

E-SMART TECHNOLOGIES INC
Form 10QSB
December 27, 2007
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U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

Form 10-QSB

(Mark One)

Quarterly report under section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended: **March 31, 2007**

Transition report under section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _____ to _____.

Commission File No: 0-30717

e-SMART TECHNOLOGIES, INC.

(Name of small business in its charter)

Nevada
(State or other jurisdiction of incorporation)

88-0409261
(IRS Employer Id. No.)

526 West 26th Street, Suite 710, New York, NY 10001

(Address of Principal Office including Zip Code)

Issuer's telephone Number: **(212) 727-3790**

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 No

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:

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Common Stock, \$.001 par value, **273,409,285** shares at March 31, 2007.

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

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

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e-SMART TECHNOLOGIES, INC. and SUBSIDIARIES

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

The unaudited condensed consolidated balance sheet of the Registrant at March 31, 2007, the audited balance sheet at December 31, 2006, and the unaudited condensed consolidated statements of operations, shareholders' equity (deficiency), and cash flows for the three months ended March 31, 2007 and March 31, 2006 follow. The unaudited condensed consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary to a fair statement of the results for the periods presented.

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e-SMART TECHNOLOGIES, INC. and SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

| | <i>[Unaudited]</i> March 31, 2007 | <i>[Audited]</i> December 31, 2006 |
|---|---|--|
| Assets | | |
| Current assets - | | |
| Cash | \$ 130,423 | \$ 49,845 |
| Prepaid expenses | 9,369 | 7,558 |
| Total current assets | 139,792 | 57,403 |
| Equipment, net | 38,577 | 41,446 |
| License of smart card technology, net of amortization | 91,252 | 92,860 |
| Officers' advances | | 11,549 |
| Receivable from IVI Smart Technologies, Inc., a related party | 106,362 | |
| Lease deposit | 78,865 | 79,713 |
| Total assets | \$ 454,848 | \$ 282,971 |
| Liabilities and Shareholders' Equity (Deficiency) | | |
| Current liabilities - | | |
| Current portion of notes payable | \$ 509,927 | \$ 509,927 |
| Accounts payable | 1,533,156 | 1,286,904 |
| Accrued officers' compensation | 606,785 | 544,285 |
| Accrued expenses | 120,127 | 76,660 |
| Total current liabilities | 2,769,995 | 2,417,776 |
| Note Payable - long-term | 2,647,371 | 1,946,394 |
| Total liabilities | 5,417,366 | 4,364,170 |
| Shareholders' Equity (Deficiency) - | | |
| Preferred Stock, \$0.001 par value, 10 million shares authorized; -0- issued and outstanding | | |
| Common shares, \$0.001 par, 490 million shares authorized; 273,409,285 and 242,540,441 shares issued and outstanding in 2007 and 2006, respectively | 273,409 | 242,540 |
| Additional paid in capital | 72,587,448 | 70,954,225 |
| Deficit accumulated during development stage | (77,823,375) | (75,277,964) |
| Total shareholders' equity (deficiency) | (4,962,518) | (4,081,199) |
| Total liabilities and shareholders' equity (deficiency) | \$ 454,848 | \$ 282,971 |

See notes to condensed consolidated financial statements.

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e-SMART TECHNOLOGIES, INC. and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

[Unaudited]

| | Three Months Ended March 31, | | January 1, 2001 |
|--|------------------------------|----------------|---------------------|
| | 2007 | 2006 | (inception of |
| | | | development period) |
| | | | to March 31, 2007 |
| | \$ | \$ | \$ |
| Revenue | | | |
| Operating expenses: | | | |
| Research and development | 159,000 | 152,475 | 15,309,309 |
| Selling, general and administrative | 2,332,786 | 817,515 | 62,100,624 |
| Interest expense | 52,975 | 46,008 | 403,992 |
| Total operating expenses | 2,544,761 | 1,015,998 | 77,813,925 |
| Loss before provision for taxes | (2,544,761) | (1,015,998) | (77,813,925) |
| Provision for income taxes | 650 | 1,040 | 9,450 |
| Net Loss | \$ (2,545,411) | \$ (1,017,038) | \$ (77,823,375) |
| Net loss per share | \$ (0.01) | \$ (0.01) | \$ (0.44) |
| Weighted average number of common shares outstanding | 265,560,824 | 200,000,000 | 175,063,566 |

See notes to condensed consolidated financial statements.

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e-SMART TECHNOLOGIES, INC. and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF

SHAREHOLDERS EQUITY (DEFICIENCY)

| | Common Stock Shares | Common Stock Amount | Additional Paid-in Capital | Accumulated Deficit | Total |
|--|------------------------|------------------------|----------------------------------|------------------------|----------------|
| <i>[Audited]</i> | | | | | |
| Balance January 1, 2006 | 200,000,000 | \$ 200,000 | \$ 63,777,497 | \$ (67,507,910) | \$ (3,530,413) |
| Issuance of shares in relation to related party borrowings | 20,990,441 | 20,990 | 4,150,278 | | 4,171,268 |
| Issuance of shares for services | 21,550,000 | 21,550 | 3,026,450 | | 3,048,000 |
| Net loss | | | | (7,770,054) | (7,770,054) |
| Balance, December 31, 2006 | 242,540,441 | 242,540 | 70,954,225 | (75,277,964) | (4,081,199) |
| <i>[Unaudited]</i> | | | | | |
| Balance, January 1, 2007 | 242,540,441 | 242,540 | 70,954,225 | (75,277,964) | (4,081,199) |
| Issuance of shares for services | 30,868,844 | 30,869 | 1,633,223 | | 1,664,092 |
| Net loss | | | | (2,545,411) | (2,545,411) |
| Balance, March 31, 2007 | 273,409,285 | \$ 273,409 | \$ 72,587,448 | \$ (77,823,375) | \$ (4,962,518) |

See notes to condensed consolidated financial statements.

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e-SMART TECHNOLOGIES, INC. and SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

[Unaudited]

| | Three Months Ended March 31, | | January 1, 2001 |
|---|------------------------------|-------------------|--|
| | 2007 | 2006 | (inception of (development) period to March 31, 2007 |
| Cash flows from Operating Activities - | | | |
| Net loss | \$ (2,545,411) | \$ (1,017,038) | \$ (77,823,375) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | | |
| Issuance of common stock and common stock options for services | 1,664,092 | | 60,660,592 |
| Depreciation and amortization | 5,502 | 3,511 | 82,938 |
| Bad debt expense | | | 312,505 |
| Changes in Assets and Liabilities - | | | |
| (Increase) decrease in prepaid expenses | (1,811) | 150 | (9,369) |
| Decrease in officers' advances | 11,549 | 16,151 | |
| Increase in accounts payable | 246,252 | 156,284 | 1,533,156 |
| Increase in accrued expenses | 105,967 | 70,637 | 999,152 |
| Net Cash Used in Operating Activities | (513,860) | (770,305) | (14,244,401) |
| Cash Flows from Investing Activities - | | | |
| Acquisition of equipment | (1,025) | (5,709) | (84,167) |
| Purchase of technology licenses | | | (128,600) |
| Advances to Biosensor, LLC | | | (312,505) |
| Advances to IVI Smart Technologies, Inc., a related party | (106,362) | | (106,362) |
| (Addition) reduction of lease deposit | 848 | (3,711) | (78,865) |
| Net Cash Used in Investing Activities | (106,539) | (9,420) | (710,499) |
| Cash Flows from Financing Activities - | | | |
| Advances from Intermarket Ventures, Inc., a related party | 700,977 | 750,324 | 7,664,232 |
| Proceeds from other borrowings, net | | | 47,500 |
| Proceeds from issuances of common stock | | | 7,373,591 |
| Net Cash Provided by Financing Activities | 700,977 | 750,324 | 15,085,323 |
| Net Increase (decrease) in Cash | 80,578 | (29,401) | 130,423 |
| Cash at Beginning of Period | 49,845 | 164,584 | |
| Cash at End of Period | \$ 130,423 | \$ 135,183 | \$ 130,423 |
| Supplemental non-cash financing activities - | | | |
| Issuance of common stock for services | \$ 1,644,092 | \$ | \$ 4,994,592 |

See notes to condensed consolidated financial statements.

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e-SMART TECHNOLOGIES, INC. and SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Basis of Presentation

The Company has been in the development stage since the commencement of its operations on January 1, 2001. The accompanying unaudited consolidated financial statements include the accounts of the Registrant and those of its wholly-owned subsidiaries, e-Smart Korea, Inc. and e-Smart Systems, Inc., and have been prepared in accordance with generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three month periods ended March 31, 2007 and 2006, are not necessarily indicative of the results that may be expected for the respective years ended December 31, 2007 and 2006.

The unaudited condensed consolidated financial statements should be read in conjunction with the audited financial statements and related footnotes included in the Registrant's Annual Report on Form 10-KSB for the fiscal year ended December 31, 2006, supplemented by the notes included herein.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Certain prior year amounts disclosed in the accompanying financial statements and notes thereto have been reclassified to conform to the current period's presentation.

Note 2 Letter of Comment

From time to time the Staff of the Securities and Exchange Commission's Division of Corporate Finance may examine the periodic reports of a Registrant for compliance and form and forward to the Registrant comments regarding the Registrant's prior filings (a Letter of Comment). The Company seeks to respond to all Letters of Comment received addressing any and all issues raised, including the filing of amended quarterly and annual reports as appropriate.

Note 3 Related Party Transactions

The Company is the owner of three technology licenses each of which grants the Company exclusivity to the technology covered in a particular territory. The three territories covered are the People's Republic of China, the remainder of Asia and the United States of America. The licenses, which have a term of twenty years commencing January 1, 2001, were granted to the Company by IVI Smart Technologies, Inc. (IVI).

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In addition, at March 31, 2007 and December 31, 2006, the Company was indebted to Intermarket in the amount of \$3,097,371 and \$2,396,394, respectively, plus accrued interest. These obligations are unsecured and bear interest between 5 to 6%. Of the above amounts, \$450,000 was due on demand, and the remaining balance, \$2,647,371 and \$1,946,394 at March 31, 2007 and 2006, respectively, were due on December 31, 2008.

Intermarket, together with its two principal stockholders (the Company's President and Chief Executive Officer Mary A. Grace and its Chief Technology Officer Tamio Saito), continue to own a substantial percentage of the common stock of the Company and will continue to have the ability to materially influence the direction of the Company, its efforts in raising the additional capital critical to its success, and the strategies employed in commercialization of the licensed technology. In addition, the Planned Reorganization will include the receipt by IVI of Preferred Series A shares which possess 70% voting control of the Company in exchange for loans received from Intermarket and licenses granted by IVI.

Note 4 Going Concern

The Registrant's condensed consolidated financial statements have been presented on the basis that it is a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business.

As shown in the accompanying financial statements, the Registrant had negative working capital at March 31, 2007, of \$2,630,203. In addition, the Registrant has incurred an accumulated deficit of \$(77,823,375) through March 31, 2007. The Registrant is dependent upon the efforts of its management to raise proceeds from continued debt or equity placements to sustain the research and development and ultimate commercialization of their respective interests in the Super Smart Card technology. The Registrant's ability to continue to receive the necessary level of funding support through the efforts of its management cannot be guaranteed. The condensed consolidated financial statements do not include any adjustments that might be necessary if the Registrant is unable to continue as a going concern.

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

Plan of Operation

Since the inception of our development period on January 1, 2001, and continuing through March 31, 2007, our primary source of funds have been private placements of our equity securities to accredited investors and loans to the Company. We expect that this dependence will continue until the Company finalizes broader funding or our first system starts to generate sufficient cash flow to cover our operating costs.

As of the date of this Report, we expect this dependence to continue until the third or fourth quarter of 2007. There can be no assurance that we will continue to be able to rely on these sources of funds.

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Over the next 12 months we expect to continue our marketing and research and development efforts and to implement our first system, demonstrating the viability of our Super Smart Card and BVS2 based products and related technologies.

Our ability to maintain what we believe to be the state-of-the-art quality of our Super Smart Card and BVS2 system and related technologies is dependent upon our ability to continue to improve our products functionality and durability, and to reduce their cost of manufacture. In addition, we are constantly trying to find and develop new products that enhance the functionality of our BVS2 platform. This research and development is expected to continue throughout 2007 and well into 2008. Accordingly, the Company expects to continue to be dependent upon funds from its affiliates and from existing accredited investors, subject to the same risks enumerated in the preceding paragraph.

We are constantly acquiring software and equipment in connection with our research and development activities. Our planned 2007 budget is approximately \$3,000,000 for such acquisitions, but could change depending upon our rate of accomplishment in the anticipated sales of one or more systems. Should such sales occur, we will also require an operations and testing center near those customers' offices as a condition of contract.

During 2007 in the United States, we intend to fill a number of key management, marketing and technology positions commensurate with our intended growth and expanded operations.

Off-Balance Sheet Arrangements

During the three months ended March 31, 2007, we had no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors. The Company is presently negotiating certain proposed relationships, which if accepted by all parties, may contain terms that have off-balance sheet implications; see Note 12 to the Consolidated Financial Statements included in Item 7 of our Form 10-KSB for the year ended December 31, 2006.

Forward Looking Statements:

The following discussion contains forward-looking statements regarding the Registrant, its business, prospects and results of operations that are subject to certain risks and uncertainties posed by many factors and events that could cause the Registrant's actual business, prospects and results of operations to differ materially from those that may be anticipated by such forward-looking statements. Factors that may affect such forward-looking statements include the Registrant's ability to successfully exploit its licensed technology, develop new products and new markets for its licensed technology; the impact of competition on the Registrant's proposed operations, changes in law or regulatory requirements that adversely affect or preclude customers from using the Registrant's licensed technology, delays in the Registrant's introduction of new products or services, and failure by the Registrant to keep pace with emerging technologies.

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When used in this discussion, words such as believes, anticipates, expects, intends, and similar expressions are intended to identify forward-looking statements, but are not the exclusive means of identifying forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report. The Registrant undertakes no obligation to revise any forward-looking statements in order to reflect events or circumstances that may subsequently arise. Readers are urged to carefully review and consider the various disclosures made by the Registrant in this report and other reports filed with the Securities and Exchange Commission (SEC) that attempt to advise interested parties of the risks and factors that may affect the Registrant's business.

Discussion and Analysis of Three Months Ended March 31, 2007 and March 31, 2006

Revenues Since obtaining the license to the Super Smart Card technology in November 2000, the Registrant has been engaged in research and development efforts to enhance and broaden the technology's applications and in exploring the global market for its optimal commercialization. In the opinion of management, the Registrant's Super Smart Card is ready for commercialization. This fact notwithstanding, the Registrant is still in its development stage for accounting purposes as it has not experienced revenues in either of the three month periods ended March 31, 2007 (1Q7) or March 31, 2006 (1Q6).

Operating Expenses Operating expenses were \$2,544,761 for 1Q7 compared to \$1,015,998 1Q6 resulting in an increase of \$1,528,763 or 150%. This increase was principally attributable to the various engineering and consulting services which were acquired with common shares valued at \$1,664,092; there were no comparable charges in 1Q6

Loss Before Taxes and Income Taxes As a result of the foregoing, loss before taxes for 1Q7 was \$(2,544,761) compared to \$(1,015,998) for 1Q6 upon which the Registrant's provision for taxes in both periods was solely attributable to minimum state franchise taxes payable.

Net Loss Consistent with the foregoing analysis, the Registrant reported a net loss of \$(2,545,411) or \$(0.01) per share for 1Q7, compared to a net loss of \$(1,017,038) or \$(0.01) per share for 1Q6, based upon weighted average shares outstanding of 265,560,824 and 200,000,000, respectively.

Liquidity and Capital Resources The Registrant has limited working capital and is dependent upon the efforts of its management in raising proceeds derived from private securities offerings for funds for the continuation of its proposed smart card business. Currently, the Registrant does not have any existing credit facilities or similar bank borrowing arrangements. The Registrant will need to obtain additional financing in order to carry out its entire business plan. There can be no assurance that any additional financing will be available to the Registrant on acceptable terms, if at all. If the Registrant raises additional funds by issuing additional equity securities, further dilution to existing equity holders will result. If adequate additional funds are not available, the Registrant may be required to curtail significantly its long term business objectives and the Registrant still may not be able to transition out of the development stage, notwithstanding that the BVS2 systems and Super Smart Card and other smart card system technologies are ready for commercialization.

At March 31, 2007, the Registrant had current assets of \$139,792 (including cash of \$130,423, current liabilities of \$2,769,995, and

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an accumulated deficit of \$(77,823,375). The Registrant periodically evaluates its liquidity requirements, capital needs and availability of capital resources in view of its plans for commercialization of its technology, and other operating cash needs. In the opinion of Registrant's management, the Registrant is entirely dependent upon a material infusion of capital from loans during the next several months in order to sustain its current developmental efforts, commence commercial operations, and ultimately transition out of the development stage.

ITEM 3. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer carried out an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)) as of March 31, 2007, as required by paragraph (b) of Exchange Act Rules 13a-15 or 15d-15. Based upon this evaluation, the CEO and CFO has concluded that as of March 31, 2007, the Company's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, and summarized, within the time periods specified in the Commission's rules and forms and that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to its management, including its principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosures. Management also acknowledges that the Company has not been able to ensure that reports were filed within the time periods specified by the Commission. Management concluded that the issues relating to reporting relate not to the accuracy of data but to delays which resulted from availability and allocation of resources. The Company therefore took steps to employ an additional staff member to maintain books and records, and continued to seek to complete long term financing to ensure the availability of funds necessary to ensure timely submission of all periodic filings.

Changes in Internal Controls

The Registrant increased its staff in its New York office to improve record keeping.

PART II - OTHER INFORMATION

ITEM 5. OTHER MATTERS

During the period, the Board of Directors and a majority of the Company's shareholders, by written consent, approved an amendment to the Company's Certificate of Incorporation that would increase the number of authorized shares of Common and Preferred Stock from 490 million and 10 million to 730 million and 20 million, respectively. The planned effective date for the increase is on or after June 15, 2007.

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ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

Exhibits:

31.1 Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Reports on Form 8-K: None.

SIGNATURES

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

e-Smart Technologies, Inc.

By: /s/ Mary A. Grace
Chief Executive Officer, and Director

By: /s/ Mary A. Grace
Chief Financial Officer

Dated: December 27, 2007

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Exhibit Index

| Exhibit No. | Description |
|--------------------|--|
| 31.1 | Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1 | Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |