Stock based compensation .....	89,500	-
Loss on sale of equipment .....	16,180	-
Changes in operating assets and liabilities, net of businesses acquired:		
Accounts receivable .....	21,228	(286,315)
Forgivable Loans .....	12,875	23,000
Due from clearing broker .....	(375,784)	694,698
Notes receivable from employees .....	-	17,924
Investments in trading securities .....	162,051	312,959
Other current assets .....	(422,516)	40,880
Other assets and liabilities .....	-	20,645
Accounts payable and accrued liabilities .....	(381,157)	(549,282)
Securities, sold not yet purchased .....	512,347	37,017
	-----	-----
Net cash used in operating activities .....	(1,877,080)	(1,281,015)
INVESTING ACTIVITIES		
Purchase of equipment .....	(201,140)	(81,105)
Proceeds from sale of equipment .....	11,500	-
Purchase of treasury stock, net .....	(10,392)	-
Purchase of businesses .....	(1,233,335)	-
Disposal of businesses cash effect .....	-	1,659
Merger transaction costs .....	(185,859)	-
	-----	-----
Net cash used in investing activities .....	(1,619,226)	(79,446)
FINANCING ACTIVITIES		
Changes in capital leases .....	(8,343)	(29,749)
Changes in current debt .....	-	(31,875)
Proceeds from credit agreement .....	-	1,500,000
Proceeds from issuance of common stock related to private placement, net of cash and stock issuance costs .....	-	123,750
Increase in line of credit .....	63,504	-
Payment of long term debt .....	(66,790)	(68,500)
Repayment of shareholder's equity .....	(50,000)	-
	-----	-----
Net cash provided (used) by financing activities .	(61,629)	1,493,626
(Decrease) increase in cash and cash equivalents .	(3,557,935)	133,165
Cash and cash equivalents at beginning of year ...	5,454,071	1,826,474
	-----	-----
Cash and cash equivalents at end of period .....	\$ 1,896,136	\$ 1,959,639
	=====	=====

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See accompanying notes

6

vFinance, Inc.

Notes to Condensed Consolidated Financial Statements June 30, 2002  
(Unaudited)

## 1. DESCRIPTION OF BUSINESS

vFinance, Inc. (the "Company") is a "new-breed" financial services enterprise committed to building a worldwide audience of individuals looking to create wealth through their equity investments and businesses and the name change reflects the broader scope of services. The Company principally operates in one business segment, investment management services, consisting primarily of financial services, including retail brokerage and investment banking.

The Company conducts its broker/dealer operations and investment banking and consulting through vFinance Investments, Inc, a licensed broker dealer. It also operates its vFinance.com website through vFinance Holdings, Inc. and manages Critical Infrastructure Fund (BVI) LP through vFinance Advisors, LLC and vFinance Investors, LLC.

## 2. SIGNIFICANT ACCOUNTING POLICIES AND OTHER MATTERS

### Basis of Presentation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts have been eliminated in consolidation. Certain amounts for the prior year financial statements have been reclassified to conform to the current year presentation.

### Revenue Recognition

The Company earns revenue (commissions) from brokerage and trading which are recognized on the day of the trade - trade date basis. The Company also earns revenue from investment banking and consulting. Monthly retainer fees for investment banking and consulting are recognized as services are provided. Investment banking success fees are generally based on a percentage of the total value of a transaction and are recognized upon successful completion.

The Company does not require collateral from its customers. Revenues are not concentrated in any particular region of the country or with any individual or group.

The Company periodically receives equity instruments and stock purchase warrants from companies as part of its compensation for investment-banking services that are classified as investments in trading securities on the balance sheet, if still held at the financial reporting date. Primarily all of the equity instruments are received from small public companies. Generally, such stock purchase warrants are considered derivatives. The Company adopted Financial Accounting Standards Board Statement No. 133, ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES, ("SFAS No. 133") on January 1, 2000. The Company recognizes revenue for such stock purchase warrants when received based on the Black Scholes valuation model. On a monthly basis the Company recognizes unrealized gains or losses in the statement of operations based on the changes



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in value in the stock purchase warrants as determined by the Black Scholes valuation model.

Occasionally, the Company receives equity instruments in private companies with no readily available market value. Equity interests and warrants for which there is not a public market are valued based on factors such as significant equity financing by sophisticated, unrelated new investors, history of positive cash flow from operations, the market value of comparable publicly traded companies (discounted for liquidity) and other pertinent factors. Management also considers recent offers to purchase a portfolio company's securities and the filings of registration statements in connection with a portfolio company's initial public offering when valuing warrants.

7

### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the accompanying financial statements. Actual results may differ from those estimates, and such differences may be material to the financial statements.

### Cash and cash equivalents

Cash and cash equivalents include all highly liquid investments with maturities of three months or less when purchased.

### Investments

Investments are classified as trading securities and are held for resale in anticipation of short-term market movements or until such securities are registered or are otherwise unrestricted. Trading account assets, consisting of marketable equity securities and stock purchase warrants, are stated at fair value. At June 30, 2002 and 2001, investments consisted of common and preferred stock and stock purchase warrants held for resale. Realized gains or losses are recognized in the statement of operations when the related stock purchase warrant is exercised and the underlying shares are sold. Unrealized gains or losses are recognized in the statement of operations on a monthly basis based on changes in the fair value of the security as quoted on national or inter-dealer stock exchanges.

### New Accounting Standards

In July 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 142, GOODWILL AND OTHER INTANGIBLE ASSETS ("FAS 142"). Under the provisions of FAS 142, goodwill and indefinite lived intangible assets are no longer amortized, but are reviewed annually for impairment. Separable intangible assets that are not deemed to have an indefinite life will continue to be amortized over their useful lives. The Company adopted the new accounting rules beginning January 1, 2002. Management is currently assessing the financial impact FAS 142 will have on the consolidated financial statements, but does not believe it will be material because the Company wrote off most of the goodwill at December 31, 2001.

In August 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 144, ACCOUNTING FOR THE IMPAIRMENT OR

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DISPOSAL OF LONG-LIVED ASSETS ("FAS 144"), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes SFAS No. 121, ACCOUNTING FOR THE IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF, and the accounting and reporting provisions of APB Opinion No. 30, REPORTING THE RESULTS OF OPERATIONS - REPORTING THE EFFECTS OF DISPOSAL OF A SEGMENT OF A BUSINESS , AND EXTRAORDINARY, UNUSUAL AND INFREQUENTLY OCCURRING EVENTS AND TRANSACTIONS ("APB 30"). The Company adopted the new accounting rules beginning January 1, 2002. Management is currently assessing the financial impact FAS 144 will have on the consolidated financial statements, but does not believe it will be material because the Company wrote off most goodwill at December 31, 2001.

### Stock Based Compensation

The Company has elected to follow Accounting Principal Board Opinion No. 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES ("APB 25"), and related interpretations in accounting for its employee stock options and employee stock purchase warrants because the alternative fair value accounting provided for under Statement of Financial Accounting Standards No. 123, ACCOUNTING FOR STOCK BASED COMPENSATION ("SFAS 123"), requires the use of option valuation models that were not developed for use in valuing employee stock options. Under APB 25, if the exercise price of the Company's employee stock options or stock purchase warrants equals or exceeds the market price of the underlying stock on the date of grant no compensation expense is recognized.

8

### Fair Value of Financial Instruments

The fair values of the Company's financial instruments, which includes cash and cash equivalents, accounts receivable, investments, accounts payable, and accrued expenses approximate their carrying values.

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. The Company places its cash with high quality FDIC-insured financial institutions.

### Goodwill

The carrying values of goodwill as well as other long-lived assets will be tested annually under FAS 142. If this review indicates that the assets will not in part or fully be recoverable, as determined based on the undiscounted estimated cash flows of the Company, the Company's carrying values of the assets would be reduced to their estimated fair values in accordance with FAS 144.

### Income Taxes

The Company accounts for income taxes under the liability method in accordance with Statement of Financial Accounting Standards No. 109, ACCOUNTING FOR INCOME TAXES. Under this method, deferred income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

### Earnings per Share

The Company calculates earnings per share in accordance with Statement of

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Financial Accounting Standards No. 128, EARNINGS PER SHARE ("SFAS No. 128"). In accordance with SFAS No. 128, basic earnings per share is computed using the weighted average number of shares of common stock outstanding and diluted earnings per share is computed using the weighted average number of shares of common stock and the dilutive effect of options and warrants outstanding, using the "treasury stock" method.

### 3. IMPAIRMENT OF GOODWILL

Management determined that, as of December 31, 2001, a write-down of the goodwill related to the NW Holdings acquisition was necessary as the Company's projections of the future operating results of First Level indicated impairment. Based on such projections and other analysis the Company took an impairment charge aggregating \$876,000 related to NWH goodwill. Goodwill remaining as of June 30, 2002 and December 31, 2001 totaled \$420,000.

### 4. INCOME TAXES

Deferred income taxes reflect the net income tax effect of temporary differences between the carrying amounts of the assets and liabilities for financial reporting purposes and amounts used for income taxes.

### 5. SHAREHOLDERS' EQUITY

On November 28, 2001, the Company entered into a Note Purchase Agreement, as amended by subsequent letter agreements dated November 30, 2001, December 14, 2001, and December 28, 2001, February 13, 2002 and March 4, 2002 (collectively, the "Note Purchase Agreement"), with SBI Investments (USA) Inc. ("SBI"). Under the terms of the Note Purchase Agreement, SBI may provide a subordinated loan to the Company of up to \$1,500,000 in the form of a 48-month non-interest bearing, convertible note (the "Note"). As of December 31, 2001, the Company had received \$975,000 under the Note Purchase Agreement. The Note is convertible, at SBI's option, into as many as 3,421,053 shares of the Company's common stock at \$0.285 per share. The Company, at any time during the first three years of the agreement, can call for redemption of the Note at a price equal to 116.67% of the then outstanding principal amount of the Note, in whole (but not in part), or force the conversion of the Note into shares of the Company's common stock. Refer to footnote 9, Subsequent Events for certain conversions of the Note.

9

In accordance with EITF Issue No. 00-27, APPLICATION OF ISSUE NO. 98-5, ACCOUNTING FOR CONVERTIBLE SECURITIES WITH BENEFICIAL CONVERSION FEATURES OF CONTINGENTLY ADJUSTABLE CONVERSION RATIOS, TO CERTAIN CONVERTIBLE INSTRUMENTS, and APB 21, the Company recorded an imputed interest factor related to the Note Purchase Agreement of \$563,000. The Company fully expensed any beneficial conversion factor due to the fact that the SBI Note was immediately convertible. The imputed interest will be accreted ratably over the term of the loan as additional interest expense

The Company has elected to follow Accounting Principal Board Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25"), and related interpretations in accounting for its employee stock options because the alternative fair value accounting provided under FASB Statement No. 123, ACCOUNTING FOR STOCK-BASED COMPENSATION, ("SFAS 123") requires the use of option valuation models that were not developed for use in valuing employee stock options. As permitted, the Company adopted the disclosure alternative of SFAS 123. Under APB 25, when the

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exercise price of the Company's stock options equals or exceeds the fair value of the underlying stock on the date of grant, no compensation expense is recorded.

A summary of the stock option activity for the six months ended June 30, 2002 is as follows:

	Weighted Average Exercise Price	Number of Shares	Exer Pe
Outstanding options at December 31, 2001 .....	\$0.98	9,687,050	\$0.
Granted .....	\$0.52	1,446,117	\$0.
Canceled .....	\$2.34	455,143	
		-----	
Outstanding options at June 30, 2002 .....	\$0.90	10,678,024	\$0.
		-----	

A summary of the stock purchase warrant activity for the six months ended June 30, 2002 is as follows:

	Weighted Average Exercise Price	Number of Warrants	Exer Pe
Outstanding warrants at December 31, 2001 .....	\$2.73	3,108,499	\$0.
Granted .....	-	-	
Canceled .....	-	-	
		-----	
Outstanding options at June 30, 2002 .....	\$2.73	3,108,499	\$0.
		=====	

The following table summarizes information concerning stock options outstanding at June 30, 2002.

Option Price	Options Outstanding
-----	-----
0.35	4,858,427
0.45	240,000
0.50	100,000
0.55	69,000
0.63	3,180,000
0.62	200,000
1.00	753,000
2.25	333,597
0.70	39,000
3.00	210,000
3.25	100,000
4.00	220,000
4.13	20,000
4.25	75,000
4.50	5,000
5.00	260,000
6.00	15,000
	-----
	10,678,024

The following table summarizes information concerning warrants outstanding at June 30, 2002.

Exercise Price	Warrants Outstanding
-----	-----
0.35	993,500
0.63	400,000
2.25	585,000
2.50	300,000
6.00	129,999
7.20	700,000
-----	-----
	3,108,499
	=====

Pro forma information regarding net loss is required by SFAS 123, which also requires that the information be determined as if the Company has accounted for its employee stock options under the fair value method. The fair value for options and warrants granted was estimated at the date of grant using the Black Scholes option pricing model with the following weighted-average assumptions: for 2002 risk-free interest rates of 4.765%; no dividend yields; volatility factor of the expected market price of the Company's common stock of 1.610 for options and warrants and an expected life of the options and warrants of 4-5 years; The Company's pro forma net loss for the period ended June 30, 2002 was \$ 2,318,437. The Company's pro forma basic and diluted net loss income per share for the period June 30, 2002 was \$0.10. The impact of the Company's pro-forma net loss and loss per share of the SFAS 123 pro forma requirements are not likely to be representative of future pro forma results.

6. DEBT

On January 25, 2002, the Company entered into a Credit Agreement with UBS Americas, Inc. ("UBS"). Under the terms of the Credit Agreement, UBS provided a revolving credit facility of up to \$3,000,000 to the Company for the purpose of supporting the expansion of its brokerage business or investments in infrastructure to expand its operations or its broker-dealer operations. The Company borrowed \$1,500,000 under the credit facility on January 28, 2002. In order for the Company to borrow the unused \$1,500,000 balance of such credit facility, the Company must raise an additional \$1,500,000 in capital subject of other certain requirements. The Credit Agreement does not provide for conversion of the debt into equity securities. The loan has a term of 3 years, must be repaid in full by January 2005, and bears interest at one month LIBOR plus a LIBOR margin of 2% if the loan is repaid within a month or 5% if it is outstanding more than a month. Among other covenants, Section 5.10 of the Credit Agreement requires the Company to maintain shareholder's equity of at least \$7,000,000. On April 12, 2002 UBS waived this requirement of the Credit Agreement to the extent necessary to exclude the Company's write-off of goodwill aggregating \$8,852,020 included in the Company's consolidated financial

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statements for the year ended December 31, 2001.

The Company must make early repayments under the Credit Agreement if there is an increase in the number of clearing transactions through UBS attributable to: an acquisition of a broker dealer firm, a new line of business, or the hiring of more than 4 brokers in a single or related transaction. All determinations as to required early repayment shall be made by UBS, in its reasonable judgment. To date, UBS has not notified the Company of any such determination.

### 7. DIVIDEND

As part of a meeting held on June 28, 2002 and pursuant to Delaware General Corporation Law, the Company's Board of Directors approved a dividend (the "Dividend") to the Company's Series A Preferred Shareholders of all the common stock of the Colonial Direct Financial Group, Inc. ("Colonial Direct"). The Company acquired such common stock of Colonial Direct as part of the share exchange transaction completed on January 4, 2001. The impact of the Dividend on the Company's consolidated balance sheet for the period ended June 30, 2002, was as follows:

Reduction of Total Assets .....	\$ 362,513
	-----
Reduction of Total Liabilities .....	\$ 2,581,841
	-----
Net Increase in Book Value .....	\$ 2,219,328
	-----

11

For the six month period ended June 30, 2002, the Company reflected an operating loss relating to Colonial Direct of \$292,798. Such an amount consisted of \$123,778 of general and administrative expenses, \$95,604 in depreciation and \$73,416 in interest expense. In addition, Colonial Direct and its related subsidiaries recorded no revenues for the same period and had ceased operations in 2001.

### 8. ACQUISITIONS

On May 29, 2002, the Company entered into a definitive select asset purchase agreement (the "Agreement") with Somerset Financial Partners, Inc., ("Somerset") a Delaware corporation to acquire certain of its assets. Through its subsidiaries, Somerset acted as a registered broker dealer and was engaged in other financial services including financial planning, insurance and mortgage brokerage. Through the Agreement, the Company agreed to acquire all Somerset's brokerage customer and client accounts, advances to registered representatives and certain other selected assets. The Company also agreed to assume certain liabilities including selected leases and hire select salaried personnel and independent contractors. The Agreement was subsequently amended on June 17, 2002 (the "Amendment"). The Agreement and Amendment provide for the payment of 1,000,000 shares of Common Stock. In addition, and based upon certain performance criteria, the Company also has agreed to pay up to an additional 2,000,000 shares of its Common Stock and warrants to purchase up to 500,000 additional shares of its Common Stock, during the first year after the

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transaction is closed. The Company will also issue up to 1,400,000 incentive stock options to purchase its Common shares to select Somerset employees who will be joining the Company. Those options will be issued subject to normal vesting and other conditions. All closing conditions of the Agreement and Amendment were required to be met on or before August 1, 2002 (the "Amended Closing Date").

Pursuant to the Agreement and Amendment, effective June 17, 2002 the Company received the transfer of all agreed upon brokerage customers and client accounts as well as the registration of approximately 25 registered personnel of Somerset. Furthermore, as of such date, the Company began reflecting in its financial statements the applicable revenue production and other associated costs. Under the escrow agreement signed in conjunction with the Agreement and Amendment, the Company instructed its transfer agent to deliver to and in the name of its escrow agent a total of 3,000,000 shares of the Company's Common Stock (the "Escrowed Shares"). The Escrowed Shares will only be delivered to Somerset when Somerset achieves all the closing conditions. As of June 30, 2002, the Escrowed Shares have not been reflected as outstanding in the Company's financial statements or footnotes.

In August 2002, as all closing conditions of the Agreement and Amendment were not met as of the Amended Closing Date, the Company issued a default letter to Somerset (the "Default Letter"). Among other things, the Default Letter provided formal notice to Somerset of its default under the Agreement and Amendment. The Company is negotiating revised terms and conditions with Somerset with the intention of amending the Agreement and Amendment.

### 9. Subsequent Events

In July 2002, certain SBI Note holders converted \$177,500 of principal into 622,807 Common Shares of the Company.

12

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

SIX MONTHS ENDED JUNE 30, 2001 COMPARED TO THE SIX MONTHS ENDED JUNE 30, 2002

### STATEMENTS OF OPERATIONS

Operating revenues were \$8,908,547 for the six months ended June 30, 2001 as compared to \$9,848,837 for the six months ended June 30, 2002 an increase of \$940,290 or 10.6%. The primary reason for the increase was an increase in agency brokerage commission revenues.

Cost of revenues were \$5,175,833 for the six months ended June 30, 2001 as compared to \$5,518,396 for the six months ended June 30, 2002 an increase of \$342,563 or 6.6%. The increase was primarily due to an increase in revenue which was offset by costs savings associated with the consolidation of the Company's three broker dealers into a single entity and its related clearing arrangement. As a consequence, gross profit was \$3,732,714 for the six months ended June 30, 2001 as compared to \$4,330,441 for the six months ended June 30, 2002, an increase of \$597,727. Gross margin percentage was 42% for the six months ended June 30, 2001 as compared to 44% for the six months ended June 30, 2002.

General and administrative expenses were \$4,787,911 for the six months ended

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June 30, 2001 as compared to \$4,708,840 for the six months ended June 30, 2002 a decrease of \$17,172 or 0.4%.

Net loss (gain) on trading securities was \$84,408 for the six months ended June 30, 2001 as compared to \$(13,648) for the six months ended June 30, 2002, an increase in net of \$98,056. The change was due primarily to the sale of certain securities at prices higher than the fair value reflected in prior periods.

Professional fees were \$578,849 for the six months ended June 30, 2001 as compared to \$567,198 for the six months ended June 30, 2002, a decrease of \$11,651 or 2.0%. The decrease in cost was primarily attributable to a decreased level of merger activity.

The provision for bad debt was \$123,715 for the six months ended June 30, 2001 as compared to \$236,208 for the six months ended June 30, 2002, an increase of \$112,493 or 91.0%. The Company provides for credit losses at the time it believes accounts receivable may not be collectible. Such evaluations are made and recorded on a monthly basis. Credit losses have not exceeded management's expectations. The increase was primarily due to the write-off of certain investment banking receivables relating to the Company's West cost operations which has currently been closed down. The net receivable on the financial statement as of June 30, 2002 was \$194,574.

The net unrealized loss (gain) on investments held for trading and stock purchase warrants was \$1,149,648 for the six months ended June 30, 2001, as compared to \$256,024 for the six months ended June 30, 2002. The change was primarily due to an increase in the market value of investments held by the Company in conjunction with equity instruments received from various investment banking clients.

Depreciation and amortization was \$721,339 for the six months ended June 30, 2001 as compared to \$148,013 for the six months ended June 30, 2002, a decrease of \$573,326 or 79.5%. The decrease was primarily because the Company has adopted FAS 144 that prohibits amortization of goodwill related to acquisitions and Company's write off of \$8,852,020 in goodwill for the year ending December 31, 2001.

The amount forgiven under forgivable loans was \$107,151 for the six months ended June 30, 2001 as compared to \$144,188 for the six months ended June 30, 2002. The increase was attributable to the accelerate write off of certain loans.

Total other expenses were \$7,681,731 for the six months ended June 30, 2001 as compared to \$6,147,932 the six months ended June 30, 2002 a decrease of \$1,533,799 or 20.0%. As a consequence the loss from operations was \$3,949,017 for the six months ended June 30, 2001 as compared to \$1,817,491 for the six months ended June 30, 2002 a decrease of \$2,131,526 or 54.0%.

13

### LIQUIDITY AND CAPITAL RESOURCES

The Company had \$1,959,639 of unrestricted cash at June 30, 2002.

Net cash used in operating activities for the six months ending June 30, 2001, \$1,877,080 as opposed to net cash used in operating activities of \$1,281,015 for the six months ending June 30, 2001. The decrease in net cash used in operating activities was primarily due to a decrease in the net loss from \$3,760,268 for



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the six months ending June 30, 2001 to \$2,165,576 for the six months ended June 30, 2002 offset by and increase in non-cash fees received on investment banking transactions of \$687,187.

Net cash used in investing activities for the six months ending June 30, 2001, was \$1,619,226 as opposed to net cash used in investing activities of \$79,446 for the six months ending June 30, 2002. The primary reason for the decrease in net cash used in investing activities was that the Company made no acquisitions in the six months ending June 30, 2002 and decreased purchases of equipment to \$201,140 for the six months ending June 30, 2001 from \$81,105 for the six months ending June 30, 2002.

Net cash used in financing activities for the six months ending June 30, 2001, was \$61,629 as opposed to net cash provided by financing activities of \$1,493,626 for the six months ending June 30, 2002. The primary reason for the increase in net cash provided by financing activities was that the Company entered into the agreement described above in footnote 7. Debt with UBS Paine Webber on January 25, 2002.

The Company anticipates it will need additional debt or equity financing in order to carry out its long-term business strategy. Such strategy may be financed by bank borrowings, public offerings, private placements of equity or debt securities, or a combination of the foregoing.

We do not have any material commitments for capital expenditures over the course of the next fiscal year.

The Company's operations are not affected by seasonal fluctuations however they are to some extent reliant on the continuation of mergers and acquisitions and related financings in the entrepreneurial marketplace.

14

## Part II. OTHER INFORMATION

### Item 1. LEGAL PROCEEDINGS

On April 4, 2002, Composite Industries of America, Inc. ("CIA") filed a complaint against the Company, Lenore Avenue LLC ("Lenore"), Navigator Management Ltd. ("Navigator"), Burlington Street LLC ("Burlington"), Southridge Capital Management, Union Atlantic Capital, L.C., Hyperion Holdings, LLC, Steve Hicks, Christy Constabile, Paul T. Mannion, Andrew S. Reckles, Vincent S. Sbarra and other unidentified defendants (collectively, the "Defendants") in the United States District Court, District of Nevada (Case No. CV-S-02-0482-PMP-RJJ). In its complaint, CIA alleges that on or about April 5, 2001, CIA entered into an agreement with Lenore and Navigator, pursuant to which CIA issued its 6% convertible debenture in the aggregate amount of \$1 million to Lenore and Navigator and, contrary to the terms of such purported agreement, Lenore and Navigator sold, with the assistance of the other Defendants, securities of CIA collateralizing CIA's obligations under the debenture. CIA also alleges that on or about October 22, 2001, CIA entered into an agreement with Lenore, Navigator and Burlington, pursuant to which CIA issued its 6% convertible debenture in the aggregate principal amount of \$750,000 to Lenore, Navigator and Burlington, and, contrary to the terms of the purported agreement, Lenore, Navigator and Burlington sold, with the assistance of the other Defendants, securities of CIA collateralizing CIA's obligations under the debenture.

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CIA is seeking general damages against the Defendants of \$202,500,000, punitive damages in an unspecified amount, treble damages, reasonable attorneys fees, court costs and such other relief as the court may deem just and proper. The Company believes that CIA's claims against the Company are without merit and will vigorously defend itself in the action.

Reference is made to Item 3. "Legal Proceedings" in the Form 10-KSB/A for the year ended December 31, 2001 for the Company.

### Item 2. CHANGES IN SECURITIES

On January 7, 2002 the Company sold 350,878 unregistered shares at a price of \$0.285 per share for a total consideration of \$100,000 to AMRO International, S.A.

On January 17, 2002 the Company sold 83,334 unregistered shares at a price of \$0.285 per share for a total consideration of \$23,750 to WorldVentures Fund I, LLC.

The above noted securities issued to the two investors were exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended, and Rule 506 of Regulation D promulgated thereunder because the securities were acquired in a privately negotiated transaction by sophisticated investors.

During the first quarter of 2002, the Company granted stock options to purchase an aggregate of 508,117 shares of the Company's common stock to six employees of the Company. The exercise prices of these options range from \$.35 to \$2.25. During the second quarter of 2002, the Company granted stock options to purchase an aggregate of 830,000 shares of the Company's common stock to four employees of the Company. The exercise prices of these options range from \$.35 to \$.70. The option grants were exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended, because the individuals receiving the options are sophisticated investors who have knowledge of all material information about the Company.

15

### ITEM 5. OTHER

On May 10, 2002, the Company engaged the firm of Feldman, Sherb & Co., P.C. ("Feldman") as its new independent auditors. At the time of such engagement, the Company was aware of Feldman's planned merger into Grassi & Co., CPA's, P.C. as well as the planned departure of certain of the principal accountants at Feldman who subsequently formed their own firm, Sherb & Co., LLP ("Sherb").

The Company dismissed Feldman, on August 9, 2002. The decision to dismiss Feldman was recommended and approved by the Board of Directors. During the interim period preceding the dismissal, there were no disagreements with Feldman on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which, if not resolved to the satisfaction of Feldman, would have caused Feldman to make reference to the subject matter of the disagreements in connection with its reports. Feldman was not required to issue any reports on the Company's financial statements during the period prior to Feldman's dismissal.

On August 10, 2002, the Company engaged the firm Sherb as its new independent auditors. The Company has authorized Feldman to respond fully to the inquiries

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of Sherb with regard to any accounting or financial matters relating to the Company.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) EXHIBITS

10.1 - Termination of Select Asset Purchase Agreement Among vFinance Investments, Inc., Somerset Financial Partners, Inc., Somerset Financial Group, Inc. Douglas Toth and Nicholas Thompson dated as of October 1, 2002. (1)

31.1 - Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer of the Company.

31.2 - Rule 13a-15(a)/15d-14(a) Certification of Chief Financial Officer of the Company.

32.1 - Section 1350 Certification by Chief Executive Officer of the Company.

32.2 - Section 1350 Certification by Chief Financial Officer of the Company.

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(1) Previously filed with the Company's Form 10-QSB/A dated November 14, 2002.

(b) REPORTS ON FORM 8-K

On August 14, 2002, the Company filed a Form 8-K pursuant to Item 9 thereof in order to disclose the submission to the Securities and Exchange Commission of the written statements of the Company's Chief Executive Officer and Chief Financial Officer required by Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

vFinance, Inc.

By: /s/ Leonard J. Sokolow

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LEONARD J. SOKOLOW, DIRECTOR,  
CHIEF EXECUTIVE OFFICER AND PRESIDENT

Date: August 18, 2003

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

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Signature  
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Capacity  
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Date  
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/s/ Leonard J. Sokolow  
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Director, Chief Executive Officer and  
President (Principal Executive Officer)

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