DCAP GROUP INC
Form 10-Q
November 14, 2008

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

(Mark one)

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2008
OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _________to _________

Commission File Number 0-1665

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

Delaware	36-2476480
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

1158 Broadway
Hewlett, NY 11557
(Address of principal executive offices)
(516) 374-7600

(Registrant’s telephone number, including area code)

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filero	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company þ

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

As of November 14, 2008, there were 2,972,746 shares of the registrant’s common stock outstanding.

DCAP GROUP, INC.
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Forward-Looking Statements

This Quarterly Report contains forward-looking statements as that term is defined in the federal securities laws. The events described in forward-looking statements contained in this Quarterly Report may not occur. Generally these statements relate to business plans or strategies, projected or anticipated benefits or other consequences of our plans or strategies, projected or anticipated benefits from acquisitions to be made by us, or projections involving anticipated revenues, earnings or other aspects of our operating results. The words "may," "will," "expect," "believe," "anticipate," "project," "plan," "intend," "estimate," and "continue," and their opposites and similar expressions are intended to identify forward-looking statements. We caution you that these statements are not guarantees of future performance or events and are subject to a number of uncertainties, risks and other influences, many of which are beyond our control, that may influence the accuracy of the statements and the projections upon which the statements are based. Factors which may affect our results include, but are not limited to, the risks and uncertainties discussed in Item 6 of our Annual Report on Form 10-KSB for the year ended December 31, 2007 under "Factors That May Affect Future Results and Financial Condition".

Any one or more of these uncertainties, risks and other influences could materially affect our results of operations and whether forward-looking statements made by us ultimately prove to be accurate. Our actual results, performance and achievements could differ materially from those expressed or implied in these forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether from new information, future events or otherwise.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

DCAP GROUP, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

	September 30, 2008 (Unaudited)	December 31, 2007
Assets		
Current Assets:		
Cash and cash equivalents	$ 520,558	$ 1,030,822
Accounts receivable, net of allowance for doubtful accounts of $25,000 at September 30, 2008 and $50,000 at December 31, 2007	562,331	801,718
Prepaid expenses and other current assets	178,335	295,604
Assets from discontinued operations	54,347	12,651,223
Total current assets	1,315,571	14,779,367
Property and equipment, net	325,900	464,824
Goodwill	2,601,257	2,601,257
Other intangibles, net	94,477	150,910
Notes receivable	5,901,719	5,170,804
Deposits and other assets	79,853	78,164
Total assets	$ 10,318,777	$ 23,245,326
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable and accrued expenses	$ 970,731	$ 630,412
Current portion of long-term debt	1,807,028	2,098,989
Other current liabilities	154,200	154,200
Liabilities from discontinued operations	-	12,517,305
Mandatorily redeemable preferred stock	780,000	780,000
Total current liabilities	3,711,959	16,180,906
Long-term debt	442,114	499,065
Deferred income taxes	379,000	408,000
Commitments		
Stockholders' Equity:		
Common stock, $.01 par value; authorized 10,000,000 shares; issued 3,788,771 at September 30, 2008 and 3,750,447 shares at December 31, 2007	37,888	37,505
Preferred stock, $.01 par value; authorized 1,000,000 shares; 0 shares issued and outstanding	-	-
Capital in excess of par	11,955,103	11,850,872
Deficit	(4,986,905)	(4,545,242)
	7,006,086	7,343,135
Treasury stock, at cost, 816,025 shares at September 30, 2008 and		

781,423 shares at December 31, 2007	(1,220,382)	(1,185,780)
Total stockholders' equity	5,785,704	6,157,355
Total liabilities and stockholders' equity	$ 10,318,777	$ 23,245,326

See notes to condensed consolidated financial statements.

DCAP GROUP, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Operations (Unaudited)

Nine Months Ended September 30,	2008	2007
Commissions and fee revenue	$ 3,767,475	$ 4,486,855
Operating expenses:		
General and administrative expenses	4,360,796	4,765,090
Depreciation and amortization	214,827	212,081
Total operating expenses	4,575,623	4,977,171
Operating loss	(808,148)	(490,316)
Other (expense) income:		
Interest income	3,707	7,175
Interest income - notes receivable	730,915	971,333
Interest expense	(220,690)	(368,713)
Interest expense - mandatorily redeemable preferred stock	(47,125)	(29,250)
Gain on sale of book of business	-	65,767
Total other income	466,807	646,312
(Loss) income from continuing operations before (benefit from) provision for income taxes	(341,341)	155,996
(Benefit from) provision for income taxes	(113,604)	73,696
(Loss) income from continuing operations	(227,737)	82,300
(Loss) income from discontinued operations, net of income taxes	(213,926)	200,878
Net (loss) income	$ (441,663)	$ 283,178
Basic and Diluted Net (Loss) Income Per Common Share:		
(Loss) income from continuing operations	$ (0.08)	$ 0.03
(Loss) income from discontinued operations	$ (0.07)	$ 0.07
(Loss) income per common share	$ (0.15)	$ 0.10
Weighted Average Number of Shares Outstanding:		
Basic	2,972,547	2,962,683
Diluted	2,972,547	3,288,072

See notes to condensed consolidated financial statements.

DCAP GROUP, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Operations (Unaudited)

Three Months Ended September 30,	2008	2007
Commissions and fee revenue	$ 1,143,916	$ 1,359,996
Operating expenses:		
General and administrative expenses	1,218,494	1,492,317
Depreciation and amortization	70,710	74,400
Total operating expenses	1,289,204	1,566,717
Operating loss	(145,288)	(206,721)
Other (expense) income:		
Interest income	803	3,267
Interest income - notes receivable	129,193	322,736
Interest expense	(68,938)	(119,022)
Interest expense - mandatorily redeemable preferred stock	(19,500)	(9,750)
Total other income	41,558	197,231
Loss from continuing operations before benefit from income taxes	(103,730)	(9,490)
Benefit from income taxes	(6,679)	(773)
Loss from continuing operations	(97,051)	(8,717)
(Loss) income from discontinued operations, net of income taxes	(2,974)	67,841
Net (loss) income	$ (100,025)	$ 59,124
Basic and Diluted Net (Loss) Income Per Common Share:		
Loss from continuing operations	$ (0.03)	$ -
(Loss) income from discontinued operations	$ -	$ 0.02
(Loss) income per common share	$ (0.03)	$ 0.02
Weighted Average Number of Shares Outstanding:		
Basic	2,971,521	2,981,024
Diluted	2,971,521	3,298,073

See notes to condensed consolidated financial statements.

DCAP GROUP, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows (Unaudited)

Nine Months Ended September 30,	2008	2007
Cash Flows from Operating Activities:		
Net (loss) income	$ (441,663)	$ 283,178
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:		
Depreciation and amortization	214,827	212,081
Bad debt expense	29,091	-
Accretion of discount on notes receivable	(576,228)	(740,864)
Amortization of warrants	17,731	34,210
Stock-based payments	104,614	27,820
Gain on sale of book of business	-	(65,767)
Deferred income taxes	(328,000)	136,201
Changes in operating assets and liabilities:		
Decrease (increase) in assets:		
Accounts receivable	136,774	418,336
Prepaid expenses and other current assets	338,692	(118,412)
Deposits and other assets	(1,689)	9,221
Increase (decrease) in liabilities:		
Accounts payable and accrued expenses	340,319	(324,793)
Other current liabilities	-	(12,469)
Net cash used in operating activities of continuing operations	(165,532)	(141,258)
Operating activities of discontinued operations	(435,638)	273,742
Net Cash (Used in) Provided by Operating Activities	(601,170)	132,484
Cash Flows from Investing Activities:		
Decrease in notes and other receivables - net	30,810	59,860
Proceeds from sale of book of business	-	66,300
Purchase of property and equipment	(19,470)	(152,695)
Net cash provided by (used in) investing activities of continuing operations	11,340	(26,535)
Investing activities of discontinued operations	1,008,386	1,354,332
Net Cash Provided by Investing Activities	1,019,726	1,327,797
Cash Flows from Financing Activities:		
Principal payments on long-term debt	(366,643)	(417,499)
Proceeds from exercise of options and warrants	-	112,200
Net cash used in financing activities of continuing operations	(366,643)	(305,299)
Financing activities of discontinued operations	(562,177)	(1,350,669)
Net Cash Used in Financing Activities	(928,820)	(1,655,968)
Net Decrease in Cash and Cash Equivalents	(510,264)	(195,687)
Cash and Cash Equivalents, beginning of period	1,030,822	1,196,412
Cash and Cash Equivalents, end of period	$ 520,558	$ 1,000,725

Supplemental Scheduleof Non-Cash Investing and Financing Activities:		
Liabilties assumed by purchaser of premium finance portfolio	$ 11,229,060	$ -
Reserve held by purchaser of premium finance portfolio	$ 261,363	$ -

See notes to condensed consolidated financial statements.

DCAP GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
NINE MONTHS ENDED SEPTEMBER 30, 2008 AND 2007

1. Basis of Presentation

The Condensed Consolidated Balance Sheet as of September 30, 2008, Condensed Consolidated Statements of Operations for the nine months and three months ended September 30, 2008 and 2007 and Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2008 and 2007 have been prepared by us without audit. In our opinion, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary to present fairly in all material respects our financial position as of September 30, 2008, results of operations for the nine months and three months ended September 30, 2008 and 2007 and cash flows for the nine months ended September 30, 2008 and 2007. This report should be read in conjunction with our Annual Report on Form 10-KSB for the year ended December 31, 2007. The consolidated balance sheet at December 31, 2007 was derived from the audited financial statements as of that date.

The results of operations and cash flows for the nine months ended September 30, 2008 are not necessarily indicative of the results to be expected for the full year.

Organization and Nature of Business

DCAP Group, Inc. and Subsidiaries (referred to herein as "we" or "us") operate a network of retail offices and franchise operations engaged in the sale of retail auto, motorcycle, boat, business, and homeowner's insurance, and until February 1, 2008 provided premium financing of insurance policies for customers of our offices as well as customers of non-affiliated entities. On February 1, 2008, we sold our outstanding premium finance loan portfolio. As a result of the sale, our premium financing operations have been classified as discontinued operations and prior periods have been restated. The purchaser of the premium finance portfolio has agreed that, during the five year period ending January 31, 2013 (subject to automatic renewal for successive two year terms under certain circumstances), it will purchase, assume and service premium finance contracts originated by us in the states of New York and Pennsylvania. In connection with such purchases, we will be entitled to receive a fee generally equal to a percentage of the amount financed. Our continuing operations of the premium financing business will consist of the revenue earned from placement fees and any related expenses. We also provide automobile club services for roadside emergencies and tax preparation services.

2. Summary of Significant Accounting Policies

Principles of consolidation

The accompanying consolidated financial statements include the accounts of all subsidiaries and joint ventures in which we have a majority voting interest or voting control. All significant intercompany accounts and transactions have been eliminated.

Revenue recognition

We recognize commission revenue from insurance policies at the beginning of the contract period. Refunds of commissions on the cancellation of insurance policies are reflected at the time of cancellation. For our continuing premium finance operations, we earn placement fees upon the establishment of a premium finance contract.

Franchise fee revenue on initial franchisee fees is recognized when substantially all of our contractual requirements under the franchise agreement are completed. Franchisees also pay a monthly franchise fee plus an applicable percentage of advertising expense. We are obligated to provide marketing and training support to each franchisee. During the nine months ended September 30, 2008 and 2007, approximately $-0- and $110,000, respectively, was recognized as initial franchise fee income.

Fees for income tax preparation are recognized when the services are completed. Automobile club dues are recognized equally over the contract period.

Website Development Costs

Technology and content costs are generally expensed as incurred, except for certain costs relating to the development of internal-use software, including those relating to operating our website, that are capitalized and depreciated over two years. A total of approximately $3,000 and $49,000 in such capitalized costs were incurred during the nine months ended September 30, 2008 and 2007, respectively.

Reclassifications

Certain reclassifications have been made to the consolidated financial statements for the nine months and three months ended September 30, 2007 to conform to the classifications used for the nine months and three months ended September 30, 2008.

3. Notes Receivable

Purchase of Notes Receivable

On January 31, 2006, we purchased from Eagle Insurance Company ("Eagle") two surplus notes issued by Commercial Mutual Insurance Company ("CMIC") in the aggregate principal amount of $3,750,000 (the "Surplus Notes"), plus accrued interest of $1,794,688. The aggregate purchase price for the Surplus Notes was $3,075,141, of which $1,303,434 was paid to Eagle by delivery of a six month promissory note which provided for interest at the rate of 7.5% per annum. The promissory note was paid in full on July 28, 2006. CMIC is a New York property and casualty insurer. The Surplus Notes acquired by us are past due and provide for interest at the prime rate or 8.5% per annum, whichever is less. Payments of principal and interest on the Surplus Notes may only be made out of the surplus of CMIC and require the approval of the New York State Department of Insurance. During the nine months ended September 30, 2008 and 2007, interest payments totaling $-0- and $125,000, respectively, were received. The discount on the Surplus Notes and the accrued interest at the time of acquisition were accreted over a 30 month period through July 31, 2008, the estimated period to collect such amounts. Such accretion amount, together with interest on the Surplus Notes for the nine months and three months ended September 30, 2008 and 2007, are included in our consolidated statement of operations as "Interest income-notes receivable."

Possible Future Conversion of Notes Receivable

In March 2007, CMIC's Board of Directors adopted a resolution to convert CMIC from an advance premium cooperative insurance company to a stock property and casualty insurance company. CMIC has advised us that it has obtained permission from the Superintendent of Insurance of the State of New York (the "Superintendent") to proceed with the conversion process (subject to certain conditions as discussed below).

The conversion by CMIC to a stock property and casualty insurance company is subject to a number of conditions, including the approval of the plan of conversion, which was filed with the Superintendent on April 25, 2008, by both the Superintendent and CMIC's policyholders. As part of the approval process, the Superintendent had an appraisal performed with respect to the fair market value of CMIC as of December 31, 2006. In addition, the Insurance Department conducted a five year examination of CMIC as of December 31, 2006 and held public hearing in October 2008 to consider the conversion plan. We, as a holder of the CMIC Surplus Notes, at our option, would be able to exchange the Surplus Notes for an equitable share of the securities or other consideration, or both, of the corporation into which CMIC would be converted. Based upon the amount payable on the Surplus Notes and the statutory surplus of CMIC, the plan of conversion provides that, in the event of a conversion by CMIC into a stock corporation, in exchange for our relinquishing our rights to any unpaid principal and interest under the Surplus Notes, we would receive 100% of the stock of CMIC. It is anticipated that the policyholders meeting to approve the conversion will occur on or about December 31, 2008. As indicated above, such approval, as well as the prior approval of the Superintendent, is required for the conversion to occur. Upon the effectiveness of the conversion, CMIC's name will change to "Kingstone Insurance Company." We are seeking stockholder approval of an amendment to our certificate of incorporation to change our name to "Kingstone Companies, Inc." Such name change would only take place in the event that the conversion occurs and we obtain a controlling interest in Kingstone Insurance Company. No assurances can be given that the conversion will occur or as to the terms of the conversion.

Our Chairman is also Chairman of CMIC and one of our other directors and our Chief Accounting Officer are also directors of CMIC.

4. Employee Stock Compensation

In November 1998, we adopted the 1998 Stock Option Plan, which provided for the issuance of incentive stock options and non-statutory stock options. Under this plan, options to purchase not more than 400,000 of our common shares were permitted to be granted, at a price to be determined by our Board of Directors or the Stock Option Committee at the time of grant. During 2002, we increased the number of common shares authorized to be issued pursuant to the 1998 Stock Option Plan to 750,000. Incentive stock options granted under this plan expire no later than ten years from date of grant (except no later than five years for a grant to a 10% stockholder). Our Board of Directors or the Stock Option Committee determined the expiration date with respect to non-statutory options granted under this plan. This plan terminated in November 2008.

In December 2005, our shareholders ratified the adoption of the 2005 Equity Participation Plan, which provides for the issuance of incentive stock options, non-statutory stock options and restricted stock. Under this plan, a maximum of 300,000 common shares may be issued pursuant to options granted and restricted stock issued. Incentive stock options granted under this plan expire no later than ten years from date of grant (except no later than five years for a grant to a 10% stockholder). Our Board of Directors or the Stock Option Committee will determine the expiration date with respect to non-statutory options, and the vesting provisions for restricted stock, granted under this plan.

Our results for the nine months and three months ended September 30, 2008 include share-based compensation expense related to stock options totaling approximately $64,000 and $16,000, respectively. Our results for the nine months and three months ended September 30, 2007 include share-based compensation expense totaling approximately $19,000 and $9,000, respectively. Such amounts have been included in the Condensed Consolidated Statements of Operations within general and administrative expenses.

Stock option compensation expense in 2008 and 2007 is the estimated fair value of options granted amortized on a straight-line basis over the requisite service period for the entire portion of the award.

We did not grant any options under either plan during the nine months and three months ended September 30, 2008. During the nine months and three months ended September 30, 2007, we did not grant any options under the 1998 Stock Option Plan but did grant 59,524 options at $2.52 per share under the 2005 Equity Participation Plan. The weighted average fair value of options granted during the nine months and three months ended September 30, 2007 was $.78.

The following table represents our stock options granted, exercised, and forfeited during the first nine months of 2008.

Stock Options	Number of Shares	Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2008	268,624	$ 2.55	-	-
Granted	-	$ -	-&#1	