COMPUTER PROGRAMS & SYSTEMS INC
Form 10-Q
November 08, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**
For the quarterly period ended September 30, 2010.

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**
For the transition period from ______ to ______

Commission file number: 000-49796

COMPUTER PROGRAMS AND SYSTEMS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**74-3032373**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
6600 Wall Street, Mobile, Alabama	**36695**
(Address of Principal Executive Offices)	**(Zip Code)**

(251) 639-8100

(Registrant s Telephone Number, Including Area Code)

N/A

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Sections 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (of for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer (Do not check if a smaller reporting company)	¨	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of November 5, 2010, there were 10,962,874 shares of the issuer s common stock outstanding.

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COMPUTER PROGRAMS AND SYSTEMS, INC.

Form 10-Q

(For the three and nine months ended September 30, 2010)

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PART I

FINANCIAL INFORMATION

Item 1. Financial Statements.

COMPUTER PROGRAMS AND SYSTEMS, INC.

CONDENSED BALANCE SHEETS

	September 30, 2010 (Unaudited)	December 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	$ 1,688,208	$ 4,386,763
Investments	13,395,188	13,243,118
Accounts receivable, net of allowance for doubtful accounts of $1,149,000 and $759,000, respectively	24,719,064	19,472,642
Financing receivables, current portion	3,264,508	3,767,613
Inventories	1,593,305	1,703,668
Deferred tax assets	2,139,650	1,526,605
Prepaid income taxes		867,825
Prepaid expenses	844,438	705,481
Total current assets	47,644,361	45,673,715
Property and equipment		
Land	936,026	936,026
Maintenance equipment	4,145,141	3,819,469
Computer equipment	7,851,773	6,687,155
Leasehold improvements	3,042,211	963,211
Office furniture and equipment	2,817,543	1,516,376
Automobiles	158,042	132,926
	18,950,736	14,055,163
Less accumulated depreciation	(10,550,254)	(9,039,396)
Net property and equipment	8,400,482	5,015,767
Financing receivables, net of current portion	4,365,075	3,761,239
Total assets	$ 60,409,918	$ 54,450,721
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 3,641,080	$ 2,212,085
Deferred revenue	4,206,059	3,582,870
Accrued vacation	3,037,209	2,606,043
Income taxes payable	920,808	
Other accrued liabilities	4,222,913	2,846,349
Total current liabilities	16,028,069	11,247,347

Deferred tax liabilities	824,496	512,103
Stockholders equity:		
Common stock, par value $0.001 per share; 30,000,000 shares authorized; 10,962,874 and 10,972,757 shares issued and outstanding	10,963	10,973
Additional paid-in capital	30,333,864	29,679,385
Accumulated other comprehensive income	85,698	100,103
Retained earnings	13,126,828	12,900,810
Total stockholders equity	43,557,353	42,691,271
Total liabilities and stockholders equity	$ 60,409,918	$ 54,450,721

See accompanying notes.

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COMPUTER PROGRAMS AND SYSTEMS, INC.

CONDENSED STATEMENTS OF INCOME (Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Sales revenues:				
System sales	$ 17,481,708	$ 11,577,722	$ 42,048,829	$ 30,915,962
Support and maintenance	14,980,612	13,957,089	43,654,969	41,610,529
Business management services	8,450,902	7,473,192	24,464,020	21,464,551
Total sales revenues	40,913,222	33,008,003	110,167,818	93,991,042
Costs of sales:				
System sales	12,591,304	9,428,060	33,777,583	25,716,423
Support and maintenance	6,160,444	5,594,986	17,619,361	15,916,323
Business management services	5,104,340	4,372,072	13,919,487	12,611,736
Total costs of sales	23,856,088	19,395,118	65,316,431	54,244,482
Gross profit	17,057,134	13,612,885	44,851,387	39,746,560
Operating expenses:				
Sales and marketing	3,311,060	2,297,325	8,314,560	6,625,308
General and administrative	6,067,938	5,210,398	17,645,458	15,392,763
Total operating expenses	9,378,998	7,507,723	25,960,018	22,018,071
Operating income	7,678,136	6,105,162	18,891,369	17,728,489
Other income:				
Interest income	221,955	218,407	512,836	690,334
Total other income	221,955	218,407	512,836	690,334
Income before taxes	7,900,091	6,323,569	19,404,205	18,418,823
Income taxes	3,011,622	2,303,025	7,331,167	6,831,842
Net income	$ 4,888,469	$ 4,020,544	$ 12,073,038	$ 11,586,981
Net income per share - basic	$ 0.45	$ 0.37	$ 1.10	$ 1.06
Net income per share - diluted	$ 0.45	$ 0.37	$ 1.10	$ 1.06
Weighted average shares outstanding				
Basic	10,962,874	10,972,757	10,962,874	10,947,341
Diluted	10,962,874	10,972,757	10,962,874	10,949,239
Dividends declared per share	$ 0.36	$ 0.36	$ 1.08	$ 1.08

See accompanying notes.

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COMPUTER PROGRAMS AND SYSTEMS, INC.

CONDENSED STATEMENT OF STOCKHOLDERS EQUITY (Unaudited)

	Common Shares	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Retained Earnings	Total Stockholders Equity
Balance at December 31, 2009	10,972,757	$ 10,973	$ 29,679,385	$ 100,103	$ 12,900,810	$ 42,691,271
Net income					12,073,038	12,073,038
Forfeiture of restricted stock	(9,883)	(10)	10			
Unrealized loss on investments available for sale, net of tax				(14,405)		(14,405)
Stock-based compensation			643,324			643,324
Income tax benefit from dividends on restricted stock			11,145			11,145
Dividends					(11,847,020)	(11,847,020)
Balance at September 30, 2010	10,962,874	$ 10,963	$ 30,333,864	$ 85,698	$ 13,126,828	$ 43,557,353

See accompanying notes.

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COMPUTER PROGRAMS AND SYSTEMS, INC.

CONDENSED STATEMENTS OF CASH FLOWS (Unaudited)

	Nine months ended September 30, 2010	2009
Operating Activities		
Net income	$ 12,073,038	$ 11,586,981
Adjustments to net income:		
Provision for bad debt	406,408	747,943
Deferred taxes	(278,779)	(500,558)
Stock-based compensation	643,324	689,985
Excess tax benefit from stock option exercises		(418,830)
Income tax benefit from restricted stock dividends	(11,145)	
Depreciation	1,510,858	1,294,136
Changes in operating assets and liabilities:		
Accounts receivable	(5,652,830)	(4,305,921)
Financing receivables	(100,731)	(719,003)
Inventories	(215,308)	(322,308)
Prepaid expenses	(138,958)	(260,666)
Accounts payable	1,428,995	(905,915)
Deferred revenue	623,189	(391,529)
Other liabilities	1,807,731	(495,062)
Income taxes payable	1,799,778	124,711
Net cash provided by operating activities	13,895,570	6,123,964
Investing Activities		
Purchases of property and equipment	(4,569,902)	(1,385,976)
Sales of investments		1,500,000
Purchases of investments	(188,348)	(2,897,693)
Net cash used in investing activities	(4,758,250)	(2,783,669)
Financing Activities		
Proceeds from exercise of stock options		1,303,599
Income tax benefit from restricted stock dividends	11,145	
Excess tax benefit from stock option exercises		418,830
Dividends paid	(11,847,020)	(11,817,268)
Net cash used in financing activities	(11,835,875)	(10,094,839)
Decrease in cash and cash equivalents	(2,698,555)	(6,754,544)
Cash and cash equivalents at beginning of period	4,386,763	11,744,466
Cash and cash equivalents at end of period	$ 1,688,208	$ 4,989,922
Cash paid for interest	$	$
Cash paid for income taxes, net of refund	$ 5,751,143	$ 7,207,693
Reclassification of inventory to property and equipment	$ 325,671	$

See accompanying notes.

COMPUTER PROGRAMS AND SYSTEMS, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS (Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited condensed financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and include all adjustments that, in the opinion of management, are necessary for a fair presentation of the results of the periods presented. All such adjustments are considered of a normal recurring nature. Quarterly results of operations are not necessarily indicative of annual results.

Certain footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These unaudited condensed financial statements should be read in conjunction with the audited financial statements of Computer Programs and Systems, Inc. (the Company) for the year ended December 31, 2009 and the notes thereto contained in our Annual Report on Form 10-K for the year ended December 31, 2009.

2. REVENUE RECOGNITION

The Company recognizes revenue in accordance with accounting principles generally accepted in the United States of America, principally those required by the *Software* topic and *Revenue Recognition* subtopic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (the Codification) and those prescribed by the SEC.

The Company s revenue is generated from three sources:

- the sale of information systems, which includes software, conversion, installation and training services, hardware, peripherals, forms and supplies.

- the provision of system support services, which includes software application support, hardware maintenance, continuing education, application service provider (ASP) services hereinafter referred to as software as a service or (SAAS), and internet service provider (ISP) services.

- the provision of business management services, which includes electronic billing, statement processing, payroll processing and accounts receivable management.

The Company enters into contractual obligations to sell hardware, perpetual software licenses and conversion, installation, training and maintenance services. Revenue from hardware sales is recognized upon shipment, when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collection is probable. Revenue from the perpetual software licenses and installation and training services are recognized using the residual method. The residual method allocates an amount of the arrangement to the elements for which fair value can be determined and any remaining arrangement consideration (the residual revenue) is then allocated to the delivered elements. The fair value of maintenance services is determined based on vendor specific objective evidence (VSOE) of fair value and is deferred and recognized as revenue ratably over the maintenance term. VSOE of fair value of maintenance services is determined by reference to the price the Company s customers are required to pay for the services when sold separately via renewals. The residual revenue is allocated to the perpetual license and installation and training services and is recognized over the term that the installation and training services are performed for the entire arrangement. The method of recognizing revenue for the perpetual license for the associated modules included in the arrangement and related installation and training services over the term the services are performed is on a module by module basis as the respective installation and training for each specific module is completed as this is representative of the pattern of provision of these services. The installation and training services are normally completed in three to four weeks.

Revenue derived from maintenance contracts primarily includes revenue from software application support, hardware maintenance, continuing education and related services. Maintenance contracts are typically sold for a separate fee with initial contract periods ranging from one to seven years, with renewal for additional periods thereafter. Maintenance revenue is recognized ratably over the term of the maintenance agreement.

The Company accounts for SAAS contracts in accordance with the requirements of the *Hosting Arrangement* section under the *Software* topic and *Revenue Recognition* subtopic of the FASB Codification. The Codification states that the software element of SAAS services should not be accounted for as a hosting arrangement if the customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty and it is feasible for the customer to either run the software on its own hardware or contract with another party related to the vendor to host the software. Each SAAS contract includes a system purchase and buyout clause, and this clause specifies the total amount of the system buyout.

In addition, a clause is included in SAAS contracts which states that should the system be bought by the customer, the customer would be required to enter into a general support agreement (for post-contract support services) for the remainder of the original SAAS term. Accordingly, the Company has concluded that SAAS customers do not have the right to take possession of the system without significant penalty (i.e. the purchase price of the system), and thus SAAS revenue of the Company falls within the scope of the *Hosting Arrangement* section of the Codification. In accordance with SEC regulations, revenue is recognized when the SAAS services are performed.

Revenue for ISP and business management services are recognized in the period in which the services are performed.

3. OTHER ACCRUED LIABILITIES

Other accrued liabilities are comprised of the following:

	September 30, 2010	December 31, 2009
Salaries and benefits	$ 2,399,957	$ 1,378,473
Commissions	500,000	182,525
Self-insurance reserves	493,000	510,900
Unrecognized tax benefit	589,477	536,717
Other	240,479	237,734
	$ 4,222,913	$ 2,846,349

4. INVESTMENTS

The Company accounts for investments in accordance with FASB Codification topic, *Investments Debt and Equity Securities*. Accordingly, investments are classified as available-for-sale securities and are reported at fair value, with unrealized gains and losses excluded from earnings and reported in a separate component of stockholders equity. The Company s management determines the appropriate classifications of investments in fixed maturity securities at the time of acquisition and re-evaluates the classifications at each balance sheet date. The Company s investments in fixed maturity securities are classified as available-for-sale.

Investments are comprised of the following at September 30, 2010:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Short term investments (cash and accrued income)	$ 224,554	$	$	$ 224,554
Obligations of U.S. Treasury, U.S. government corporations and agencies	5,664,845	18,484	983	5,682,346
Mortgage backed securities	128,662	3,050		131,712
Corporate bonds	7,236,639	121,473	1,536	7,356,576
	$ 13,254,700	$ 143,007	$ 2,519	$ 13,395,188

Shown below are the amortized cost and estimated fair value of debt securities with fixed maturities at September 30, 2010, by contract maturity date. Actual maturities may differ from contractual maturities because issuers of certain securities retain early call or prepayment rights.

	Amortized Cost	Fair Value
Due in 2010	$ 1,582,654	$ 1,584,096
Due in 2011	4,362,145	4,412,165
Due in 2012	6,165,078	6,251,040
Due in 2013	1,016,161	1,016,176
Due thereafter	128,662	131,711
	$ 13,254,700	$ 13,395,188

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Investments were comprised of the following at December 31, 2009:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Short term investments (cash and accrued income)	$ 311,895	$	$	$ 311,895
Obligations of U.S. Treasury, U.S. government corporations and agencies	4,648,496	15,047	847	4,662,696
Mortgage backed securities	153,083	737		153,820
Corporate bonds	7,965,541	149,430	264	8,114,707
	$ 13,079,015	$ 165,214	$ 1,111	$ 13,243,118

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5. NET INCOME PER SHARE

The Company presents both basic and diluted earnings per share (EPS) amounts. Basic EPS is calculated by dividing net income by the weighted average number of common shares outstanding during the period presented. Diluted EPS amounts are based upon the weighted average number of common and common equivalent shares outstanding during the period presented. The Company used the treasury stock method to calculate the impact of outstanding stock options. Potentially dilutive shares for a period are derived from outstanding stock options that have an exercise price less than the weighted average market price of our common stock during such period. The difference between basic and diluted EPS is solely attributable to stock options. There were no dilutive shares for the three and nine month periods ended September 30, 2010 or the three month period ended September 30, 2009. There were 1,898 dilutive shares for the nine month period ended September 30, 2009.

6. INCOME TAXES

The Company accounts for income taxes in accordance with FASB s Codification topic, *Income Taxes*. Deferred income taxes arise from the temporary differences in the recognition of income and expenses for tax purposes. A valuation allowance is established when the Company believes that it is more likely than not that some portion of its deferred tax assets will not be realized. Deferred tax assets and liabilities are comprised of the following at September 30, 2010 and December 31, 2009:

	September 30, 2010	December 31, 2009
Deferred tax assets:		
Accounts receivable	$ 448,093	$ 296,194
Accrued vacation	1,184,511	1,027,065
Stock-based compensation	285,142	390,847
Other accrued liabilities	291,124	325,153
Total deferred tax assets	$ 2,208,870	$ 2,039,259
Deferred tax liabilities:		
Other comprehensive income	$ 42,128	$ 64,001
Depreciation	851,588	960,756
Total deferred tax liabilities	$ 893,716	$ 1,024,757

Significant components of the Company s income tax provision in the Condensed Statements of Income for the nine months ended September 30 are as follows:

	2010	2009
Current provision:		
Federal	$ 6,231,706	$ 5,889,245
State	1,378,240	1,443,155
Deferred benefit:		
Federal	(250,186)	(449,219)
State	(28,593)	(51,339)
Total income tax provision	$ 7,331,167	$ 6,831,842

The difference between income taxes at the U. S. federal statutory income tax rate of 35% and those reported in the Condensed Statements of Income for the nine months ended September 30 is as follows:

	2010	2009
Income taxes at U. S. Federal statutory rate	$ 6,787,972	$ 6,446,588
State income tax, net of federal tax effect	867,264	886,712
Impact of tax credits	(209,274)	(468,061)
Other	(114,795)	(33,397)
Total income tax provision	$ 7,331,167	$ 6,831,842

The federal returns for the tax years 2004, 2005, and 2006 are currently under examination by Internal Revenue Service, primarily in relation to research credits claimed on those returns by the Company. The federal returns for tax years 2007, 2008 and 2009 remain open to examination, and the tax years 2004 2009 remain open to other taxing jurisdictions to which the Company is subject. The Company had unrecognized tax benefits of $589,477 related to uncertain tax positions as of September 30, 2010 under the provisions of FASB Codification topic, *Income Taxes*, which is recorded in Other accrued liabilities on the Condensed Balance Sheet. No accrued interest or penalties for such positions is recorded. The tax provision for 2010 does not currently include the impact of certain tax credits that expired on December 31, 2009. These credits are currently up for renewal in Congress, and when passed may have a significant impact to our 2010 provision for income taxes.

7. STOCK BASED COMPENSATION

Effective January 1, 2006, the Company adopted the provisions of FASB Codification topic, *Compensation Stock Compensation,* which establishes accounting for stock-based awards exchanged for employee services. Accordingly, stock-based compensation cost is measured at the grant date based on the fair value of the award, and is recognized as an expense over the employee s requisite service period.

The following table shows total stock-based compen