VERAMARK TECHNOLOGIES INC
Form 10-Q
August 12, 2011

Table of Contents

FORM 10-Q
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

þ **Quarterly Report Under Section 13 or 15 (d)of the Securities Exchange Act of 1934**

or

o **Transition Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934**

For Quarter Ended June 30, 2011
Commission File Number 0-13898
Veramark Technologies, Inc.
(Exact name of registrant as specified in its charter)

Delaware	16-1192368
(State or other jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

1565 Jefferson Road, Suite 120 Rochester, NY 14623
(Address of principal executive offices)(Zip Code)
(585) 381-6000
(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 Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES þ NO o

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 (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES þ NO o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller Reporting Company þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES o NO þ

The number of shares of Common Stock, $.10 par value, outstanding on June 30, 2011 was 10,254,379.

INDEX

	Page
PART I FINANCIAL INFORMATION	
Item 1 Financial Statements	
Condensed Balance Sheets - June 30, 2011 (Unaudited) and December 31, 2010	3
Condensed Statements of Operations (Unaudited) Three and Six Months ended June 30, 2011 and 2010	4
Condensed Statements of Cash Flows (Unaudited) Six Months Ended June 30, 2011 and 2010	5
Notes To Condensed Financial Statements (Unaudited)	6 - 13
Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations	14 - 23
Item 3 Quantative and Qualitative Disclosures About Market Risk	23
Item 4 Controls and Procedures	23
PART II OTHER INFORMATION	
Item 1 Legal Proceedings	24
Item 1A Risk Factors	24 - 26
Item 5 Other Information	27
Item 6 Exhibit Index	27 - 28

Exhibit 10.12
Exhibit 10.13
Exhibit 10.14
Exhibit 10.15
Exhibit 31.1
Exhibit 31.2
Exhibit 32.1
Exhibit 32.2
EX-101 INSTANCE DOCUMENT
EX-101 SCHEMA DOCUMENT
EX-101 CALCULATION LINKBASE DOCUMENT
EX-101 LABELS LINKBASE DOCUMENT
EX-101 PRESENTATION LINKBASE DOCUMENT

Table of Contents

PART I FINANCIAL INFORMATION

VERAMARK TECHNOLOGIES, INC.
CONDENSED BALANCE SHEETS

	(Unaudited) June 30, 2011	December 31, 2010
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 466,269	$ 1,236,375
Investments	162,962	265,962
Accounts receivable, trade (net of allowance for doubtful accounts of $34,000 and $33,000)	2,034,510	1,911,693
Prepaid expenses	512,885	294,090
Other current assets	751,659	290,762
Total Current Assets	3,928,285	3,998,882
PROPERTY AND EQUIPMENT		
Cost	2,582,546	2,512,162
Less accumulated depreciation	(1,989,716)	(1,909,965)
Property and Equipment (net)	592,830	602,197
OTHER ASSETS:		
Software development costs (net of accumulated amortization of $2,748,444 and $2,245,268)	2,818,580	2,961,617
Pension assets	3,160,331	3,107,952
Intangibles, net	683,500	804,000
Goodwill	336,219	336,219
Deposits and other assets	1,104,374	1,062,152
Total Other Assets	8,103,004	8,271,940
TOTAL ASSETS	$ 12,624,119	$ 12,873,019
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 592,664	$ 360,382
Accrued compensation	572,870	667,062
Deferred revenue	4,494,439	4,250,933
Current portion of pension obligation	512,399	502,059
Contingent liability	447,040	899,400
Short term bank debt	66,667	246,667
Short term note payable	250,000	0
Other accrued liabilities	809,289	415,459
Total Current Liabilities	7,745,368	7,341,962

Long-Term debt	194,986	174,555
Long-Term portion of pension obligation	4,773,388	4,914,757
Total Liabilities	12,713,742	12,431,274
STOCKHOLDERS EQUITY:		
Common Stock, par value $.10; shares authorized, 40,000,000; 10,334,604 shares and 10,190,595 shares issued	1,033,460	1,019,059
Additional paid-in capital	22,743,591	22,661,405
Accumulated deficit	(23,186,330)	(22,568,440)
Treasury stock (80,225 shares, at cost)	(385,757)	(385,757)
Accumulated other comprehensive income	(294,587)	(284,522)
Total Stockholders Equity	(89,623)	441,745
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 12,624,119	$ 12,873,019

The accompanying notes are an integral part of these financial statements.

Table of Contents

VERAMARK TECHNOLOGIES, INC.
CONDENSED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	**2010**	**2011**	**2010**
NET REVENUES				
Product revenues	$ 466,999	$ 662,304	$ 841,569	$ 1,194,710
Service revenues	2,779,644	2,504,887	5,791,397	4,754,210
Total Net Revenues	3,246,643	3,167,191	6,632,966	5,948,920
COSTS AND OPERATING EXPENSES:				
Cost of revenues	1,095,775	892,088	2,177,388	1,628,146
Engineering and software development	293,120	374,752	600,747	694,791
Selling, general and administrative	1,817,367	1,778,243	3,642,502	3,454,587
Litigation expenses & settlement costs	723,937	0	862,995	0
Total Costs and Operating Expenses	3,930,199	3,045,083	7,283,632	5,777,524
INCOME (LOSS) FROM OPERATIONS	(683,556)	122,108	(650,666)	171,396
NET INTEREST INCOME	12,704	236	32,776	17,459
INCOME (LOSS) BEFORE TAXES	(670,852)	122,344	(617,890)	188,855
INCOME TAXES	0	0	0	0
NET INCOME (LOSS)	$ (670,852)	$ 122,344	$ (617,890)	$ 188,855
NET INCOME (LOSS) PER SHARE				
Basic	$ (0.07)	$ 0.01	$ (0.06)	$ 0.02
Diluted	$ (0.07)	$ 0.01	$ (0.06)	$ 0.02

The accompanying notes are an integral part of these financial statements.

Table of Contents

VERAMARK TECHNOLOGIES, INC.
CONDENSED STATEMENTS OF CASH FLOWS (Unaudited)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
OPERATING ACTIVITIES:		
Net income (loss)	$ (617,890)	$ 188,855
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	746,069	766,195
Increase in bad debt reserve	1,000	12,000
Change in acquisition liabilities	(152,360)	(6,980)
Compensation expense equity grants	9,573	60,327
Loss on disposal of fixed assets	0	989
Changes in assets and liabilities:		
Accounts receivable	(123,817)	(449,934)
Prepaid expenses and other current assets	(679,692)	49,159
Pension assets	(52,379)	(61,371)
Deposits and other assets	(42,222)	(42,222)
Accounts payable	232,282	20,056
Accrued compensation	(94,192)	200,574
Deferred revenue	243,506	(4,802)
Other accrued liabilities	392,401	(29,037)
Note payable	250,000	0
Prepaid rent liability	55,193	0
Pension obligation	(131,029)	(176,030)
Net cash provided (used) by operating activities	36,443	527,779
INVESTING ACTIVITIES:		
Acquisition cash paid	(300,000)	(300,000)
Sale of investments	92,935	(17,257)
Additions to property and equipment	(93,962)	(128,474)
Capitalized software development costs	(379,203)	(572,914)
Net cash flows used by investing activities	(680,230)	(1,018,645)
FINANCING ACTIVITY:		
Borrowing (repayment) line of credit	(180,000)	300,000
Bank borrowing repayment of term loan	(33,333)	0
Exercise of stock options	74,600	0
Employee stock purchase plan	12,414	13,282
Net cash provided by financing activities	(126,319)	313,282
Net change in cash and cash equivalents	(770,106)	(177,584)
Cash and cash equivalents, beginning of year	1,236,375	488,381
Cash and cash equivalents, end of quarter	$ 466,269	$ 310,797

CONDENSED STATEMENTS OF CASH FLOWS

	2011	2010
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash Transactions:		
Income taxes paid	$ 3,850	$ 1,850
Interest paid	$ 6,782	$ 1,650

The accompanying notes are an integral part of these financial statements.

Table of Contents

NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

(1) GENERAL

The accompanying unaudited financial statements include all adjustments of a normal and recurring nature which, in the opinion of Company s management, are necessary to present fairly the Company s financial position as of June 30, 2011, the results of its operations for the three and six months ended June 30, 2011 and 2010, and cash flows for the six months ended June 30, 2011 and 2010.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission. These condensed financial statements should be read in conjunction with the financial statements and related notes contained in the Company s Annual Report on Form 10-K to the Securities and Exchange Commission for the year ended December 31, 2010.

The results of operations and cash flows for the three and six months ended June 30, 2011 are not necessarily indicative of the results to be expected for the full year s operation. Certain prior period amounts have been reclassified to conform to the current period presentation.

(2) PROPERTY AND EQUIPMENT

The major classifications of property and equipment at June 30, 2011, and December 31, 2010 were:

	June 30, 2011	December 31, 2010
Machinery and equipment	$ 117,541	$ 117,541
Computer hardware and software	1,282,525	1,216,120
Furniture and fixtures	1,182,480	1,178,501
	$ 2,582,546	$ 2,512,162

For the six months ended June 30, 2011 and 2010, the Company recorded depreciation expense of $103,329 and $100,523, respectively.

(3) STOCK-BASED COMPENSATION

The Company s share-based compensation consists of restricted stock and stock options, vesting over periods ranging from one to four years. For the six months ended June 30, 2011, the Company awarded 290,375 stock options vesting over four years, canceled 38,500 stock options, and cancelled 53,333 restricted shares granted in previous periods. During the first six months of 2010, the Company awarded 23,000 stock options vesting over four years, cancelled 41,775 stock options, and cancelled 120,000 shares of restricted stock previously granted.

Table of Contents

A summary of the status of the Company s stock option plan as of June 30, 2011, is presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Grant-Date Fair Value	Average Remaining Contractual Term (Yrs)	Intrinsic Value
Outstanding as of December 31, 2010	1,557,768	$ 0.62	$ 0.58	4.1	$ 79,154
Granted	290,375	0.69	0.67		0
Exercised	(173,000)	0.43			(13,870)
Canceled	(38,500)	0.64			(2,618)
Outstanding as of June 30, 2011	1,636,643	$ 0.66	$ 0.61	5.0	$ 62,666
Options exercisable at June 30, 2011	1,279,143	$ 0.66	$ 0.61	3.8	$ 62,666

As of June 30, 2011, there was $156,607 of total unrecognized compensation cost related to non-vested stock options granted under the Plan, and $32,595 of unrecognized compensation cost related to non-vested restricted stock grants. The compensation cost for stock options will be recognized over a weighted-average period of 1.3 years. The compensation costs of restricted stock will be recognized over a weighted-average period of 0.9 years.

(4) COMPREHENSIVE INCOME

Total comprehensive income for the three and six months ended June 30 of 2011 and 2010 was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	**2010**	**2011**	**2010**
Net income (loss)	$ (670,852)	$ 122,344	$ (617,890)	$ 188,855
Unrealized change pension	0	(29,400)	0	(58,800)
Unrealized change investments	(5,221)	9,200	(10,065)	(4,347)
Total comprehensive income	$ (676,073)	$ 102,144	$ (627,955)	$ 125,708

(5) NET INCOME (LOSS) PER SHARE (EPS)

ASC 260-10 Earnings Per Share requires the Company to calculate net income (loss) per share based on basic and diluted net income (loss) per share, as defined. Basic EPS excludes dilution and is computed by dividing net income (loss) by the weighted average number of shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. The dilutive effect of outstanding options issued by the Company are reflected in diluted EPS using the treasury stock method. Under the treasury stock method, options will only have a dilutive effect when the average market price of common stock during the period exceeds the exercise price of the options.

Table of Contents

Calculations of Earnings (Loss) Per Share

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Basic				
Net Income (loss)	$ (670,852)	$ 122,344	$ (617,890)	$ 188,855
Weighted average common shares outstanding	10,183,547	9,954,770	10,138,204	9,891,749
Net Income (loss) per common share	$ (0.07)	$ 0.01	$ (0.06)	$ 0.02
Diluted				
Net Income (loss)	$ (670,852)	$ 122,344	$ (617,890)	$ 188,855
Weighted average common shares outstanding	10,183,547	9,954,770	10,138,204	9,891,749
Additional dilutive effect of stock options and warrants after application of treasury stock method	0	108,474	0	63,662
Weighted average dilutive shares outstanding	10,183,547	10,063,244	10,138,204	9,955,411
Net Income (loss) per common share assuming full dilution	$ (0.07)	$ 0.01	$ (0.06)	$ 0.02

There were no dilutive effects of stock options for the three and six months ended June 30, 2011 as the effect would have been anti-dilutive due to the net losses incurred for those periods.

(6) INDEMNIFICATION OF CUSTOMERS

Our agreements with customers generally require us to indemnify the customer against claims that our software infringes third party patent, copyright, trademark or other proprietary rights. Such indemnification obligations are generally limited in a variety of industry-standard respects, including our right to replace an infringing product. As of June 30, 2011 we had not experienced any material losses related to these indemnification obligations and no material claims with respect thereto were outstanding. We do not expect significant claims related to these indemnification obligations, and consequently, we have not established any related reserves.

(7) BENEFIT PLANS

The Company sponsors an employee incentive savings plan under Section 401(k) for all eligible employees. The Company s contributions to the plan are discretionary. During the first quarter of 2011 the Company contributed $26,589 to employee s 401(k) accounts. During the first quarter of 2010 the Company s contribution to employee 401(k) accounts totaled $24,644.

Table of Contents

The Company also sponsors an unfunded Supplemental Executive Retirement Program (SERP), which is a non-qualified plan that provides certain key employees defined pension benefits. Periodic pension expense for the three and six months ended June 30, 2011 and 2010 consists of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	**2010**	**2011**	**2010**
Interest Cost	60,000	41,901	120,000	133,800
Unrealized Actuarial Gain	0	(29,400)	0	(58,800)
Pension Expense	$ 60,000	$ 12,501	$ 120,000	$ 75,000

The Company paid pension obligations of $251,030 for both the six months ended June 30, 2011 and June 30, 2010.

The discount rate used in determining the actuarial present value of the projected benefit obligation was 5.0% for the six months ended June 30, 2011 and 5.5% for the six months ended June 30, 2010.

The Company maintains life insurance covering certain current and former employees under its Supplemental Executive Retirement Program with the Company named as beneficiary. The Company intends to use the death benefits of these policies, as well as loans against the accumulating cash surrender value of the policies, to fund future pension obligations. The total death benefit associated with these policies is $10.2 million, with an associated accumulated cash surrender value of approximately $3,160,000 at June 30, 2011. The accumulated cash surrender values of these policies at December 31, 2010 was approximately $3,108,000.

The projected pension benefits paid or expected to be paid under this plan are as follows, assuming retirement at 65 and a life expectancy of 80 years for all participants:

Period Ending December 31, Unless Stated Otherwise,	
Q3 - Q4 2011	251,030
2012	538,159
2013	558,660
2014	460,526
2015	418,926
2016 - 2020	2,401,241

Table of Contents

The Company has a contractual obligation to maintain certain health benefits for two of its former executive officers. These benefits are accounted for as Post Retirement Healthcare Benefits, (PRHB). Periodic PRHB expensed and paid for the three and six months ended June 30, 2011 and 2010 consists of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	**2010**	**2011**	**2010**
Current Service Cost	$ 2,252	$ 2,125	$ 4,505	$ 4,250
Interest Cost	1,160	1,287	2,319	2,574
PRHB Expense	$ 3,412	$ 3,412	$ 6,824	$ 6,824

The projected PRHB paid or expected to be paid are as follows:

Period Ending December 31, Unless Stated Otherwise,	
Q3 - Q4 2011	6,825
2012	13,649
2013	13,649
2014	10,149
2015	6,649
2016 - 2020	33,245

8. ACQUISITION

On June 18, 2010 we acquired the enterprise telecom expense management (TEM) consulting business of privately held Source Loop, LLC, based in Alpharetta, Georgia. The aggregate purchase price paid for those assets was up to $1.5 million, plus the issuance of up to 500,000 shares of Veramark s common stock. At closing, $300,000 in cash was paid and 100,000 shares of Veramark common stock were issued to the principals of Source Loop. In addition, Source Loop retained $300,000 in accounts receivable and cash on hand prior to the acquisition date, leaving contingent consideration of $900,000 and 400,000 shares of Veramark common stock that could be earned, subject to attaining certain revenue and employee retention parameters through December 31, 2011. Through June 30, 2011 we have paid the Principals of Source Loop $300,000 and issued 100,000 shares of common stock reflecting the attainment of 100% of the performance targets for 2010.

As of June 30, 2011, based on management s projections of actual performance against targets contained in the asset purchase agreement for 2011, the estimated remaining contingent liability is $447,000 in cash and common stock. Under the purchase method of accounting, the remaining contingent stock consideration (300,000 shares) is treated as a financial derivative, and recorded as a liability, as it does not have a fixed settlement provision. This liability will vary in a mark-to-market fashion with the value of the Company s stock, until the settlement amount is known. Increases in the Company s stock price will result in an accounting expense, and decreases in the Company s stock price will be recorded as income.

Table of Contents

The unaudited financial information in the table below summarizes the combined results of operations on a pro-forma basis, as if we had acquired Source Loop on January 1, 2010.

	Three Months Ended June 30,		**Six Months Ended June 30,**	
Unaudited (In 000s)	**2011**	**2010**	**2011**	**2010**
Revenue	$ 3,247	$ 3,735	$ 6,633	$ 6,916
Income (Loss)	$ (671)	$ 125	$ (618)	$ 168
Earnings Per Share	$ (0.07)	$ 0.01	$ (0.06)	$ 0.02

9. INTANGIBLE ASSETS AND GOODWILL

Under the purchase method of accounting, we allocated the fair value of the total consideration expected to be transferred, to the tangible and identifiable intangible assets acquired from Source Loop based on their estimated fair values on the date of acquisition. The fair values assigned to the identifiable intangible assets were based on estimates and assumptions determined by management. The table below summarizes the fair values assigned to the identifiable intangible assets by asset class at the time of acquisition, and the subsequent amortization through June 30, 2011 of those intangible assets.

Table of Contents

Amortization of Intangible Assets Acquired in Source Loop Acquisition
(In 000s except weighted ave life in years)

Intangible Asset Class	**Weighted Avg Life Years**	**FMV at Acquisition Date**	**Current Year Amortization**	**Accumulated Amortization at 6/30/11**	**Net Value by Asset Class at 6/30/11**
Customer Contracts	3	$ 526	$ 56	$ 134	$ 392
Customer Relationships	3	260	36	86	174
Key Employee Agreements	1	177	24	74	103
Other	1	30	4	15	15
Sub-Total Intangibles Subject to Amoritization	3	993	$ 120	$ 309	$ 684
Goodwill		336			
Total Intangible Assets Acquired		$ 1,329			

Expected Future Amoritzation

Intangible Asset Class	**Q3 - Q4**	**2012**	**2013**	**2014**	**2015**
Customer Contracts	$ 56	$ 88	$ 67	$ 60	$ 51
Customer Relationships	36	42	31	25	19
Key Employee Agreements	23	42	39	0	0
Other	5	5	3	1	0
Sub-Total Intangibles Subject to Amoritization	$ 120	$ 177	$ 140	$ 86	$ 70

Goodwill represents the excess of the purchase price paid over the fair value of assets acquired. Goodwill is not amortized and is subject to an impairment test conducted in December of each year, or more frequently if a change in circumstances or the occurrence of events indicates that potential impairment exists. Through June 30, 2011, there has been no impairment of goodwill associated with the Source Loop acquisition.

10. COMMITMENTS AND CONTINGENCIES

On June 16, 2011 the Company entered into a Nonexclusive Patent License and settlement agreement relating to an action brought by Asentinel LLC, against Veramark, AnchorPoint a division of MTS, and CASS Information Systems, alleging infringement of two patents held by Asentinel concerning systems and methods for identifying and processing billing exceptions in telecommunications invoices.

Table of Contents

Material terms of the agreement included:

Asentinel waived all claims for damages for prior infringement and agreed not to make claims for future infringement of its patents.

The Company agreed to pay Asentinel $500,000. Of that amount $250,000 was paid upon execution of the agreement, and $250,000 is payable without interest, on June 16, 2012, and is represented by the Company s promissory note

The lawsuit was dismissed against the Company.

A copy of that settlement agreement is attached to this report on Form 10-Q as Exhibit 10.14. A copy of the promissory note is attached as exhibit 10.15.

11. REVOLVING DEMAND NOTE AGREEMENT

On October 31, 2008, Veramark Technologies, Inc. entered into a Revolving Demand Note Agreement (the Agreement), effective as of October 31, 2008, with Manufacturers and Traders Trust Company (the Bank) to provide working capital in the ordinary course of business. This Agreement was amended in October 2010 increasing the amount available under the agreement from $400,000 to $750,000. At June 30, 2011, the Company did not have any outstanding balance under this Agreement.

The material terms of the Agreement include:

The maximum outstanding principal balance under the Agreement is Seven Hundred Fifty Thousand Dollars ($750,000).

Veramark may borrow under the Agreement, from time to time, an amount less than or equal to, but not greater than the available balance.

The outstanding principal balance will bear interest at a per annum rate equal to LIBOR rate plus 3.5% with a minimum rate of 4.0%.

The Bank may demand payment of the outstanding principal balance at any time.

12. TERM NOTE AGREEMENT

On October 29, 2010, the Company entered into an agreement with Manufacturers and Traders Trust Company to provide a three year term loan in the amount of $200,000, the proceeds of which were used to purchase furnishings and fixtures for the Company s new headquarters facility. The loan bears an interest rate of LIBOR plus 4.0%, with a minimum interest rate of 4.5%. At June 30, 2011, the remaining balance of the term loan was $155,556.

Table of Contents

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

Results of Operations

Management s Discussion and Analysis contains statements that are forward-looking. Such statements are identified by the use of words like plans, expects, intends, believes, will, anticipates, estimates and other wor meaning in conjunction with, among other things, discussions of future operations, financial performance, the Company s strategy for growth, product development, regulatory approvals, market position and expenditures. Forward-looking statements are based on management s expectations as of the date of this report. The Company cannot guarantee that any forward-looking statement will be accurate, although the Company believes that it has been reasonable in its expectations and assumptions. Forward-looking statements are subject to the risks identified in Issues and Risks and elsewhere in this report. Readers are cautioned not to place undue reliance on forward-looking statements and are advised to review the risks identified in Issues and Risks and elsewhere in this report. The Company has no obligation to update forward-looking statements.

Overview

Revenues of $3,247,000 for the second quarter ended June 30, 2011 increased 3% from revenues of $3,167,000 for the second quarter of 2010. For the six months ended June 30, 2011 revenues of $6,633,000 increased 11% from revenues of $5,949,000 for the first six months of 2010.

On June 16, 2011, the Company settled the patent litigation complaint brought by Asentinel LLC, which also named CASS Information Systems and AnchorPoint, a division of MTS, as defendants. The complaint alleged the infringement of two telecom expense management (TEM) patents held by Asentinel concerning systems and methods for identifying and processing billing exceptions in telecommunications invoices. Under the terms of the settlement, Veramark agreed to pay Asentinel $500,000 in return for a waiver of all known claims for past damages relating to any infringement of the Asentinel patents, and the lawsuit was dismissed. Of the settlement amount, $250,000 was paid on the date the agreement was reached, with the remaining $250,000 represented by a note payable with a maturity date of June 16, 2012. The entire $500,000 settlement, and legal fees of $224,000 pertaining to this action were charged to the Statement of Operations for the quarter ended June 30, 2011. Additionally, the Company expensed $139,000 of legal fees associated with this action in the first quarter of 2011.

As a result of the settlement agreement and associated legal fees, we incurred a net loss of $671,000, or $0.07 per share, for the quarter ended June 30, 2011, and a net loss of $618,000, or $0.06 per share for the six months ended June 30, 2011. This compares with net income of $122,000 and $189,000, respectively, for the three and six months ended June 30, 2010.

Non-GAAP Financial Measures

Absent the settlement and litigation costs referenced above, Veramark would have earned net income of $53,000 for the second quarter of 2011 and $245,000 for the six months ended June 30, 2011, as depicted in the table below.

Reconcilation of GAAP Net Income to Non-GAAP Net Income

Unaudited (In 000s)	Q-1 2011	Q-2 2011	Six Months Ended June 2011
GAAP Net Income (Loss)	$ 53	$ (671)	$ (618)
Legal Expenses	139	224	363
Settlement Amount	0	500	500
Adjusted Net Income (Non-GAAP)	$ 192	$ 53	$ 245
Fully Diluted EPS (Non-GAAP)	$ 0.02	$ 0.00	$ 0.02

	Q-1 2010	Q-2 2010	Six Months Ended June 2011
GAAP Net Income	$ 67	$ 122	$ 189
Fully Diluted EPS	$ 0.01	$ 0.01	$ 0.02

Orders booked for the quarter ended June 30, 2011 of $3.8 million increased 58% from $2.4 million for the same quarter of 2010. Orders booked for the six months ended June 30, 2011 of $8.0 million, increased 48% from orders of $5.4 million for the first six months of 2010. Embedded revenues, which represent our backlog of orders for products and services to be provided in future periods, has increased 10% from the December 31, 2010 total of $9.6 million to $10.7 million at June 30, 2011.

Revenues

The majority of our revenues are earned by providing Telecom Expense Management (TEM) products and services, including call accounting, either through the direct sale of licensed software, or under managed service contracts offered in either a Software as a Service (SaaS), or a hosted managed service environment. For the three and six months ended June 30, 2011, revenues from managed service contracts and related TEM services increased 27% and 52%, respectively, from the same three and six month periods of 2010. Revenues from the direct sale of licensed software and the associated services, including maintenance revenues on our installed base, decreased 7% for the three months ended June 30, 2011 and 4% for the six months ended June 30, 2011, when compared to the same three and six month periods of 2010.

Gross Margin

Gross margin (defined as revenues less cost of revenues) totaled $2,151,000 for the three months ended June 30, 2011, representing 66% of revenues, and $4,456,000 for the six months ended June 30, 2011, representing 67% of revenues. For the same three and six months ended June 30, 2010, gross margins were $2,275,000, (72% of revenues) and $4,321,000, (73% of revenues). The reduction in gross margins as a percentage of revenues for 2011 when compared with prior year results reflects a growing percentage of managed service revenues and associated expenses in the product mix. Margins earned from multi-year managed service contracts are lower as a percentage of revenues than revenues earned from the one-time sales of a software license, which typically provide greater revenues and margin dollars over the life of the contract.

Table of Contents

Engineering and Software Development Costs

Engineering and software development expenses, net of development costs capitalized, decreased $82,000, or 22% for the three months ended June 30, 2011 and $94,000, or 14%, for the six months ended June 30, 2011, as compared with the same periods of 2010. The reduction in engineering and software development costs on a gross basis, prior to the capitalization of development costs, totaled 24% and 23%, respectively, for the three and six months ended June 30, 2011, as compared with the same periods of 2010. The table below summarizes for the three and six months ended June 30, 2011 and 2010, total gross costs for engineering and software development, costs capitalized , and the resulting net expense for engineering and software development costs included in the Statement of Operations.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Gross expenditures for engineering & software development	$ 493,000	$ 645,000	$ 980,000	$ 1,268,000
Less: Software development costs capitalized	(200,000)	(270,000)	(379,000)	(573,000)
Net expense for engineering and software development	$ 293,000	$ 375,000	$ 601,000	$ 695,000

Selling, General, and Administrative Costs

SG&A expenses of $1,817,000 for the three months ended June 30, 2011, and $3,643,000 for the six months ended June 30, 2011, increased 2% and 5%, respectively, from SG&A expenses of $1,778,000 and $3,455,000 for the three and six months ended June 30, 2010. The increase in costs through June 30, 2011 from the prior year, reflect higher selling expenses, primarily the result of increased travel costs and commissions, combined with an increase in administration costs for additional salary expense associated with the June 2010 acquisition of Source Loop LLC.

Liquidity and Capital Resources

Our total cash position (cash plus short term investments) at June 30, 2011 of $629,000 compares with a total cash position of $1,502,000 at December 31, 2010. The decrease of $873,000 is attributable to settlement of the patent infringement law suit and related legal fees, a $300,000 payment in connection with the 2010 acquisition of Source Loop, and the repayment of $180,000 of net borrowing against the Company s line of credit agreement. As of June 30, 2011 we have no outstanding balance against our line of credit agreement, which provides for up to $750,000 of working capital.

The accounts receivable balance of $2,035,000 at June 30, 2011, increased 6% from the December 31, 2010 balance of $1,912,000. The reserve for bad debts of $34,000 at June 30, 2011 remains relatively unchanged from the December 31, 2010 reserve of $33,000.

Table of Contents

Prepaid expenses have increased 74% from the December 31, 2010 balance of $294,000 to $513,000 at June 30, 2011. The increase includes the renewal of several key business insurance policies, and the purchase and renewal of various software licenses and email upgrades utilized within the Company s internal network infrastructure.

Other current assets of $752,000 at June 30, 2011 include $733,000 of funds held by the Company on behalf of clients for whom we provide bill payment services as a component of their managed service agreements. This same amount is included in other accrued liabilities, offsetting the asset.

For the six months ended June 30, 2011 we have purchased $94,000 of capital equipment, a decrease of 27% from capital purchases of $128,000 for the same six months of 2010. Depreciation expense totaled $103,000 for the six months ended June 30, 2011, which compared with depreciation expense of $101,000 for the first six months of 2010.

Software development cost capitalized and included in the balance sheet at June 30, 2011 of $2,819,000 decreased 5% from $2,962,000 at December 31, 2010. For the six months ended June 30, 2011 we capitalized $379,000 of software development costs, or 34% less than the $573,000 of software development costs capitalized in the first six months of 2010. Amortization of previously capitalized development costs, which are charged to cost of revenues, totaled $522,000 for the first six months of 2011. For the same six months of 2010, amortization expense totaled $639,000.

Pension assets of $3,160,000 at June 30, 2011 increased $52,000 from $3,108,000 at December 31, 2010, and represent the accumulated cash surrender values of a series of company-owned life insurance policies intended to fund current and future pension obligations. These cash surrender values may also be utilized to fund current operations if required.

The intangible asset of $684,000 represents management s estimate, as of June 30, 2011, of the unamortized fair market value of the assets acquired from Source Loop in June 2010. The assets acquired continue to perform as contemplated at the date of acquisition, and the current expectation is that amortization will approximate $60,000 per quarter for the balance of 2011.

Current liabilities increased $403,000, or 5%, from the December 31, 2010 total of $7,342,000 to $7,745,000 at June 30, 2011, which includes an increase of $456,000 in funds held on behalf of clients utilizing our bill pay services referenced above. The increase in accounts payable of $232,000 from December 31, 2010 to June 30, 2011 is attributable to legal fees incurred in connection with the patent infringement litigation discussed earlier. Deferred revenue, which forms a portion of the embedded revenues discussed in the overview section of this report, increased 6% from the December 31, 2010 balance of $4,250,000 to $4,494,000 at June 30, 2011. Deferred revenues consist of the unrecognized portion of customer orders for services such as training, installation and maintenance that will be performed in future periods and recognized as revenue at that time.

The contingent liability of $447,000 at June 30, 2011, is our estimate of the remaining consideration to be paid in cash and common stock, in connection with the acquisition of the assets of Source Loop in June 2010. The final amount paid will be dependent upon the achievement of specific revenue goals contained in the asset purchase agreement. In July 2011, $150,000 of the remaining estimated liability will be paid based on employee retention goals included in the asset purchase agreement as measured at June 30, 2011.

Table of Contents

Long-term liabilities at June 30, 2011 include $89,000 for the non-current portion of a three year term note used to purchase office equipment and other furnishings in the fourth quarter of 2010, and a long-term rent liability of $106,000 associated with the lease of our current facility, which provided a five month rent-free period at inception. Accounting rules require that rent expense for operating leases with rent-free periods or tiered monthly payments be accounted for on a straight line basis over the lease term (7 years), including the related rent free period. Our balance sheet will therefore include a lease liability over the term of the lease equal to the difference between the amount of rent expense recognized and the amount of rent paid through the reporting period.

Due to the loss incurred in the second quarter, equity decreased from $442,000 at December 31, 2010, to a negative $90,000 at June 30, 2011. During the first six months of 2011, 173,000 stock options have been exercised and 24,000 shares of common stock purchased by employees via the Company s employee stock purchase plan, yielding proceeds to the company of $87,000.

Despite the loss incurred in the second quarter of 2011 resulting from the settlement of the litigation, it is management s opinion that in light of current cash and investment positions, a fully available line of credit agreement in place, and access to other sources of capital, that more than sufficient resources exist to fully fund operations for the next twelve months and beyond.

Table of Contents

Accounting Pronouncements

In October 2009, the FASB issued Accounting Standards Update No. 2009-13, *Multiple-Deliverable Revenue Arrangements,* which amends existing revenue recognition accounting pronouncements that are currently within the scope of FASB Codification Subtopic 605-25 (previously included within EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*, or EITF 00-21). The consensus to EITF Issue No. 08-01, *Revenue Arrangements with Multiple Deliverables*, or EITF 08-01, provides accounting principles and application guidance on whether multiple deliverables exist, how the arrangement should be separated, and the consideration allocated. This guidance eliminates the requirement to establish the fair value of undelivered products and services and instead provides for separate revenue recognition based upon management s estimate of the selling price for an undelivered item when there is no other means to determine the fair value of that undelivered item. EITF 00-21 previously required that the fair value of the undelivered item be the price of the item either sold in a separate transaction between unrelated third parties or the price charged for each item when the item is sold separately by the vendor. This was difficult to determine when the product was not individually sold because of its unique features. Under EITF 00-21, if the fair value of all of the elements in the arrangement was not determinable, then revenue was deferred until all of the items were delivered or fair value was determined. This new approach is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. This update does not have a material effect on the Company s financial statements.

In January 2010, the FASB issued Accounting Standards Update No. 2010-06, topic 820, *Fair Value Measurements and Disclosures*, which amends existing fair value disclosure pronouncements. This update provides amendments to Subtopic 820-10 that require new disclosures as follows:

1. Transfers in and out of Levels 1 and 2. A reporting entity should disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers.

2. Activity in Level 3 fair value measurements. In the reconciliation for fair value measurements using significant unobservable inputs (Level 3), a reporting entity should present separately information about purchases, sales, issuances, and settlements (that is, on a gross basis rather than as one net number).

This update also provides amendments to Subtopic 820-10 that clarify existing disclosures as follows:

1. Level of disaggregation. A reporting entity should provide fair value measurement disclosures for each class of assets and liabilities. A class is often a subset of assets or liabilities within a line item in the statement of financial position. A reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities.
2. Disclosures about inputs and valuation techniques. A reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements. Those disclosures are required for fair value measurements that fall in either Level 2 or Level 3.

Table of Contents

This update also includes conforming amendments to the guidance on employers disclosures about postretirement benefit plan assets (Subtopic 715-20). The conforming amendments to Subtopic 715-20 change the terminology from *major categories* of assets to *classes* of assets and provide a cross reference to the guidance of Subtopic 820-10 on how to determine appropriate classes to present fair value disclosures.

This update is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. This update does not have a material effect on the Company s financial statements.

In April 2010, the FASB issued Accounting Standards Update No. 2010-13, topic 718, *Compensation Stock Compensation*, which adds clarification that an employee share-based award with an exercise price denominated in the currency of a market in which a substantial portion of the entity s equity securities trades should not be considered to contain a condition that is not a market, performance, or service condition. Therefore, an entity would not classify such an award as a liability if it otherwise qualifies as an equity. This update is effective for fiscal years, and interim periods within those fiscal years beginning on or after December 15, 2010. This update does not have a material effect on the Company s financial statements.

In April 2010, the FASB issued Accounting Standards Update No. 2010-17, topic 605, *Revenue Recognition Milestone Method*, which provides guidance on the criteria that should be met for determining whether the milestone method of revenue recognition is appropriate. A vendor can recognize consideration that is contingent upon achievement of a milestone in its entirety as revenue in the period in which the milestone is achieved only if the milestone meets all criteria to be considered substantive. This update is effective on a prospective basis for milestones achieved in fiscal years, and interim periods within those years, beginning on or after June 15, 2010. This update does not have a material effect on the Company s financial statements.

In July 2010, the FASB issued Accounting Standards Update No. 2010-20, topic 310, *Receivables*, which requires disclosures about the credit quality of financing receivables and the allowance for credit losses. The disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. This update does not have a material effect on the Company s financial statements.

In December 2010, the FASB issued Accounting Standards Update No. 2010-28, topic 350, *When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts.* For those reporting units with zero or negative carrying value, step 2 of the impairment test is required to be performed, even if step 1 indicates it is not necessary. This update does not have a material effect on the Company s financial statements.

In December 2010, the FASB issued Accounting Standards Update No. 2010-29, topic 805, *Disclosure of Supplementary Pro Forma Information for Business Combinations*, to clarify diversity in practice of applying this topic. Paragraph 805-10-50-2(h) requires a public entity to disclose pro forma information for business combinations that occurred in the current reporting period. The disclosures include pro forma revenue and earnings of the combined entity for the current reporting period as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual reporting period. If comparative financial statements are presented, the pro forma revenue and earnings of the combined entity for the comparable prior reporting period should be reported as though the acquisition date for all business combinations that occurred during the current year had been as of the beginning of the comparable prior annual reporting period. The Company properly reports such supplementary information in its filings.

In May 2011, the FASB issued Accounting Standards Update No. 2011-04, topic 820, *Fair Value Measurement*, to improve the comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with United States GAAP and International Financial Reporting Standards. Some of the amendments clarify the Board s intent about the application of existing fair value measurement requirements. Other amendments change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. Specifically, the guidance requires additional disclosures for fair value measurements that are based on significant unobservable inputs. The updated guidance is to be applied prospectively and is effective for the Company s interim and annual periods beginning January 1, 2012. The adoption of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

In June 2011, the FASB issued Accounting Standards Update No. 2011-05, topic 220, *Comprehensive Income.* The objective of this Update is to improve the comparability, consistency, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. To increase the prominence of items reported in other comprehensive income and to facilitate convergence of U.S. generally accepted accounting principles (GAAP) and International Financial Reporting Standards (IFRS), the FASB decided to eliminate the option to present components of other comprehensive income as part of the statement of changes in stockholders equity, among other amendments in this Update.

The amendments require that all non-owner changes in stockholders equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-statement approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. The amendments in this Update should be applied retrospectively, and are effective for the Company s interim and annual periods beginning after December 15, 2011. The Company does not expect this update to have a material effect on the Company s financial statements.

Critical Accounting Policies

The preparation of financial statements requires management to make estimates and assumptions that affect amounts reported therein. The most significant of these involves difficult or complex judgments as described below. In each situation, management is required to make estimates about the effects of matters or future events that are inherently uncertain.

Revenue Recognition

The Company s revenue consists of revenues from the licensing of software to resellers and end user customers; fees for services rendered including installation, training, implementation, and customer maintenance contracts; and the outsourcing or hosting of services, commonly referred to as Software as a Service (SaaS).

The Company recognizes software license revenue under ASC 985-605, formerly Statement of Position No 97-2 Software Revenue Recognition , Statement of Position No. 98-9, Software Revenue Recognition With Respect to Certain Transactions , and under ASC 605-25, formerly Emerging Issues Task Force 00-21, Revenue Arrangements with Multiple Deliverables , and related interpretations, as amended.

Licensed software may be sold as a stand-alone element, with other software elements, or in conjunction with supplemental services. When an order consists of more than one element, it is considered to be a multiple element arrangement (MEA). When sold as a stand-alone element, the revenue is recognized upon shipment. When sold as part of a MEA, revenue from the licensed software is recognized when each element is activated at the customer site, via the entry of a software key-code. This typically occurs at the same time that installation occurs. Service revenues such as training, installation and implementation, are recognized when the service is complete, and acknowledged by the customer.

For either a single element transaction or a MEA, Veramark allocates consideration to all deliverables based on their relative stand-alone selling prices. Amendments to ASC 605-25, which became effective January 1, 2011, establish a hierarchy to determine the stand-alone selling price as follows:

- Vendor Specific Objective Evidence of the fair value (VSOE),
- Third Party Evidence (TPE)
- Best Estimate of the Selling Price (ESP)

Sales which constitute a MEA are accounted for by determining if the elements can be accounted for as separate accounting units, and if so, by applying values to those units, per the hierarchy above. If VSOE is not available, management estimates the fair selling price using historical pricing for similar items, in conjunction with current pricing and discount policies.

Regardless of the form of sale, no revenue is recognized without persuasive evidence of an arrangement existing. Persuasive evidence is determined to be a signed purchase order received from the customer, or an equivalent form for those customers lacking a formalized purchase order system. Additionally, revenue is only recognized when a selling price is fixed or determinable, and collectability of the receivable is deemed to be probable.

Fees charged to customers for post-contract Technical Support are recognized ratably over the term of the contract. Costs related to maintenance obligations are expensed as incurred.

The Company s revenues generated through hosting solutions are recognized using the proportional performance method. Revenues are recognized in the month services are rendered and earned under service agreements with clients where service fees are fixed or determinable. Contracts can be terminated with 90 days written notice. All services provided by the Company through the date of cancellation are due and payable under the contract terms.

The Company believes its revenue recognition policies are appropriate, in all circumstances, and that its policies are reflective of complexities arising from customer arrangements involving such features as maintenance, warranty agreements, license agreements, and other normal course of business arrangements.

Capitalization of Software Development

The Company capitalizes software development costs when technological feasibility has been established for the software in accordance with ASC 985-20, Costs of to be Sold, Leased, or Marketed. Such capitalized costs are amortized on a product-by-product basis over their economic life or the ratio of current revenues to current and anticipated revenues from such software, whichever provides the greater amortization. The Company periodically reviews the carrying value of capitalized software development costs and impairments are recognized in the results of operations when the expected future undiscounted operating cash flow derived from the capitalized software is less than its carrying value. Should the Company inaccurately determine when a product reaches technological feasibility or the economic life of a product, results could differ materially from those reported. The Company uses what it believes are reasonable assumptions and where applicable, established valuation techniques in making its estimates.

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the potential inability of its customers to make required payments. Management specifically analyzes accounts receivable, historical bad debts, credit concentrations and customer payment terms when evaluating the adequacy of the allowance for doubtful accounts.

Pension Liability

The Company sponsors an unfunded Supplemental Executive Retirement Program (SERP), which is a nonqualified plan that provides certain key employees a defined pension benefit. In order to properly record the net present value of future pension obligations a number of assumptions are required to be made by Company s management. These assumptions include years of service, and life expectancies. In addition, management must make assumptions with regard to the proper long-term interest and liability discount rates to be applied to these future obligations.

Should the Company need to alter any of these assumptions, there is the potential for significant adjustments to future projected pension liabilities.

Item 3 Quantitative and Qualitative Disclosures About Market Risk

On October 29, 2010 the Company entered into an agreement with Manufacturers and Traders Trust Company to provide a three year term note in the amount of $200,000, the proceeds of which were used to purchase furnishings and fixtures for the Company s new headquarters facility. The loan bears an interest rate of LIBOR plus 4.0%, with a minimum interest rate of 4.5%. At June 30, 2011 the remaining balance of the term loan was $155,556.

Item 4 Controls and Procedures

Based upon an evaluation as of the end of the period covered by this report, the Company s Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported, within the time periods specified in the SEC s rules and forms and (ii) accumulated and communicated to the Company s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. There have been no changes in the Company s internal controls over financial reporting, that occurred during the period covered by this report, that have materially affected, or are reasonably likely to materially affect the Company s internal controls over financial reporting.

The Company s disclosure controls and procedures and internal controls over financial reporting provide reasonable, but not absolute, assurance that all deficiencies in design or operation of those control systems, or all instances of errors or fraud, will be prevented or detected. Those control systems are designed to provide reasonable assurance of achieving the goals of those systems in light of the Company s resources and nature of the Company s business operations. The Company s disclosure controls and procedures and internal control over financial reporting remain subject to risks of human error and the risk that controls can be circumvented for wrongful purposes by one or more individuals in management or non-management positions.

Table of Contents

PART II OTHER INFORMATION

Item 1 Legal Proceedings

On June 16, 2011 the Company entered into a Nonexclusive Patent License and settlement agreement relating to an action brought by Asentinel LLC, against Veramark, AnchorPoint a division of MTS, and CASS Information Systems, alleging infringement of two patents held by Asentinel concerning systems and methods for identifying and processing billing exceptions in telecommunications invoices.

Material terms of the agreement included:

Asentinel waived all claims for damages for prior infringement and agreed not to make claims for future infringement of its patents.

The Company agreed to pay Asentinel $500,000. Of that amount $250,000 was paid upon execution of the agreement and $250,000 is payable ,without interest on June 16, 2012 and is represented by the Company s promissory note

The lawsuit was dismissed against the Company.

A copy of that settlement agreement is attached to this report on Form 10-Q as Exhibit 10.14. A copy of the promissory note is attached as exhibit 10.15.

Item 1A Risk Factors

The following factors, among others discussed herein and in the Company s filings under the Act, could cause actual results and future events to differ materially from those set forth or contemplated in this report: economic, competitive, governmental and technological factors, increased operating costs, failure to obtain necessary financing, risks related to natural disasters and financial market fluctuations. Such factors also include:

Intellectual Property Rights

Veramark regards its products as proprietary and attempts to protect them with a combination of copyright, trademark and trade secret protections, employee and third-party non-disclosure agreements and other methods of protection. Despite those precautions, it may be possible for unauthorized third parties to copy certain portions of Veramark s products, reverse engineer or obtain and use information that Veramark regards as proprietary. The laws of some foreign countries do not protect Veramark s proprietary rights to the same extent as the laws of the United States. Any misappropriation of Veramark s intellectual property could have a material adverse effect on its business and results of operations. Furthermore, although Veramark takes steps to prevent unlawful infringement of other s intellectual property, there can be no assurance that third parties will not assert infringement claims against Veramark in the future with respect to current or future products. Any such assertion could require Veramark to enter into royalty arrangements or result in costly litigation.

Existing Customer Base

We derive a significant portion of our revenues from multi-year Managed Service contracts. As a result, if we lose a major customer, or if a Managed Service contract is delayed, reduced, or cancelled, our revenues could be adversely affected. In addition, customers who have accounted for significant revenues in the past may not generate the same amount of revenues in future periods.

Table of Contents

Product Development

Veramark has made significant investments in research, development and marketing for new products, services and technologies, including the VeraSMART software offering and its hosted or managed solutions. Significant revenue from new product and service investments may not be achieved for a number of years, if at all. Moreover, if such products or services are profitable, operating margins may not be as high as the margins historically experienced by Veramark. The development of software products is a complex and time-consuming process. New products and enhancements to existing products can require long development and testing periods. Significant delays in new product releases or significant problems in creating new products, particularly any delays in future releases of the VeraSMART suite of products or services, could adversely affect Veramark revenues.

Declines in Demand for Software

If overall market demands for software and computer devices generally, as well as call accounting software or enterprise level products and services specifically, declines, or corporate spending for such products declines, Veramark s revenue could be adversely affected. Additionally, Veramark s revenues could be unfavorably impacted if customers reduce their purchases of new software products or upgrades to existing products.

Competition

Veramark experiences intense competition across all markets for its products and services. Some competing firms have greater name recognition and more financial, marketing and technological resources than Veramark. These competitive pressures may result in decreased sales volumes, price reductions, and/or increased operating costs, such as for marketing and sales incentives, resulting in lower revenues, gross margins and operating income.

Marketing and Sales

Veramark s marketing and distribution strategy is founded on building mutually beneficial relationships with companies that have established distribution networks. Some sell privately labeled, customized products developed and manufactured by Veramark to their specific specifications, while others resell Veramark s products. Any loss of the continued availability of those relationships could have a material adverse effect on Veramark s business and results of operations.

Security and Privacy Breaches in our Systems May Damage Client Relations and Inhibit our Growth

The uninterrupted operation of our hosted solutions and the confidentiality of third party information that resides on our systems is critical to our business. We have what we believe to be sufficient security in place to prevent major interruptions in service and to prevent unauthorized access. Any failure in our security and privacy measures could have a material adverse impact on our financial position and results of operations.

Loss of Key Employees

Veramark s delivery of quality products and services requires the experience and knowledge of our staff. The loss of key employees could hinder our ability to deliver services, possibly resulting in loss of customers or loss of revenue. Any loss of key employees could have a material adverse effect on Veramark s business and results of operations.

Changing Market

Veramark serves the highly dynamic telecommunications market, which is characterized by continuous technological enhancements and choices that effect the costs incurred versus benefit received by our customers. Veramark staff must remain current otherwise the quality and value of our services could be diminished and competition could offer better value. The failure to remain current could have a material adverse effect on Veramark s business and results of operations.

Table of Contents

Access to Capital

Veramark may not have the access to capital that will be necessary to maintain competitive products, to hire the experienced staff, to fund growth or to fund acquisitions. This could cause Veramark to fall behind market growth rates and have an adverse effect on Veramark s business.

Public Company

Veramark is one of only a few TEM companies that has a publicly traded stock. In addition, Veramark s revenue is small relative to most public companies and the cost of compliance is relatively high when compared with revenue and earnings. This reduces the capital available to run operations and to invest in innovation which could have an adverse effect on business.

Stock Price Volatility

The acquisition of Source Loop has resulted in a contingent liability, comprised in part by shares of Company stock that may be issued in the future, as partial consideration of the acquisition. The value of the stock liability could vary based upon several factors, including changes in the Company s stock price through December 31, 2011. Under ASC 805, the Company is required to record the change in the value of the stock liability, if any, through the Statement of Operations.

Table of Contents

Item 5: Other Information

None

Item 6: Exhibits

(a) Financial Statements as set forth under Item 1 of this report on Form 10-Q

(b) Exhibits required to be filed by Item 601 of Regulation S-K

3.1	Restated Certificate of Incorporation (incorporated by reference to Exhibit 4.1 to the Company s Registration Statement on Form S-18 (File No. 2-96787) filed on March 22, 1985)
3.2	Bylaws (incorporated by reference to Exhibit 3 to the Company s Registration Statement on Form S-8 filed on October 5, 1992)
10.1	Letter Agreement dated as of March 29, 2007 by and between the Company and David G. Mazzella (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on April 3, 2007)
10.2*	Amended and Restated Board of Directors Deferred Compensation Plan (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on November 26, 2007)
10.3*	Employment Agreement dated as of December 17, 2007 by and between the Company and Anthony C. Mazzullo (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on December 19, 2007)
10.4*	Restricted Stock Award Agreement dated as of January 1, 2008 by and between the Company and Anthony C. Mazzullo (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on March 25, 2008)
10.5*	2008 Incentive Plan for Management and Key Employees (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on April 2, 2008)
10.6*	2008 Employee Stock Purchase Plan (incorporated by reference to Exhibit F to the Company s Proxy Statement for its 2008 Annual Meeting of Shareholders filed on April 29, 2008)
10.7*	Description of non-employee director compensation (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on August 18, 2008)
10.8*	Amended Salary Continuation Agreement dated as of October 10, 2008 by and between the Company and Ronald C. Lundy (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on October 17, 2008)
10.9*	Form of 2008 Employee Stock Purchase Plan Enrollment Agreement (incorporated by reference to Exhibit 4.2 to the Company s Registration Statement on Form S-8 (File No. 333-155286) filed on November 12, 2008)
10.10*	2010 Bonus Compensation Plan dated as of March 1, 2010 by and between the Company and Anthony C. Mazzullo (incorporated by reference to Exhibit 10.1 to the Company s Current Report on Form 8-K filed on March 5, 2010)

27

Table of Contents

10.11*	2010 Incentive Plan for Management and Key Employees (incorporated by reference to Exhibit 10.2 to the Company s Current Report on Form 8-K filed on March 5, 2010)
10.12*	Amendment to Employee Agreement between Josh Bouk and the Company, dated March 31, 2011.
10.13*	Amendment to Employee Agreement between Thomas McAlees and the Company, dated March 31, 2011.
10.14	Nonexclusive Patent License and Settlement Agreement between Asentinel LLC and the Company, dated June 16, 2011.
10.15	Promissory Note between Asentinel LLC and the Company, dated June 16, 2011.
14	Code of Business Conduct and Ethics (incorporated by reference to Exhibit E to the Company s Proxy Statement for its 2011 Annual Meeting of Shareholders filed on April 14, 2011)
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 Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Management contract or compensatory plan or arrangement

(c) Schedules required to be filed by Regulation S-X

none

All other schedules are omitted because they are not applicable or the required information is shown in the financial statements or notes thereto.

Table of Contents

SIGNATURES

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

VERAMARK TECHNOLOGIES, INC.
REGISTRANT

Date: August 12, 2011

/s/ Anthony C. Mazzullo

Anthony C. Mazzullo
President and CEO

Date: August 12, 2011

/s/ Ronald C. Lundy

Ronald C. Lundy
Vice President of Finance and CFO