

INSIGNIA SYSTEMS INC/MN
Form 10-Q
November 14, 2008
[Table of Contents](#)

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

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

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: 1-13471

INSIGNIA SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Minnesota
(State or other jurisdiction of
incorporation or organization)

41-1656308
(IRS Employer Identification No.)

8799 Brooklyn Blvd.
Minneapolis, MN 55445

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

(Address of principal executive offices)

(763) 392-6200

(Registrant's telephone number, including area code)

Not applicable.

(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 report(s)), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Number of shares outstanding of Common Stock, \$.01 par value, as of October 31, 2008, was 15,369,464.

1

Insignia Systems, Inc.

TABLE OF CONTENTS

<u>PART I.</u>	<u>FINANCIAL INFORMATION</u>	3
<u>Item 1.</u>	<u>Financial Statements</u>	3
	<u>Balance Sheets – September 30, 2008 and December 31, 2007 (unaudited)</u>	3
	<u>Statements of Operations – Three and nine months ended September 30, 2008 and 2007 (unaudited)</u>	4
	<u>Statements of Shareholders' Equity – Nine months ended September 30, 2008 and 2007 (unaudited)</u>	5
	<u>Statements of Cash Flows – Nine months ended September 30, 2008 and 2007 (unaudited)</u>	6

	<u>Notes to Financial Statements – September 30, 2008 (unaudited)</u>	7
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	10
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	15
Item 4.	<u>Controls and Procedures</u>	15
PART II.	<u>OTHER INFORMATION</u>	16
Item 1.	<u>Legal Proceedings</u>	16
Item 1A.	<u>Risk Factors</u>	17
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	17
Item 3.	<u>Defaults Upon Senior Securities</u>	18
Item 4.	<u>Submission of Matters to a Vote of Security Holders</u>	18
Item 5.	<u>Other Information</u>	18
Item 6.	<u>Exhibits</u>	18

2

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Insignia Systems, Inc.

BALANCE SHEETS

(Unaudited)

	September 30, 2008	December 31, 2007
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 8,336,000	\$ 7,393,000
Accounts receivable – net of \$10,000 allowance	4,007,000	2,155,000
Inventories	515,000	397,000
Deferred tax assets, net	164,000	164,000
Prepaid expenses and other	798,000	883,000
Total Current Assets	13,820,000	10,992,000

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Other Assets:

Property and equipment, net	1,095,000	375,000
Non-current deferred tax assets, net	1,967,000	1,967,000
Other	40,000	6,000
Total Assets	\$ 16,922,000	\$ 13,340,000

LIABILITIES AND SHAREHOLDERS EQUITY

Current Liabilities:

Current maturities of long-term liabilities	\$ 93,000	\$ 266,000
Accounts payable	2,100,000	1,369,000
Accrued liabilities		
Compensation	875,000	622,000
Employee stock purchase plan	99,000	98,000
Legal	1,273,000	208,000
Other commissions	860,000	152,000
Other	589,000	221,000
Deferred revenue	1,015,000	305,000
Total Current Liabilities	6,904,000	3,241,000

Long-Term Liabilities, less current maturities	398,000	422,000
---	----------------	----------------

Commitments and Contingencies

Shareholders Equity:

Common stock, par value \$.01:		
Authorized shares 40,000,000		
Issued and outstanding shares 15,369,000 at September 30, 2008 and 15,550,000 at December 31, 2007	154,000	156,000
Additional paid-in capital	32,054,000	32,025,000
Accumulated deficit	(22,588,000)	(22,504,000)
Total Shareholders Equity	9,620,000	9,677,000

Total Liabilities and Shareholders Equity	\$ 16,922,000	\$ 13,340,000
--	----------------------	----------------------

See accompanying notes to financial statements.

3

Table of Contents

Insignia Systems, Inc.

STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30 2008	2007	September 30 2008	2007
Services revenues	\$7,999,000	\$5,718,000	\$20,830,000	\$17,281,000
Products sold	598,000	743,000	1,908,000	2,214,000

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Total Net Sales	8,597,000	6,461,000	22,738,000	19,495,000
Cost of services	3,699,000	2,372,000	9,190,000	7,017,000
Cost of products sold	399,000	481,000	1,221,000	1,352,000
Total Cost of Sales	4,098,000	2,853,000	10,411,000	8,369,000
Gross Profit	4,499,000	3,608,000	12,327,000	11,126,000
Operating Expenses:				
Selling	2,561,000	1,400,000	5,878,000	4,295,000
Marketing	451,000	357,000	1,211,000	1,052,000
Warrant expense (selling & marketing)		1,521,000		1,521,000
General and administrative	1,992,000	1,245,000	5,457,000	3,569,000
Total Operating Expenses	5,004,000	4,523,000	12,546,000	10,437,000
Operating Income (Loss)	(505,000)	(915,000)	(219,000)	689,000
Other Income (Expense):				
Interest income	55,000	71,000	178,000	166,000
Interest expense	(13,000)	(19,000)	(43,000)	(77,000)
Other income	2,000			
Total Other Income	44,000	52,000	135,000	89,000
Income (Loss) Before Taxes	(461,000)	(863,000)	(84,000)	778,000
Income tax expense (benefit)	(207,000)	44,000		60,000
Net Income (Loss)	\$(254,000)	\$(907,000)	\$(84,000)	\$718,000
Net income (loss) per share:				
Basic	\$(0.02)	\$(0.06)	\$(0.01)	\$0.05
Diluted	\$(0.02)	\$(0.06)	\$(0.01)	\$0.04
Shares used in calculation of net income (loss) per share:				
Basic	15,527,000	15,454,000	15,569,000	15,367,000
Diluted	15,527,000	15,454,000	15,569,000	16,178,000

See accompanying notes to financial statements.

4

Table of Contents

Insignia Systems, Inc.

STATEMENTS OF SHAREHOLDERS' EQUITY

(Unaudited)

	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-In Capital	Deficit	
<u>Nine Months Ended September 30, 2008</u>					
Balance at December 31, 2007	15,550,000	\$ 156,000	\$ 32,025,000	\$(22,504,000)	\$ 9,677,000
Issuance of common stock, net	44,000		98,000		98,000

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Stock-based compensation			393,000		393,000
Repurchase of common stock, net	(225,000)	(2,000)	(462,000)		(464,000)
Net loss				(84,000)	(84,000)
Balance at September 30, 2008	15,369,000	\$ 154,000	\$ 32,054,000	\$(22,588,000)	\$ 9,620,000
<u>Nine Months Ended September 30, 2007</u>					
Balance at December 31, 2006	15,152,000	\$ 152,000	\$ 29,557,000	\$(24,847,000)	\$ 4,862,000
Issuance of common stock, net	384,000	3,000	442,000		445,000
Stock-based compensation			348,000		348,000
Warrant expense			1,521,000		1,521,000
Net income				718,000	718,000
Balance at September 30, 2007	15,536,000	\$ 155,000	\$ 31,868,000	\$(24,129,000)	\$ 7,894,000

See accompanying notes to financial statements.

5

Table of Contents

Insignia Systems, Inc.

STATEMENTS OF CASH FLOWS

(Unaudited)

Nine Months Ended September 30	2008	2007
Operating Activities:		
Net income (loss)	\$ (84,000)	\$ 718,000
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	267,000	188,000
Stock-based compensation	393,000	348,000
Warrant expense		1,521,000
Changes in operating assets and liabilities:		
Accounts receivable	(1,852,000)	83,000
Inventories	(118,000)	(44,000)
Prepaid expenses and other	51,000	16,000
Accounts payable	731,000	135,000
Accrued liabilities	2,395,000	277,000
Deferred revenue	710,000	(109,000)
Net cash provided by operating activities	2,493,000	3,133,000
Investing Activities:		
Purchases of property and equipment	(987,000)	(124,000)
Net cash used in investing activities	(987,000)	(124,000)
Financing Activities:		
Net change in line of credit		(186,000)
Payment of long-term liabilities	(197,000)	(178,000)
Proceeds from issuance of common stock, net	98,000	445,000
Repurchase of common stock, net	(464,000)	

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Net cash provided by (used in) financing activities	(563,000)	81,000
Increase in cash and cash equivalents	943,000	3,090,000
Cash and cash equivalents at beginning of period	7,393,000	3,785,000
Cash and cash equivalents at end of period	\$ 8,336,000	\$ 6,875,000
Supplemental disclosures for cash flow information:		
Cash paid during periods for interest	\$ 14,000	\$ 45,000
Cash paid during periods for income taxes	8,000	60,000

See accompanying notes to financial statements.

6

Table of Contents

Insignia Systems, Inc.

NOTES TO FINANCIAL STATEMENTS

(Unaudited)

1. Summary of Significant Accounting Policies.

Description of Business. Insignia Systems, Inc. (the Company) markets in-store advertising programs, services and products to retailers and consumer packaged goods manufacturers. The Company's services and products include the Insignia Point-of-Purchase Services (POPS) in-store advertising program, thermal sign card supplies for the Company's SIGNright and Impulse systems, Stylus software and laser printable cardstock and label supplies.

Basis of Presentation. Financial statements for the interim periods included herein are unaudited; however, they contain all adjustments, including normal recurring accruals, which in the opinion of management, are necessary to present fairly the financial position of the Company at September 30, 2008, and its results of operations and cash flows for the three and nine months ended September 30, 2008 and 2007. Results of operations for the periods presented are not necessarily indicative of the results to be expected for the full year.

The financial statements do not include certain footnote disclosures and financial information normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America and, therefore, should be read in conjunction with the financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

The Summary of Significant Accounting Policies in the Company's 2007 Annual Report on Form

10-K describes the Company's accounting policies.

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Inventories. Inventories are primarily comprised of parts and supplies for Impulse and SIGNright machines, sign cards, and rollstock. Inventory is valued at the lower of cost or market using the first-in, first-out (FIFO) method, and consists of the following:

	September 30, 2008	December 31, 2007
Raw materials	\$ 114,000	\$ 82,000
Work-in-process	90,000	36,000
Finished goods	311,000	279,000
	\$ 515,000	\$ 397,000

Property and Equipment. Property and equipment consists of the following:

	September 30, 2008		December 31, 2007
Production tooling, machinery and equipment	\$2,263,000		\$ 1,725,000
Office furniture and fixtures	249,000		191,000
Computer equipment and software	706,000		698,000
Leasehold improvements	261,000		368,000
	3,479,000		2,982,000
Accumulated depreciation and amortization	(2,384,000)	(2,607,000
Net Property and Equipment	\$ 1,095,000		\$ 375,000

7

Table of Contents

Stock-Based Compensation. The Company accounts for its stock-based compensation in accordance with the provisions of Statement of Financial Accounting Standards No. 123(R). The Company recognizes stock compensation expense on a straight-line method over the requisite service period of the award.

There were 321,000 stock option awards during the nine months ended September 30, 2008. Total stock-based compensation expense recorded for the nine months ended September 30, 2008 and 2007, was \$393,000 and \$348,000, respectively. The Company uses the Black-Scholes option-pricing model to estimate the fair value of stock-based awards with the following weighted average assumptions for the stock option awards granted during the nine months ended September 30, 2008: expected life of 3.4 years, expected volatility of 75%, dividend yield of 0% and a risk-free interest rate of 2.67%.

Net Income (Loss) Per Share. Basic net income (loss) per share is computed by dividing net income by the weighted average shares outstanding and excludes any dilutive effects of options, warrants and convertible securities. Diluted net income (loss) per share gives effect to all diluted potential common shares outstanding during the period. Options and warrants to purchase approximately 2,292,000 and 1,061,000 shares of common stock with weighted average exercise prices of \$4.74 and \$6.24 were outstanding at September 30, 2008 and 2007 and were not included in the computation of common stock equivalents for the three months ended September 30, 2008 and 2007 because their exercise prices were higher than the average fair market value of the common shares during the reporting period. Options and warrants to purchase approximately 2,154,000 and 1,207,000 shares of common stock with weighted average exercise prices of \$4.95 and \$6.12 were outstanding at

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

September 30, 2008 and 2007 and were not included in the computation of common stock equivalents for the nine months ended September 30, 2008 and 2007 because their exercise prices were higher than the average fair market value of the common shares during the reporting period. During the three months ended September 30, 2008 and 2007 and the nine months ended September 30, 2008, the effect of options and warrants outstanding was anti-dilutive due to the net losses incurred during the periods. Had net income been achieved, approximately 392,000, 1,003,000 and 440,000, respectively, of common stock equivalents would have been included in the computation of diluted net income per share.

Weighted average common shares outstanding for the three and nine months ended September 30, 2008 and 2007 were as follows:

	Three Months Ended		Nine Months Ended	
	September 30 2008	2007	September 30 2008	2007
Denominator for basic net income (loss) per share weighted average shares	15,527,000	15,454,000	15,569,000	15,367,000
Effect of dilutive securities: Stock options and warrants				811,000
Denominator for diluted net income (loss) per share adjusted weighted average shares	15,527,000	15,454,000	15,569,000	16,178,000

2. **Commitments and Contingencies.**

Legal. In August 2000, News America Marketing In-Store, Inc. (News America), brought suit against the Company in U.S. District Court in New York, New York. The case was settled in November 2002. The terms of the settlement agreement are confidential. The settlement did not impact the Company's operating results.

8

Table of Contents

In October 2003, News America brought suit against the Company in U.S. District Court in New York, New York, alleging that the Company has engaged in deceptive acts and practices, has interfered with existing business relationships with retailers and prospective economic advantage, and has engaged in unfair competition. The suit sought unspecified damages and injunctive relief. In February 2007 the U.S. District Court in New York transferred this action to Minnesota where the claims became part of the lawsuit the Company filed against News America and Albertson's Inc. in 2004 (described below), and the New York action was subsequently dismissed.

On September 23, 2004, the Company brought suit against News America and Albertson's Inc. (Albertson's) in Federal District Court in Minneapolis, Minnesota, for violations of federal and state antitrust and false advertising laws, alleging that News America has acquired and maintained monopoly power through various wrongful acts designed to harm the Company in the in-store advertising and promotion products and services market. The suit seeks injunctive relief sufficient to prevent further antitrust injury and an award of treble damages to be determined at trial for the harm caused to the Company. On June 30, 2006 the Court denied the motions of News America and Albertson's to dismiss the suit. On September 20, 2006, the State of Minnesota through its Attorney General intervened as a co-plaintiff in the business disparagement portion of the Minnesota case. In December 2006, News America filed counterclaims in the Minnesota case that included claims similar to those in its New York action against Insignia and one of its officers, plus claims for damages for two alleged incidents of libel and slander. Motions to dismiss the counterclaims were argued in June 2007, and on September 28, 2007 the Court denied the motions to dismiss the counterclaims. The parties are now engaged in pre-trial discovery. Pursuant to Court order, all discovery and pre-trial matters must be completed by May 1, 2009. On February 4, 2008, the Court approved a Consent Decree entered into by News America and the State of Minnesota under which News America agreed to not violate Minnesota's statutes prohibiting commercial disparagement. On July 29, 2008, the Company and Albertson's entered into a Settlement Agreement and Mutual Release, in which they each agreed to release all claims against the other, and the

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Company agreed to dismiss its lawsuit against Albertson's.

The Company filed claims in December 2006 and January 2007 with its director's and officer's liability and general liability insurers related to the defense costs and insurance coverage for claims asserted against the Company and one of its officers in News America's counterclaims. On August 9, 2007, the Company filed a complaint against the insurers in Hennepin County District Court, State of Minnesota requesting a declaratory judgment that the insurers owe the Company and its officer such defense costs and insurance coverage. In December 2007, the Company settled its claim against one of the insurers, and the litigation is continuing against the other insurer.

Although management believes that News America's counterclaims are without merit, an evaluation of the likelihood of an unfavorable outcome and an estimate of the potential liability cannot be rendered at this time. If the Company is required to pay a significant amount in settlement or damages, it will have a material adverse effect on its operations and financial condition. In addition, a negative outcome of this litigation could affect long-term competitive aspects of the Company's business.

Management currently expects the amount of legal fees and expenses that will be incurred in connection with the ongoing lawsuits to be significant throughout 2008 and 2009. During the nine months ended September 30, 2008, the Company incurred legal fees and expenses of \$3,270,000 related to the ongoing lawsuits. Legal fees and expenses are expensed as incurred and are included in general and administrative expenses in the statement of operations.

The Company is subject to various other legal proceedings in the normal course of business. Management believes the outcome of these proceedings will not have a material adverse effect on the Company's financial position or results of operations.

9

Table of Contents

- Income Taxes.** The Company did not record a cumulative income tax benefit for the nine months ended September 30, 2008, as a result of the net loss for the nine months and its continued analysis of future taxable income levels and the amount of net deferred tax assets recorded at September 30, 2008. For the three months ended September 30, 2008, the Company recorded an income tax benefit of \$207,000 in order to adjust the cumulative income expense/benefit to \$0 for the nine month period. The Company recorded income tax expense of \$44,000 and \$60,000 for the three and nine months ended September 30, 2007, respectively, which was related to alternative minimum taxes. With the exception of alternative minimum taxes and certain state taxes, the Company will not use cash for income taxes until its net operating losses are fully utilized on its tax returns.

In accordance with SFAS No. 109, *Accounting for Income Taxes*, the Company has assessed the likelihood of realization of its deferred tax assets. The Company has determined that it is not more likely than not that its entire deferred tax asset will be utilized. Therefore, the Company continues to record a valuation allowance against the amount of its deferred tax asset that does not meet the more likely than not threshold. The Company will continue to evaluate this conclusion in future periods. See Footnote 7 of the Company's 2007 Annual Report on Form 10-K for further discussion of the valuation allowance. The Company has also concluded that it does not need to record any reserve for income tax uncertainties under FASB Interpretation No. 48 (*FIN 48*).

- Concentrations.** During the nine months ended September 30, 2008, two customers accounted for 15.8% and 12.8% of the Company's total net sales. At September 30, 2008 these customers represented 14.5% and 16.6% of the Company's total accounts receivable and one other customer represented 11.2% of the Company's total accounts receivable. During the nine months ended September 30, 2007, two customers

accounted for 13.1% and 11% of the Company's total net sales.

Although there are a number of customers that the Company sells to, the loss of a major customer could cause a delay in and possible loss of sales, which would adversely affect operating results.

5. **New Accounting Pronouncements.** In May 2008, the Financial Accounting Standards Board released Statement No. 162, "The Hierarchy of Generally Accepted Accounting Principles" (SFAS No.162). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that presented in conformity with generally accepted accounting principles in the United States of America. SFAS No. 162 will be effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. The Company does not believe SFAS No. 162 will have a significant impact on the Company's financial statements.

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

Overview

Insignia Systems, Inc. markets in-store advertising programs, services and products to retailers and consumer packaged goods manufacturers. The Company's services and products include the Insignia Point-of-Purchase Services (POPS) in-store advertising program, thermal sign card supplies for the Company's SIGNright and Impulse systems, Stylus software and laser printable cardstock and label supplies.

10

Table of Contents

Results of Operations

The following table sets forth, for the periods indicated, certain items in the Company's Statements of Operations as a percentage of total net sales.

	Three Months Ended		Nine Months Ended				
	September 30		September 30				
	2008	2007	2008	2007			
Net sales	100.0	% 100.0	%	100.0	%	100.0	%
Cost of sales	47.7	44.2	45.8	42.9			
Gross profit	52.3	55.8	54.2	57.1			
Operating expenses:							
Selling	29.8	21.7	25.9	22.0			
Marketing	5.2	5.5	5.3	5.4			
Warrant expense (selling & marketing)		23.5		7.8			
General and administrative	23.2	19.3	24.0	18.3			
Total operating expenses	58.2	70.0	55.2	53.5			

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Operating income (loss)	(5.9)	(14.2)	(1.0)	3.6
Other income (expense)	0.5	0.8	0.6	0.5
Income (loss) before taxes	(5.4)	(13.4)	(0.4)	4.1
Income tax expense (benefit)	(2.4)	0.7	0.0	0.4
Net income (loss)	(3.0)%	(14.1)%	(0.4)%	3.7 %

Increased net sales in the first nine months of 2008 compared to the first nine months of 2007 resulted in increased gross profit in 2008. This increase in gross profit was more than offset by increased operating expense in 2008 resulting in a net loss in the first nine months of 2008 as compared to net income in the first nine months of 2007. The increased operating expense in the 2008 period was primarily legal fees and expenses related to the News America litigation and increased sales commissions related to increased sales and higher incentives.

Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Our significant accounting policies are described in Note 1 to the annual financial statements as of and for the year ended December 31, 2007, included in our Form 10-K filed with the Securities and Exchange Commission on March 31, 2008. We believe our most critical accounting policies and estimates include the following:

- revenue recognition;
- allowance for doubtful accounts;
- accounting for deferred income taxes; and
- stock-based compensation.

11

Table of Contents

Three and Nine Months ended September 30, 2008 Compared to Three and Nine Months Ended September 30, 2007

Net Sales. Net sales for the three months ended September 30, 2008, increased 33.1% to \$8,597,000 compared to \$6,461,000 for the three months ended September 30, 2007. Net sales for the nine months ended September 30, 2008, increased 16.6% to \$22,738,000 compared to \$19,495,000 for the nine months ended September 30, 2007.

Service revenues from our POPSign programs for the three months ended September 30, 2008, increased 39.9% to \$7,999,000 compared to \$5,718,000 for the three months ended September 30, 2007. Service revenues from our POPSign programs for the nine months ended September 30, 2008, increased 20.5% to \$20,830,000 compared to \$17,281,000 for the nine months ended September 30, 2007. The increases were primarily due to an increase in the number of POPSign programs executed for customers (consumer packaged goods manufacturers) during the

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

2008 periods which more than offset reductions in the average sign price during the 2008 periods.

Product sales for the three months ended September 30, 2008, decreased 19.5% to \$598,000 compared to \$743,000 for the three months ended September 30, 2007. Product sales for the nine months ended September 30, 2008, decreased 13.8% to \$1,908,000 compared to \$2,214,000 for the nine months ended September 30, 2007. The decreases were primarily due to lower sales of thermal and laser sign card supplies based on decreased demand for those products from our customers.

Gross Profit. Gross profit for the three months ended September 30, 2008, increased 24.7% to \$4,499,000 compared to \$3,608,000 for the three months ended September 30, 2007. Gross profit for the nine months ended September 30, 2008, increased 10.8% to \$12,327,000 compared to \$11,126,000 for the nine months ended September 30, 2007. Gross profit as a percentage of total net sales decreased to 52.3% for the three months ended September 30, 2008, compared to 55.8% for the three months ended September 30, 2007. Gross profit as a percentage of total net sales decreased to 54.2% for the nine months ended September 30, 2008, compared to 57.1% for the nine months ended September 30, 2007.

Gross profit from our POPSign program revenues for the three months ended September 30, 2008, increased 28.5% to \$4,300,000 compared to \$3,346,000 for the three months ended September 30, 2007. Gross profit from our POPSign program revenues for the nine months ended September 30, 2008, increased 13.4% to \$11,640,000 compared to \$10,264,000 for the nine months ended September 30, 2007. The increases in gross profit in the 2008 periods were primarily due to increased sales partially offset by increased costs (primarily retailer expenses). Gross profit as a percentage of POPSign program revenues for the three months ended September 30, 2008, decreased to 53.8% compared to 58.5% for the three months ended September 30, 2007. Gross profit as a percentage of POPSign program revenues for the nine months ended September 30, 2008 decreased to 55.9%, compared to 59.4% for the nine months ended September 30, 2007. The decreases in gross profit as a percentage of POPSign program revenues in the 2008 periods were primarily due to lower average sign prices combined with higher average sign costs (primarily retailer expenses) in the 2008 periods.

Gross profit from our product sales for the three months ended September 30, 2008, decreased 24.0% to \$199,000 compared to \$262,000 for the three months ended September 30, 2007. Gross profit from our product sales for the nine months ended September 30, 2008, decreased 20.3% to \$687,000 compared to \$862,000 for the nine months ended September 30, 2007. The decreases in gross profit in the 2008 periods were primarily due to decreased sales combined with fixed costs. Gross profit as a percentage of product sales was 33.3% for the three months ended September 30, 2008, compared to 35.3% for the three months ended September 30, 2007. Gross profit as a percentage of product sales was 36.0% for the nine months ended September 30, 2008, compared to 38.9% for the nine months ended September 30, 2007. The decreases in gross profit as a percentage of products sales in the 2008 periods were primarily due to decreased sales and the effect of fixed costs.

12

Table of Contents

Operating Expenses

Selling. Selling expenses (exclusive of selling related warrant expense) for the three months ended September 30, 2008, increased 82.9% to \$2,561,000 compared to \$1,400,000 for the three months ended September 30, 2007. Selling expenses (exclusive of selling related warrant expense) for the nine months ended September 30, 2008, increased 36.9% to \$5,878,000 compared to \$4,295,000 for the nine months ended September 30, 2007. Increases in the 2008 periods were primarily due to increased sales commissions, staffing levels and meals and entertainment. The increased sales commissions were due to increased POPSign program sales and the effect of increased incentives for our strategic partner (Valassis Sales & Marketing Services, Inc. (Valassis)) and our employed sales force.

Selling expenses (exclusive of selling related warrant expense) as a percentage of total net sales increased to 29.8% for the three months ended September 30, 2008, compared to 21.7% for the three months ended September 30, 2007. Selling expenses (exclusive of selling related warrant expense) as a percentage of total net sales increased to 25.9% for the nine months ended September 30, 2008, compared to 22.0% for the nine months ended September 30, 2007. The increases in selling expenses as a percentage of total net sales in the 2008 periods was due to the factors described above, partially offset by the effect of increased sales in the 2008 periods.

Marketing. Marketing expenses (exclusive of marketing related warrant expense) for the three months ended September 30, 2008, increased 26.3% to \$451,000 compared to \$357,000 for the three months ended September 30, 2007, primarily due to increased staffing levels and increased data acquisition expense. Marketing expenses (exclusive of marketing related warrant expense) for the nine months ended September 30, 2008, increased 15.1% to \$1,211,000 compared to \$1,052,000 for the nine months ended September 30, 2007, primarily due to increased staffing levels partially offset by decreased data acquisition expense.

Marketing expenses (exclusive of marketing related warrant expense) as a percentage of total net sales decreased to 5.2% for the three months ended September 30, 2008, compared to 5.5% for the three months ended September 30, 2007. Marketing expenses (exclusive of marketing related warrant expense) as a percentage of total net sales decreased to 5.3% for the nine months ended September 30, 2008, compared to 5.4% for the nine months ended September 30, 2007. Decreases in the 2008 periods were primarily due to the increased expenses discussed above which were more than offset by the effect of higher net sales during the 2008 periods.

Warrant expense (selling and marketing). On July 2, 2007, the Company and Valassis, entered into Amendment No. 2 (the Amendment) to the Exclusive Reseller Agreement between the parties. The Amendment extends the term of the strategic alliance between the parties to December 31, 2017. The Amendment also expands the strategic alliance to increase the role of Valassis in developing and expanding the Company's participating retailer network. Valassis received a five-year warrant to acquire 800,000 shares of the Company's common stock at a price of \$4.04 and will be paid a cash commission by the Company on the revenue the Company realizes from POPS programs the consumer packaged goods manufacturers conduct in the new retail chains. The Company recorded \$1,521,000 of expense for the quarter ended September 30, 2007, related to the fair value of the warrant.

General and administrative. General and administrative expenses for the three months ended September 30, 2008, increased 60% to \$1,992,000 compared to \$1,245,000 for the three months ended September 30, 2007. General and administrative expenses for the nine months ended September 30, 2008 increased 52.9% to \$5,457,000 compared to \$3,569,000 for the nine months ended September 30, 2007. The increases in the 2008 periods were primarily due to increased legal expense related to the News America litigation (see below) and increased staffing which were partially offset by receipt of a lease termination payment. The Company received a payment of \$400,000 for early termination of its previous facility lease on July 31, 2008. The payment, net of \$115,000 of moving expense, is recorded as part of general and administrative expenses.

Table of Contents

General and administrative expenses as a percentage of total net sales increased to 23.2% for the three months ended September 30, 2008, compared to 19.3% for the three months ended September 30, 2007. General and administrative expenses as a percentage of total net sales increased to 24.0% for the nine months ended September 30, 2008, compared to 18.3% for the nine months ended September 30, 2007. The increases in the 2008 periods were primarily due to factors discussed above partially mitigated by the effect of higher net sales during the 2008 periods.

Legal fees for the three months ended September 30, 2008, were \$1,526,000 compared to \$496,000 for the three months ended September 30, 2007. Legal fees for the nine months ended September 30, 2008, were \$3,406,000 compared to \$1,388,000 for the nine months ended September 30, 2007. The legal fees in each period were incurred primarily in connection with the News America lawsuit described in Note 2 to the financial statements. Legal fees increased in the 2008 periods primarily due to the increase in activity in the News America litigation as the parties prepare for trial scheduled to commence in 2009. We currently expect the amount of additional legal fees that will be incurred in connection with the ongoing lawsuits to be significant throughout the remainder of 2008 and 2009. Also, if the Company is required to pay a significant amount in settlement or damages, it will have a material adverse effect on its operations and financial condition. In addition, a negative outcome of this litigation could affect long-term competitive aspects of the Company's business.

Other Income (Expense). Other income for the three months ended September 30, 2008, was \$44,000 compared to \$52,000 for the three months ended September 30, 2007, primarily due to lower interest income. Lower interest income rates in the 2008 period more than offset the effect of higher cash balances in the 2008 period. Other income for the nine months ended September 30, 2008, was \$135,000 compared to \$89,000 for the nine months ended September 30, 2007, due to higher interest income and lower interest expense during the 2008 period. During the first nine months of 2008 the effect on interest income of higher cash balances was partially offset by lower interest rates, especially in the second and third quarter of 2008. Interest expense was lower in the nine months ended September 30, 2008, as a result of the expiration of the line of credit on April 30, 2007.

Income Taxes. The Company did not record a cumulative income tax benefit for the nine months ended September 30, 2008, as a result of the net loss for the nine months and its continued analysis of future taxable income levels and the amount of net deferred tax assets recorded at September 30, 2008. For the three months ended September 30, 2008, the Company recorded an income tax benefit of \$207,000 in order to adjust the cumulative income expense/benefit to \$0 for the nine month period. The Company recorded income tax expense of \$44,000 and \$60,000 for the three and nine months ended September 30, 2007, respectively, which was related to alternative minimum taxes.

Net Income (Loss). The net loss for the three months ended September 30, 2008, was \$(254,000) compared to a net loss of \$(907,000) for the three months ended September 30, 2007. The net loss for the nine months ended September 30, 2008, was \$(84,000) compared to net income of \$718,000 for the nine months ended September 30, 2007.

Liquidity and Capital Resources

The Company has financed its operations with proceeds from public and private stock sales and sales of its services and products. At September 30, 2008, working capital was \$6,916,000 compared to \$7,751,000 at December 31, 2007. During the first nine months of 2008, cash and cash equivalents increased by \$943,000 to \$8,336,000 at September 30, 2008, compared to \$7,393,000 at December 31, 2007.

Table of Contents

Net cash provided by operating activities during the nine months ended September 30, 2008, was \$2,493,000. The increase in cash and cash equivalents resulted from the net loss of \$(84,000), non-cash expense of \$660,000 for depreciation, amortization and stock-based compensation expense, and \$1,917,000 of changes to operating assets and liabilities during the nine months ended September 30, 2008.

Edgar Filing: INSIGNIA SYSTEMS INC/MN - Form 10-Q

Net cash of \$987,000 was used in investing activities during the nine months ended September 30, 2008, due to the purchase of property and equipment, primarily the purchase of digital printing equipment, computer hardware and software and leasehold improvements in the new facility. Capital expenditures for the remainder of 2008 are expected to be minimal.

Net cash of \$563,000 was used in financing activities during the nine months ended September 30, 2008. The Company received \$98,000 of proceeds (net of expenses) from the issuance of common stock related to the employee stock purchase plan and exercises of stock options. The Company used \$464,000 (including fees) of cash to repurchase 225,000 shares of common stock as part of the stock repurchase plan adopted in August 2008. The Company also used \$197,000 of cash for the payment of long-term liabilities.

The Company believes that based upon current business conditions, its existing cash balance and future cash from operations will be sufficient for its cash requirements in the foreseeable future. However, there can be no assurances that this will occur or that the Company will be able to secure additional financing from public or private stock sales or from other financing agreements if needed.

Cautionary Statement Regarding Forward-Looking Information

Statements made in this quarterly report on Form 10-Q, in the Company's other SEC filings, in press releases and in oral statements to shareholders and securities analysts, which are not statements of historical or current facts, are forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results or performance of the Company to be materially different from the results or performance expressed or implied by such forward-looking statements. The words believes, expects, anticipates, seeks and similar expressions identify forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date the statement was made. These statements are subject to the risks and uncertainties that could cause actual results to differ materially and adversely from the forward-looking statements. These risks and uncertainties include, but are not limited to, the risks presented in our Annual Report on Form 10-K for the year ended December 31, 2007, and updated in Part II, Item 1A of this Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

The Company's management carried out an evaluation, under the supervision and with the participation of the Company's Chief Executive Officer and the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report, pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Company's Chief Executive Officer and the Company's Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company required to be included in the Company's periodic filings under the Exchange Act.

Table of Contents

(b) Changes in Internal Controls Over Financial Reporting

There was no change in our internal controls over financial reporting that occurred during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION**Item 1. Legal Proceedings**

In August 2000, News America Marketing In-Store, Inc. (News America), brought suit against the Company in U.S. District Court in New York, New York. The case was settled in November 2002. The terms of the settlement agreement are confidential. The settlement did not impact the Company's operating results.

In October 2003, News America brought suit against the Company in U.S. District Court in New York, New York, alleging that the Company has engaged in deceptive acts and practices, has interfered with existing business relationships with retailers and prospective economic advantage, and has engaged in unfair competition. The suit sought unspecified damages and injunctive relief. In February 2007 the U.S. District Court in New York transferred this action to Minnesota where the claims became part of the lawsuit the Company filed against News America and Albertson's Inc. in 2004 (described below), and the New York action was subsequently dismissed.

On September 23, 2004, the Company brought suit against News America and Albertson's Inc. (Albertson's) in Federal District Court in Minneapolis, Minnesota, for violations of federal and state antitrust and false advertising laws, alleging that News America has acquired and maintained monopoly power through various wrongful acts designed to harm the Company in the in-store advertising and promotion products and services market. The suit seeks injunctive relief sufficient to prevent further antitrust injury and an award of treble damages to be determined at trial for the harm caused to the Company. On June 30, 2006 the Court denied the motions of News America and Albertson's to dismiss the suit. On September 20, 2006, the State of Minnesota through its Attorney General intervened as a co-plaintiff in the business disparagement portion of the Minnesota case. In December 2006, News America filed counterclaims in the Minnesota case that included claims similar to those in its New York action against Insignia and one of its officers, plus claims for damages for two alleged incidents of libel and slander. Motions to dismiss the counterclaims were argued in June 2007, and on September 28, 2007 the Court denied the motions to dismiss the counterclaims. The parties are now engaged in pre-trial discovery. Pursuant to Court order, all discovery and pre-trial matters must be completed by May 1, 2009. On February 4, 2008, the Court approved a Consent Decree entered into by News America and the State of Minnesota under which News America agreed to not violate Minnesota's statutes prohibiting commercial disparagement. On July 29, 2008, the Company and Albertson's entered into a Settlement Agreement and Mutual Release, in which they each agreed to release all claims against the other, and the Company agreed to dismiss its lawsuit against Albertson's.

The Company filed claims in December 2006 and January 2007 with its director's and officer's liability and general liability insurers related to the defense costs and insurance coverage for claims asserted against the Company and one of its officers in News America's counterclaims. On August 9, 2007, the Company filed a complaint against the insurers in Hennepin County District Court, State of Minnesota requesting a declaratory judgment that the insurers owe the Company and its officer such defense costs and insurance coverage. In December 2007, the Company settled its claim against one of the insurers, and the litigation is continuing against the other insurer.

Table of Contents

Although management believes that News America's counterclaims are without merit, an evaluation of the likelihood of an unfavorable outcome and an estimate of the potential liability cannot be rendered at this time. If the Company is required to pay a significant amount in settlement or damages, it will have a material adverse effect on its operations and financial condition. In addition, a negative outcome of this litigation could affect long-term competitive aspects of the Company's business.

Management currently expects the amount of legal fees and expenses that will be incurred in connection with the ongoing lawsuits to be significant throughout 2008 and 2009. During the nine months ended September 30, 2008, the Company incurred legal fees and expenses of \$3,270,000 related to the ongoing lawsuits. Legal fees and expenses are expensed as incurred and are included in general and administrative expenses in the statements of operations.

The Company is subject to various other legal proceedings in the normal course of business. Management believes the outcome of these proceedings will not have a material adverse effect on the Company's financial position or results of operations.

Item 1A. Risk Factors

Set forth below is an update to one of the Risk Factors contained in our report on Form 10-K for the year ended December 31, 2007:

We are Dependent On Our Contracts With Retailers And Our Ability To Renew Those Contracts When Their Terms Expire

On an ongoing basis, we negotiate renewals of various retailer contracts. Some of our retailer contracts require us to guarantee minimum payments to our retailers. If we are unable to offer guarantees at the required levels in the new contracts, and the contracts are not renewed because of that or because of other reasons, it will have a material adverse effect on our operations and financial condition.

Our POPS business and results of operations could be adversely affected if the number of retailer partners decreases significantly or if the retailer partners fail to continue to provide good service including performing their duties in placing and maintaining POPS signs at the shelf in their stores and providing product movement data to us.

Our current contract with Safeway Stores was scheduled to expire on June 30, 2008. In May of this year, we entered into an agreement with Safeway to extend the contract to December 31, 2008. Failure to extend the Safeway contract beyond December 31, 2008, could have a material adverse effect on our business.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On August 19, 2008, the Board of Directors authorized the repurchase of up to \$2,000,000 of the Company's common stock on or before July 31, 2009. The plan does not obligate the Company to repurchase any particular number of shares, and may be suspended at any time at the Company's discretion.

17

Table of Contents

Our share repurchase program activity for the three months ended September 30, 2008 was:

	Total Number Of Shares Repurchased	Average Price Paid Per Share	Total Number Of Shares Purchased As Part Of Publicly Announced Plans Or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under The Plans Or Programs
July 1-31, 2008		\$		\$
August 1-31, 2008		\$		\$ 2,000,000
September 1-30, 2008	225,000	\$ 2.04	225,000	\$ 1,541,000
Totals	225,000			

Item 3. Defaults upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Item 6. Exhibits

The following exhibits are included herewith:

- 31.1 Certification of Principal Executive Officer
- 31.2 Certification of Principal Financial Officer
- 32 Section 1350 Certification

18

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.

Dated: November 13, 2008

Insignia Systems, Inc.
(Registrant)

/s/ Scott F. Drill
Scott F. Drill

President and Chief Executive Officer

(principal executive officer)

/s/ Justin W. Shireman
Justin W. Shireman

Vice President, Finance and

Chief Financial Officer

(principal financial officer)

19

Table of Contents

EXHIBIT INDEX

31.1 Certification of Principal Executive Officer

31.2 Certification of Principal Financial Officer

32 Section 1350 Certification

20
