

SPESCOM SOFTWARE INC  
Form S-1  
January 06, 2006

As filed with the Securities and Exchange Commission on January 6, 2006

Registration No. 333-[ ]

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM S-1**

**REGISTRATION STATEMENT  
Under  
THE SECURITIES ACT OF 1933**

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**SPESCOM SOFTWARE INC.**

(Exact Name of Registrant as Specified in Its Charter)

**California**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**7373**  
(Primary Standard Industrial  
Classification Code Number)

**95-3634089**  
(IRS Employer Identification Number)

**10052 Mesa Ridge Court, Suite 100  
San Diego, California 92121  
(858) 625-3000**

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

**Agent for Service:  
John W. Low  
Chief Financial Officer and Secretary**

**Copy to:  
Russell C. Hansen  
Jeffrey N. Petit  
Gibson, Dunn & Crutcher, LLP**

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**Spescom Software Inc.**  
**10052 Mesa Ridge Court, Suite 100**  
**San Diego, California 92121**  
**(858) 625-3000**

**1881 Page Mill Rd.**  
**Palo Alto, CA 94304**  
**(650) 849-5300**

(Name and address, including zip code, and telephone number, including area code, of agent for service)

**Approximate Date of Commencement of Proposed Sale to the Public:** As soon as practicable after the Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended (the Securities Act ), check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

**CALCULATION OF REGISTRATION FEE**

<b>Title of Each Class of Securities to be Registered</b>	<b>Amount to be Registered</b>	<b>Proposed Maximum Offering Price Per Unit</b>	<b>Proposed Maximum Aggregate Offering Price</b>	<b>Amount of Registration Fee</b>
Common Shares, no par value	26,896,552	\$ 0.17	\$ 4,572,414(1)	\$ 489.25
Common Shares, no par value, underlying certain of selling shareholders warrants	925,926	\$ 0.27	\$ 250,000(2)	\$ 26.75
Common Shares, no par value, underlying certain of selling shareholders warrants	300,000	\$ 0.17	\$ 51,000(2)	\$ 5.46
<b>Total</b>	<b>28,122,478</b>		<b>\$</b>	<b>\$ 521.46</b>

(1) Estimated solely for purposes of calculating the registration fee pursuant to Rule 457(c) under the Securities Act of 1933, as amended. The average of the high and low prices as of January 3, 2006 was \$0.17 per share.

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(2) In accordance with Rule 457(g), the proposed maximum aggregate offering price of shares issuable upon the exercise of warrants is based on a proposed maximum offering price per unit equal to the higher of (i) the exercise price of the warrants, (ii) the offering price of the common shares in the registration statement, or (iii) the average sales price of the common shares as determined by 457(c).

**The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.**

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**The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.**

**Subject to Completion, dated January 6, 2006**

**PROSPECTUS**

**28,122,478 Common Shares**

**Spescom Software Inc.**

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The selling shareholders named in this prospectus are offering up to 28,122,478 of our common shares, including up to 26,896,552 common shares to be issued upon conversion of Series H Preferred Stock and the exercise of certain options and warrants. We will not receive any of the proceeds from their sale of our shares, but if the selling shareholders pay the exercise price under any of the options or warrants in cash, we will use those proceeds for general corporate purposes, including working capital.

Our common shares are currently listed on the Over the Counter Bulletin Board ( OTCBB ). Our trading symbol is SPCO.OB.

**Investing in our shares involves a high degree of risk. See Risk Factors beginning on page 6 of this prospectus to read about the risks you should consider before buying our shares.**

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The selling shareholders are offering these common shares. The selling shareholders may sell all or a portion of these shares from time to time in market transactions through any market on which our common shares are then traded, in negotiated transactions or otherwise, and at prices and on terms that will be determined by the then prevailing market price or at negotiated prices directly or through a broker or brokers, who may act as agent or as principal or by a combination of such methods of sale. The selling shareholders will receive all proceeds from the sale of the common shares. For additional information on the methods of sale, you should refer to the section entitled Plan of Distribution.

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

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The date of this prospectus is January 6, 2006

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You may only rely on the information contained in this prospectus or that we have referred you to. We have not authorized anyone to provide you with different information. This prospectus does not constitute an offer to sell or a solicitation of an offer to buy any securities other than the common shares offered by this prospectus. This prospectus does not constitute an offer to sell or a solicitation of an offer to buy any common shares in any circumstances in which such offer or solicitation is unlawful. Neither the delivery of this prospectus nor any sale made in connection with this prospectus shall, under any circumstances, create any implication that there has been no change in our affairs since the date of this prospectus or that the information contained by reference to this prospectus is correct as of any time after its date.

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**INFORMATION REGARDING FORWARD-LOOKING STATEMENTS**





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Some of the statements in Prospectus Summary, Risk Factors, Use of Proceeds and elsewhere in this prospectus, including those using words such as believes, expects, intends, estimates, projects, predicts, assumes, anticipates, plans, and seeks and comparable terms, statements. Forward-looking statements are not statements of historical fact and reflect our views and assumptions as of the date of this prospectus regarding future events and operating performance.

All forward-looking statements address matters that involve risks and uncertainties. There are important factors that could cause our actual results to differ materially from those indicated in these statements. We believe that these factors include but are not limited to those described under Risk Factors, including the following:

The Company's control by and indebtedness to Spescom Ltd.

Our dependence on a small number of new customers

The fluctuation of our operating results

A developing market and rapid technological changes

Our lack of product diversification

Potential violation of our intellectual property rights

Our dependence on third-party software providers

Potential intellectual property infringement claims by third parties

Potential product liability claims by customers

Our potential inability to compete effectively

Potential difficulty for investors to sell their shares of common stock in the Company

Potential volatility of the market price of the Company's common stock

The exercise of outstanding options and warrants would dilute the Company's stock

Fluctuations in foreign currency exchange rates

This list of factors is not exhaustive and should be read with the other cautionary statements that are included in this prospectus.

If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary materially from our projections. Any forward-looking statements you read in this prospectus reflect our current views with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to, among other things, our operations, results of operations, growth strategy and liquidity. All subsequent written and oral forward-looking statements attributable to us or individuals acting on our behalf are expressly qualified in their entirety by this paragraph. You should specifically consider the factors identified in this prospectus that could cause actual results to differ from those discussed in the forward-looking statements before making an investment decision. We undertake no obligation to publicly update or review any forward-looking statement, whether as a result of new information, future events or otherwise.

**PROSPECTUS SUMMARY**



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*This summary highlights information contained elsewhere in this prospectus. Because it is a summary, it does not contain all of the information that you should consider before investing in us. You should read the entire prospectus carefully before making an investment decision. The sections entitled Risk Factors, and Information Regarding Forward-Looking Statements should be read together with the more detailed information in the financial statements and the accompanying notes in the section entitled Financial Statements and Certain Other Financial Information. In this prospectus, references to the Company, we, us or our refer to Spescom Software Inc., except where the context otherwise requires.*

### **Our Company**



## Overview

Spescom Software Inc. (the Company) was founded and incorporated as a California corporation in 1981 and is headquartered in San Diego, California with an international sales and support subsidiary in London, United Kingdom. The Company develops, markets and supports eB®, its integrated suite of collaborative document, configuration and records management software solutions. The Company's eB suite is a set of software technologies that support, improve and enable collaboration among legacy enterprise solutions. The eB suite enables the efficient capture, management and distribution of all types of information across an enterprise. eB's integration of document, configuration and records management functionality onto a single platform is a major differentiator and significant competitive advantage that allows the Company to address the information management needs of an enterprise in a more holistic manner than solutions provided by other vendors.

In 2000, the Company acquired the rights to certain configuration management technology and skills from Spescom Ltd. (Spescom Ltd.), which at the same time acquired a controlling interest in the Company. From this combination of document and configuration management technologies and skills, the Company began doing business as Spescom Software Inc. on October 1, 2001. As of January 3, 2006, Spescom Ltd. owned approximately 56% of the outstanding common shares of the Company after giving effect to the conversion of the shares of the Company's Series F Preferred Stock held by Spescom Ltd.

The document/content management technology developed by the Company and integrated with the configuration management technology developed by Spescom Ltd. provides a powerful solution to the business and information management challenges faced by enterprises that design, build, manage and operate complex products and assets. The combined document and configuration management capabilities of the eB software suite enables it to provide full IDM functionality together with PDM functionality at price points that satisfy a broad range of user needs. The eB suite enables the management of all unstructured information (documents/content) as well as structured information (product/asset/process) on a single platform, thereby enabling change to be managed across both environments.

The Company's integrated document, configuration and records management (iDCR) solutions enable all requirements (design, safety, environmental, etc.), all documents, structured and unstructured, within an enterprise (including office documents, emails, CAD drawings, images, voice and computer print outs), and all data on products, assets, processes, projects and people to be captured, identified and inter-linked. This results in a unified and structured view of all enterprise information and promotes rapid access to relevant information by authorized users in context to their tasks and functions. eB's collaborative workspace environment provides an automated closed-loop change management process that ensures information integrity throughout the enterprise and compliance with legal, regulatory, corporate, audit and quality requirements.

The Company is building its business strategies around two core strengths. First, the Company's software and related services solve critical and recurring problems for companies operating in complex, asset-intensive industries. Second, the Company's software solutions have clear and significant architectural advantages that enable the Company to offer high value solutions to the Company's users as well as to distinguish itself from its competitors. To capitalize on these strengths, the Company has instituted the following strategic initiatives:

Continue to develop and position eB as a critical but complementary enterprise platform.

Continue investment in the Company's direct sales force.

Enter new markets through increased investment in and expansion of strategic partnerships.

Outsource non-core operations.

Opportunistic investing in technology.

Increase the Company's market presence.

The Company intends to continue to extend its position as a technology leader in developing and marketing integrated document, configuration and records management solutions. The Company intends to do this by continuing to enhance the features and functionality of its eB product suite using industry best practices, customer input and feedback and current technologies, including tools to allow users to tailor the look and feel of the product, administrative tools to enable systems operators to easily setup and make changes to the system and add tighter integration with other third party enterprise products. Through this enhanced functionality and integration the Company's products can provide even faster deployment and greater management control of enterprise information. The Company also plans to introduce new products and product extensions which are complementary to its existing suite of products and which address both existing and emerging market needs.

During 2005, the Company released a major update to eB 14 which is the Company's flagship platform based on the Microsoft .NET architecture. This platform has over two years of proven production use in high-volume / high-usage environments. Existing customers continue to migrate to eB Version 14, generating service revenue and new license opportunities. The Company expects that the migration of existing customers will take place over the next 12 to 24 months. In 2005, the eB product was certified by the Institute of Configuration Management, to be compliant with their CMII standard. The Company will continue to enhance its records management capabilities to fully comply with Department of Defense records management standard 5015.2. The Company is developing specific applications for the vertical markets on which the Company has focused, providing additional license and services revenue from existing customers, as well as new marketing and sales opportunities into the selected vertical markets. During 2005, the Company obtained Gold Partner status from Microsoft and is participating in Microsoft beta and new product launch programs, which allows the Company to properly plan for support of the latest and soon to be released computing environments.

The Company's principal executive offices are located at 10052 Mesa Ridge Court, Suite 100, San Diego, California 92121 and the Company's general telephone number is (858) 625-3000.

### **This Offering**

Shares offered by the selling shareholders



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28,122,478, including 26,896,552 shares of common stock issuable upon conversion of the Company's Series H Preferred Stock and 1,225,926 shares of common stock issuable upon exercise of warrants (collectively, the Warrants).

### Use of proceeds

We will not receive any proceeds from the sale of common shares by the selling shareholders. The proceeds from this offering are solely for the account of the selling shareholders. We may receive proceeds from any exercise of the Warrants. Any net proceeds that we receive from any exercise of the Warrants will be used for general corporate purposes, including working capital for our business.

### Risk factors

The purchase of our common stock involves a high degree of risk. You should carefully review and consider Risk Factors beginning on page 6.

### OTC Bulletin Board Trading Symbol

SPCO.OB

**RISK FACTORS**



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*An investment in our shares involves a high degree of risk. Before making an investment decision, you should carefully consider all of the risks described in this prospectus. If any of the risks discussed in this prospectus actually occur, our business, financial condition and results of operations could be materially and adversely affected. If this were to happen, the price of our shares could decline significantly and you may lose all or a part of your investment. The risk factors described below are not the only ones that may affect us. Additional risks and uncertainties that we do not currently know about or that we currently deem immaterial may also adversely affect our business, financial condition and results of operations. Our forward-looking statements in this prospectus are subject to the following risks and uncertainties. Our actual results could differ materially from those anticipated by our forward-looking statements as a result of the risk factors below. See Information Regarding Forward-Looking Statements.*

***The Company has a history of significant losses. If we do not sustain profitability, our financial condition and stock price could suffer.***

The Company has a history of losses and may incur losses in the foreseeable future. We incurred net losses of \$6,049,000, \$223,000 and \$3,004,000 for the fiscal 2005, 2004 and 2003, respectively. As of September 30, 2005, our accumulated deficit was \$90,291,000. If revenues do not reach the levels the Company anticipates, or if operating expenses exceed the Company's expectations, the Company may not be able to achieve or sustain profitability in the near future or at all. If the Company is unable to achieve and sustain profitability at satisfactory levels, its financial condition and stock price could be materially adversely affected.

***The Company will be controlled by Spescom Ltd. and its subsidiaries as long as they are entitled to a majority of the votes eligible to be cast in the election of directors.***

As of January 3, 2006, Spescom Ltd. (together with its subsidiaries), by virtue of its ownership of common stock and Series F Preferred Stock, was entitled to 27,408,249, or 56%, of the total number of votes eligible to be cast in the election of directors. Spescom Ltd. therefore currently has the ability to elect the Company's entire board of directors. Moreover, even if the above-referenced percentage were to drop below 50%, it is likely that Spescom Ltd. would have sufficient votes to retain control of the Company. As a result, Spescom Ltd. will likely continue to control all matters affecting the Company, including but not limited to:

the composition of the Company's board of directors and, through it, any determination with respect to the Company's business direction and policies, including the appointment and removal of officers;

the allocation of business opportunities that may be suitable for the Company and Spescom Ltd.;

any determinations with respect to mergers or other business combinations or extraordinary transactions;

the Company's acquisition or disposition of assets; and

the Company's financing.

Spescom Ltd. is not prohibited from selling a controlling interest in us to a third party.

Notwithstanding the foregoing discussion, if certain affiliates of M.A.G. Capital, LLC become entitled to elect a majority of the authorized directors, as discussed below, Spescom Ltd. would cease to control the Company. Spescom Ltd., however, would continue to exert significant influence over matters other than the election of directors for which shareholder approval is required under applicable law, such as certain types of mergers and other business combinations.

*One or more affiliates of M.A.G. Capital, LLC, as holders of Series H Convertible Preferred Stock, may become entitled to elect a majority of the Board of Directors if certain corporate transactions do not occur on or before April 30, 2006.*

Under the Certificate of Determination for the Series H Convertible Preferred Stock, if the Company has not entered into a binding agreement to consummate a consolidation, merger, or certain other corporate transactions meeting certain requirements on or before April 30, 2006, the holders of Series H Preferred Stock may, by a two-thirds vote not later than June 30, 2006, elect to have all of the outstanding Series H Preferred Stock redeemed by the Company at an amount equal to \$1,000 per share plus all declared but unpaid dividends. If such election is made and the Company does not have sufficient funds to carry out the redemption, the holders of Series H Preferred Stock as a class will be entitled to elect a majority of the authorized directors of the Company.

There are currently 1,950 shares of Series H Preferred Stock outstanding, all held by Monarch Pointe Fund, Ltd. ( Monarch ), an affiliate of M.A.G. Capital, LLC ( MAG ). Under the terms of the Series H Preferred Stock private placement, the Company has agreed to sell 500 additional shares of Series H Preferred Stock to one or more of Monarch, Mercator Momentum Fund, L.P., or Momentum Fund III, L.P., each an affiliate of MAG, at a second closing to occur on or before January 20, 2006. In the event that a corporate transaction of the variety discussed in the preceding paragraph does not occur on or before April 30, 2006 and an election for redemption by the holders of Series H Preferred Stock is made, the redemption price is anticipated to be \$1,950,000 or \$2,450,000, depending on whether an additional 500 shares have been issued in the prospective second closing, plus all declared but unpaid dividends. In the event of such an election, unless the Company is able to raise additional debt or equity funds, the Company anticipates that it would not have sufficient funds to carry out the redemption. If the Company were able to raise additional funds, it is likely that existing shareholders would suffer additional substantial dilution. If the election to redeem the Series H Preferred Stock is made and the Company is unable to pay the redemption price, those MAG affiliates holding Series H Preferred Stock would become entitled to elect a majority of the authorized directors of the Company. In this event, those entities, through their majority control of the Board of Directors, would be able to control or (with respect to matters requiring shareholder approval) exert significant influence over all matters affecting the Company, including:

any determination with respect to the Company's business direction and policies, including the appointment and removal of officers;

the allocation of business opportunities that may be suitable for the Company and Spescom Ltd.;

any determinations with respect to mergers or other business combinations or extraordinary transactions;

the Company's acquisition or disposition of assets; and

the Company's financing.

***The Company has borrowed funds from Spescom Ltd., which debts are secured by all of the Company's assets, and the Company may become insolvent if repayment of such debt is due prior to the Company's ability to obtain funds to repay such debt or if the Company fails to restructure such debt.***

At September 30, 2005, the Company owed, including accrued but unpaid interest, an aggregate amount of \$615,000 to Spescom Ltd. Interest accrues on such debt at an annual interest rate of 10%, and such debt is secured by a security interest in favor of Spescom Ltd. on all of the Company's assets. Spescom Ltd. has agreed to extend the maturity date on such debt until October 1, 2006. In addition the Company owes Spescom Ltd. \$302,000 relating to certain marketing research and analysis that Spescom Ltd. performed on behalf of the Company. The obligation accrues interest at 11% per annum. Spescom Ltd. has agreed to forego payment on the \$302,000 until October 1, 2006. If the Company is unable to generate sufficient cash flow from its operations, secure funds from the capital markets or lenders or restructure its debt to Spescom Ltd., the Company will become insolvent.

***The Company may not be able to rely on Spescom Ltd. to fund its future capital requirements, and financing from other sources may not be available on favorable terms or at all.***

Although the Company in the past has received funding from Spescom Ltd. for working capital purposes, such additional financing if necessary is not assured. The Company may need financing in the future and such financing from Spescom Ltd. or other sources may not be available on favorable terms or at all. In addition, if Spescom Ltd.

is otherwise able to provide additional loans on terms acceptable to the Company, the funding of such loans may be delayed or prevented by currency exchange regulations of the Republic of South Africa, under which Spescom Ltd. is required to apply for and obtain the approval of the South African Reserve Bank before providing any funds to the Company.

The Company believes its capital requirements will vary greatly from quarter to quarter, depending on, among other things, capital expenditures, fluctuations in its operating results, financing activities, and investments and third party products and receivables management. The Company's future liquidity will depend on its ability to generate new system sales of its eB product suite in the near term, which cannot be assured. Failure to generate sufficient system sales to meet the Company's cash flow needs can be expected to have a material adverse effect on the Company's business, results of operations, and financial condition. Management believes that the Company's current cash and receivables, as well as additional cash that may be generated from operations, will be sufficient to meet its short-term needs for working capital. However, the Company may not be able to obtain sufficient orders to enable the Company to continue on a cash flow break-even level, which would be necessary to continue operations in the absence of further financing. Future equity financings would be dilutive to the existing holders of the Company's common stock. Future debt financings could involve restrictive covenants.

***The Company is dependent on sales to a relatively small number of new customers each quarter, so any failure to close a sale to any customer could have a material adverse effect on its quarterly operating results.***

A small number of customers has typically accounted, and will continue in the future to account, for a large percentage of the Company's annual revenues. Network Rail accounted 16% of the Company's revenues in fiscal 2005. Network Rail and Constellation Energy Group accounted for 23% and 15%, respectively of revenues for fiscal 2004 while Network Rail accounted for 19% of revenue for fiscal 2003. Because of the Company's reliance on sales to relatively few customers, the loss of any sale could have a material adverse effect on the results of its operations on any given quarter. Additionally, a significant portion of the Company's revenues has historically been, and is expected in the future to be, derived from the sale of systems to new customers. The Company generally incurs significant marketing and sales expense prior to entering into a contract with a new customer that generates revenues. The length of time it takes to establish a new customer relationship typically ranges from 6 to 12 months. As such, the Company may incur significant expenses associated with its sales efforts directed to prospective customers in any particular period before any associated revenues stream begins. If the Company is not successful at obtaining significant new customers or if a small number of customers cancel or delay their orders for its products, then its business and its prospects could be harmed which may cause the price of the Company's common stock to decline.

***The Company's operating results are difficult to predict and fluctuate substantially from quarter to quarter and year to year, which may increase the difficulty of financial planning and forecasting and may result in declines in the Company's stock price.***

The Company's future operating results may vary from the Company's past operating results, are difficult to predict and may vary from year to year due to a number of factors. Many of these factors are beyond the Company's control. These factors include:

the potential delay in recognizing revenue from license transactions due to revenue recognition rules which the Company must follow;

the tendency to realize a substantial amount of revenue in the last weeks, or even days, of each quarter due to the tendency of some of the Company's customers to wait until quarter or year end in the hope of



obtaining more favorable terms;

customer decisions to delay implementation of the Company's products;

the size and complexity of the Company's license transactions;

any seasonality of technology purchases;

demand for the Company's products, which can fluctuate significantly;

the timing of new product introductions and product enhancements by both the Company and its competitors;

changes in the Company's pricing policy;

the publication of opinions concerning us, the Company's products or technology by industry analysts;

changes in foreign currency exchange rates; and

domestic and international economic and political conditions.

One or more of these factors may cause the Company's operating expenses to be disproportionately high or the Company's gross revenues to be disproportionately low during any given period, which could cause the Company's net revenue and operating results to fluctuate significantly. The Company's operating results have fluctuated significantly in the past. You should not rely on the Company's annual operating results to predict its future results because of the significant fluctuations to which the Company's results are subject.

As a result of these and other factors, operating results for any fiscal year are subject to significant variation, and the Company believes that period-to-period comparisons of its results of operations are not necessarily meaningful in terms of their relation to future performance. You should not rely upon these comparisons as indications of future performance. It is likely that the Company's future quarterly and annual operating results from time to time will not meet the expectations of public market analysts or investors, which could cause a drop in the price of its common stock.

***The Company's market is subject to rapid technological change and if the Company fails to continually enhance its products and services in a timely manner, its revenue and business would be harmed.***

The Company must continue to enhance and improve the performance, functionality and reliability of its products and services in a timely manner. The software industry is characterized by rapid technological change, changes in user requirements and preferences, frequent new product and services introductions embodying new technologies, and the emergence of new industry standards and practices that could render the Company's products and services obsolete. The Company has experienced product development delays in the past, and may experience delays in the future. The Company's failure to continually enhance its products and services in a timely manner would adversely impact its business and prospects. In the past, the Company has also discovered that some of its customers desire additional performance and functionality not currently offered by its products. The Company's success will depend, in part, on its ability to internally develop and license leading

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technologies to enhance its existing products and services, to develop new products and services that address the increasingly sophisticated and varied needs of its customers, and to respond to technological advances and emerging industry standards and practices on a cost-effective and timely basis. The Company's product development efforts with respect to its eB product suite are expected to continue to require substantial investments by the Company, and the Company may not have sufficient resources to make the necessary investments. If the Company is unable to adapt its products and services to changing market conditions, customer requirements or emerging industry standards, it may not be able to maintain or increase its revenue and expand its business.

*The Company's lack of product diversification means that any decline in price or demand for its products and services would seriously harm its business.*

The eB product suite and related services have accounted for substantially all of the Company's revenue and this situation is expected to continue for the foreseeable future. Consequently, a decline in the price of, or demand for, the eB product suite or related services, or their failure to achieve broad market acceptance, would seriously harm the Company's business.

***Significant unauthorized use of the Company's products would result in material loss of potential revenues and the Company's pursuit of protection for its intellectual property rights could result in substantial costs to it.***

The Company's software is licensed to customers under license agreements containing provisions prohibiting the unauthorized use, copying and transfer of the licensed program. Policing unauthorized use of the Company's products is difficult and, while the Company is unable to determine the extent to which piracy of its software products exists, any significant piracy of its products could materially and adversely affect the Company's business, results of operations and financial condition. In addition, the laws of some foreign countries do not protect the Company's proprietary rights to as great an extent as do the laws of the United States and the Company's means of protecting its proprietary rights may not be adequate.

***The Company relies on third party software products incorporated in its products. Any loss of use to such third party software could result in delays in the Company's product shipments.***

The Company relies on certain software that it licenses from third parties, including software that is integrated with internally developed software and used in the Company's products to perform key functions. There can be no assurances that the developers of such software will remain in business, that they will continue to support their products, that their products will otherwise continue to be available to the Company on commercially reasonable terms or that their products are free from bugs or defects. The loss of or inability to maintain any of these software licenses could result in delays or reductions in product shipments until equivalent software can be developed, identified, licensed and integrated, which could adversely affect the Company's business, operating results and financial condition.

***If third parties claim that the Company infringes on their patents, trademarks, or other intellectual property rights, it may result in costly litigation or require the Company to make royalty payments.***

The Company is not aware that any of its software products infringe the proprietary rights of third parties. There can be no assurance, however, that third parties will not claim infringement by the Company with respect to its current or future products. The Company expects that software product developers will increasingly be subject to infringement claims. Any such claims, with or without merit, could be time-consuming, result in costly litigation, cause product shipment delays, consume significant management time or require the Company to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to the Company or at all, which could have a material adverse effect on the Company's business, results of operations and financial condition.

***The Company may face product liability claims from its customers.***

The Company's license agreements with its customers usually contain provisions designed to limit its exposure to potential product liability claims. It is possible, however, that the limitation of liability provisions contained in the Company's license agreements may not be effective under the laws of some jurisdictions. A successful product liability claim brought against the Company could result in payment by the Company of substantial damages, which would harm its business, operating results and financial condition and cause the price of its common stock to fall.

***If the Company loses key personnel, or is unable to attract and retain additional key personnel, the Company may not be able to successfully grow and manage its business.***

The Company believes that its future success will depend upon its ability to attract and retain its key technical and management personnel. These employees are not subject to employment contracts. The Company may not be successful in retaining its key employees in the future or in attracting and assimilating replacement or additional key personnel. Any failure in retaining and attracting management personnel may impair its ability to rapidly grow and manage its business.

*The Company faces intense competition from several competitors and may be unable to compete successfully.*

The market for the Company's products is intensely competitive, subject to rapid change and significantly affected by new product introductions and other market activities of industry participants. The Company currently encounters competition from a number of public and private companies, including Electronic Document Management System/Enterprise Content Management vendors such as EMC (formerly Documentum), FileNet,

OpenText, Sword and Hummingbird; Enterprise Asset Management vendors such as Indus and MRO/Maximo; and to a lesser extent Product Data Management/Product Lifecycle Management vendors such as Matrix I, PTC and EDS. Many of these direct competitors have significantly greater financial, technical, marketing and other resources than the Company. The Company also expects that direct competition will increase as a result of recent consolidation in the software industry.

The Company also faces indirect competition from systems integrators and VARs. The Company relies on a number of systems consulting and systems integration firms for implementation and other customer support services, as well as for recommendation of its products to potential purchasers. Although the Company seeks to maintain close relationships with these service providers, many of these third parties have similar, and often more established, relationships with the Company's principal competitors. If the Company were unable to develop and retain effective, long-term relationships with these third parties, the Company's competitive position would be materially and adversely affected. Further, these third parties may market software products in competition with the Company in the future and may otherwise reduce or discontinue their relationship with, or support of, the Company and its products.

In addition, database vendors, such as Oracle, IBM and Microsoft are potential competitors in the future if they acquire competitive technology or otherwise expand their current product offerings. Like the Company's current competitors, these companies have longer operating histories, significantly greater financial, technical, marketing and other resources and name recognition and a larger installed base of customers than the Company. Several of these companies, including Oracle, Microsoft, IBM and others, have well-established relationships with the Company's current and potential customers and strategic partners, as well as extensive resources and knowledge of the enterprise software industry that may enable them to offer a single-vendor solution more easily than the Company can. In addition, the Company's competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements, or to devote greater resources to the development, promotion and sale of their products than the Company can. If the Company cannot respond to its competitors adequately and in a timely manner, then it may be required to reduce prices for its products and could suffer reduced gross margins and loss of market share, any of which could harm its business, prospects, financial condition and operating results, causing the price of its common stock to decline. In addition, the Company's past financial losses and customer uncertainty regarding the Company's financial condition are likely to have a material adverse effect on the Company's ability to sell its products in the future against competitors.

*The Company's common stock is deemed to be penny stock, which may make it more difficult for investors to sell their shares due to suitability requirements.*

The Company's common stock is deemed to be penny stock as that term is defined in Rule 3a51-1 promulgated under the Securities Exchange Act of 1934. These requirements may reduce the potential market for the Company's common stock by reducing the number of potential investors. This may make it more difficult for investors in the Company's common stock to sell shares to third parties or to otherwise dispose of them. This could cause the Company's stock price to decline. Penny stock is stock:

With a price of less than \$5.00 per share;

That is not traded on a recognized national exchange;

Whose prices are not quoted on the NASDAQ automated quotation system (NASDAQ listed stock must still have a price of not less than \$5.00 per share); or

In issuers with net tangible assets less than or equal to \$2.0 million (if the issuer has been in continuous operation for at least three years) or \$5.0 million (if in continuous operation for less than three years), or with average revenues of less than \$6.0 million for the last three years.

Broker/dealers dealing in penny stocks are required to provide potential investors with a document disclosing the risks of penny stock. Moreover, broker/dealers are required to determine whether an investment in a penny stock is a suitable investment for a prospective investor.

***The Company's common stock trades sporadically; the market price of the Company's common stock may be volatile.***

The Company's common stock currently trades sporadically on the OTC Bulletin Board. The market for the Company's common stock may continue to be an inactive market, and the market price of the Company's common stock may experience significant volatility. The Company's quarterly results, failure to meet analysts' expectations, announcements by the Company or its competitors regarding acquisitions or dispositions, loss of existing customers, new industry standards or technology, changes in general conditions in the economy, and general market conditions could cause the market price of the common stock to fluctuate substantially. In addition, the stock market has experienced significant price and volume fluctuations that have particularly affected the trading prices of equity securities of many technology companies. These price and volume fluctuations often have been unrelated to the operating performance of the affected companies.

***Conversion of the Company's preferred stock will result in significant dilution to existing shareholders.***

In October 2005 the Company completed the first closing of a private placement to issue, in addition to certain warrants, a new Series H Convertible Preferred Stock which upon conversion into common stock will result in substantial dilution to common shareholders. Additional Series H Preferred Stock and warrants may be issued at a second closing which is anticipated to occur in January 2006. The number of shares of the Company's common stock into which shares of Series H Preferred Stock may be converted varies based on a volume-weighted measure of the market price of the common stock and based on the trailing revenues of the last four fiscal quarters reported by the Company. The shares of preferred stock issued at the first closing and the shares subject to issuance at the second closing are convertible into no fewer than 4,875,000 and 1,250,000 common shares, respectively and into no more than 26,896,552 and 6,896,552 common shares, respectively if the Company's trailing revenues of the last four fiscal quarters were to be less than \$5 million.

On September 30, 2003, the Company issued 5,291 shares of Series F Preferred Stock with a stated value of \$1,000 per share in consideration of the cancellation of \$5,291,000 of its debt owed to Spescom Ltd. and its subsidiary. The Series F Preferred Stock is convertible into the Company's common stock at a stated conversion price of \$0.45 per share, subject to certain adjustments to prevent dilution, representing a total of 11,757,778 shares of the Company's common stock. Such conversion may occur at the option of the holder until September 30, 2008. On that date, any outstanding Series F Preferred Stock not previously converted will be converted automatically. Conversion of the Series F Preferred Stock will result in substantial dilution to common shareholders.

***Future sales of common stock by the Company's shareholders, including investors in future offerings and Spescom Ltd., could adversely affect the Company's stock price.***

As part of the Series H Convertible Preferred Stock private placement completed in October 2005, the Company agreed to file a registration statement for the common stock of the Company issuable upon conversion of such preferred stock. Any sales of these shares of common stock or shares of the Company's common stock issued in any future offering could cause a decline in the price of the Company's stock. In addition, Spescom Ltd. holds 27,408,249 shares of the Company's common stock on a fully diluted basis as of January 3, 2006, and if it sells its shares of the Company from time to time in the future, the Company's stock price may be adversely affected. Spescom Ltd. also has certain demand and piggyback registration rights relating to 11,757,778 of these shares.

***The exercise of outstanding options and warrants would result in dilution of the Company's stock.***



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As of September 30, 2005, the Company had outstanding stock options to purchase approximately 4,856,000 shares of common stock and warrants to purchase approximately 5,492,502 shares of common stock. If all or a significant number of the options are exercised, shareholders could suffer significant dilution.

*The Company is subject to significant foreign currency fluctuations which may have a material adverse effect on the Company's business and financial results.*

Changes in foreign currency rates, the condition of local economies, and the general volatility of software markets may result in a higher or lower proportion of foreign revenues in the future. Although the Company's operating and

pricing strategies take into account changes in exchange rates over time, future fluctuations in the value of foreign currencies may have a material adverse effect on the Company's business, operating results and financial condition.

*Beginning in fiscal 2006 under SFAS 123R the Company will begin recording compensation expense in connection with the incentive stock options provided to its employees and directors which may have a significant negative impact on future operating results.*

In December 2004, the FASB issued SFAS 123R which requires companies to measure all employee stock-based compensation awards using a fair value method and record such expense in the Company's consolidated financial statements. The impact of adoption of SFAS 123R cannot be predicted at this time because it will depend on, among other things, levels of share-based payments granted in the future, the market value of the Company's common stock as well as assumptions regarding a number of complex variables. These variables include, but are not limited to, the Company's stock price, volatility, and employee stock option exercise behaviors and the related tax impact. However, the expense recorded in future periods may significantly impact future earnings of the Company.

#### **USE OF PROCEEDS**

We will not receive any proceeds from the sale of common shares by the selling shareholders. The proceeds from this offering are solely for the account of the selling shareholders. We may receive proceeds if the Warrants are exercised. Any net proceeds that we receive from any exercise of the Warrants will be used for general corporate purposes, including working capital for our business.

**DILUTION**

The following table compares the \$0.11 offering price (the average of the high and low price of the shares in December 15, 2005) of the shares to the cost to our existing shareholders of shares of common stock that they acquired from us within the past five years, that are issuable upon conversion of outstanding shares of preferred stock acquired from us within the past five years, or that they have the right to acquire from us under outstanding stock options or warrants.

	Shares Purchased		Total Consideration		Average price per share
	Number	Percent	Amount	Percent (3)	
Existing stockholders	58,662,721(1)	68%	\$ 13,065,843(4)	82%	\$ 0.22(6)
New investors	28,122,478(2)	32%	\$ 2,952,860(5)	18%	\$ 0.11(7)
Total	86,785,199	100%	\$ 16,018,703	100%	

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(1) The number of shares of our common stock currently outstanding that were purchased from us within the five years ended December 15, 2005 plus the number of shares of common stock that are issuable upon the conversion of outstanding shares of preferred stock that were purchased from us within the past five years, plus the number of shares issuable upon the exercise of currently outstanding stock options and warrants.

(2) The maximum number of shares being offered to investors in this offering.

(3) The percent that each number represents of the sum of both numbers.

(4) The sum of the price paid to us for all shares of common stock purchased from us within the five years ended December 15, 2005 (including shares of preferred stock that are convertible into common stock) and the aggregate exercise price of all currently outstanding stock options and warrants.

(5) The product of an assumed offering price of \$0.11 per share (the average of the high and low price of the shares on December 15, 2005) and the aggregate maximum number of shares being offered to investors in the offering.

(6) The weighted average price of all shares purchased from us within the five years ended December 15, 2005 (including shares of preferred stock that are convertible into common stock) and the exercise price of all currently outstanding stock options and warrants.

(7) For purposes of this table, we have assumed an offering price of \$0.11 per share (the average of the high and low price of the shares on December 15, 2005).

Our net tangible book value as of September 30, 2005 was approximately (\$5,465,000), or (\$0.07) per share of our common stock. If you invest in our common stock, your interest will be diluted to the extent of the difference between the price you pay per share of our common stock and the net tangible book value per share of our common stock at the time of your purchase. Net tangible book value per share is calculated by subtracting our total liabilities from our total tangible assets, and dividing this amount by the number of shares of our common stock issued and outstanding after giving effect to the conversion of all shares of our outstanding preferred stock. The sale of shares of common stock in this offering by the selling shareholders will not affect our net tangible book value because we will not receive any proceeds from their sale of our common stock. Based on our net tangible book value as of September 30, 2005 and assuming an offering price of \$0.11 per share, investors in this offering will experience immediate and substantial dilution of \$0.18 per share.

The foregoing discussion is based upon the number of shares actually issued and outstanding as of December 15, 2005, which assumes the conversion of all of our outstanding shares of preferred stock into 38,654,330 shares of common stock. As of that date, there were 13,756,428 options and warrants outstanding at a weighted average exercise price of \$0.32 per share and there were a total of 2,262,962 shares available for future awards under our stock incentive plans. To the extent outstanding options or warrants are exercised, you may experience further dilution.

In addition, we may choose to raise additional capital due to market conditions or strategic considerations even if we believe we have sufficient funds for our current or future operating plans. To the extent that additional capital is raised through the sale of equity or convertible debt securities, the issuance of these securities could result in further dilution to our shareholders.

**SELLING SHAREHOLDERS**

The following table sets forth the number of common shares beneficially owned by each of the selling shareholders as of January 3, 2006, except as provided in footnote 4 below. To our knowledge, except as provided in footnote 3 below, none of the selling shareholders has had a material relationship with us within the past three years other than as a result of the ownership of the shares covered by this prospectus. Because the selling shareholders may offer all or some of the shares which they hold pursuant to the offering contemplated by this prospectus, and because there are currently no agreements, arrangements or understandings with respect to the sale of any of the shares, no definitive estimate can be given as to the amount of shares that will be held by the selling shareholders after completion of this offering and the following table has been prepared on the assumption that all options and warrants will be exercised and all common shares offered hereby will be sold. The selling shareholders named below are not obligated to sell any of the shares shown as offered by them below but may offer the shares offered by this prospectus from time to time.

Name of Shareholder	Shares beneficially owned before offering		Shares being offered	Shares beneficially owned after offering	
	Common Shares	Common Shares issuable on conversion of Preferred Stock and/or exercise of warrants		Number of Shares	Percent of Class
Monarch Pointe Fund, Ltd. (1)(3)	3,081,083	29,559,515	27,359,515	5,281,083	17%
M. A. G. Capital, LLC (2)(3)	0	1,012,963	462,963	550,000	2%
Liolios Group, Inc. (4)	0	300,000	300,000	0	0%
Total	3,081,083	30,322,478	28,122,478	5,831,083	19%

This table is based upon information supplied by the selling shareholders.

(1) M. A. G. Capital, LLC ( MAG ) controls the investments of Monarch Pointe Fund, Ltd. ( Monarch ). David F. Firestone is the Managing Member of MAG. The right to vote and the right to dispose of the shares beneficially owned by Monarch are shared among Monarch, MAG and David Firestone. See footnote 5 to the table provided under Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters, page 51.

(2) David Firestone is the Managing Member of MAG. The right to vote and the right to dispose of the shares beneficially owned by MAG are shared by MAG and David F. Firestone.

(3) On November 4, 2004, the Company issued 1) 2,200 shares of Series G Convertible Preferred Stock to Monarch and 2) warrants, which expire November 5, 2007, to purchase an aggregate of 2.75 million shares of common stock at \$0.44 per share to Monarch and MAG, which was then named Mercator Advisory Group, LLC. The aggregate purchase price of the Series G Convertible Preferred Stock and warrants was \$2.2 million. During fiscal 2005, 750 shares of this preferred stock was converted into 2,428,000 shares of common stock. The remaining 1,450 shares of this preferred stock were transferred to the Company on October 25, 2005 in connection with the first closing of the private placement of Series H Preferred Stock.

(4) The Company anticipates the issuance of warrants for the purchase of up to an aggregate of 300,000 common shares to Liolios Group, Inc. pursuant to an agreement entered into between the parties on November 15, 2005, as further described under The Warrants on pages 19 and 20.

**PLAN OF DISTRIBUTION**



The selling shareholders, or their pledgees, donees, transferees, or any of their successors in interest selling shares received from a named selling shareholder as a gift, partnership distribution or other non-sale-related transfer after the date of this prospectus (all of whom may be selling shareholders) may sell the common shares offered by this prospectus from time to time on any stock exchange or automated interdealer quotation system on which the common shares are listed or quoted at the time of sale, in the over-the-counter market, in privately negotiated

transactions or otherwise, at fixed prices that may be changed, at market prices prevailing at the time of sale, at prices related to prevailing market prices or at prices otherwise negotiated. The selling shareholders may sell the common shares by one or more of the following methods, without limitation:

Block trades in which the broker or dealer so engaged will attempt to sell the common shares as agent but may position and resell a portion of the block as principal to facilitate the transaction;

An exchange distribution in accordance with the rules of any stock exchange on which the common shares are listed;

Ordinary brokerage transactions and transactions in which the broker solicits purchases;

Privately negotiated transactions;

In connection with short sales of Company shares;

Through the distribution of common shares by any selling shareholder to its partners, members or stockholders;

By pledge to secure debts of other obligations;

In connection with the writing of non-traded and exchange-traded call options, in hedge transactions and in settlement of other transactions in standardized or over-the-counter options;

Purchases by a broker-dealer as principal and resale by the broker-dealer for its account; or

In a combination of any of the above.

These transactions may include crosses, which are transactions in which the same broker acts as an agent on both sides of the trade. The selling shareholders may also transfer the common shares by gift. We do not know of any arrangements by the selling shareholders for the sale of any of the common shares.

The selling shareholders may engage brokers and dealers, and any brokers or dealers may arrange for other brokers or dealers to participate in effecting sales of the common shares. These brokers or dealers may act as principals, or as an agent of a selling shareholder. Broker-dealers may agree with a selling shareholder to sell a specified number of the shares at a stipulated price per share. If the broker-dealer is unable to sell common shares acting as agent for a selling shareholder, it may purchase as principal any unsold shares at the stipulated price. Broker-dealers who acquire common shares as principals may thereafter resell the shares from time to time in transactions in any stock exchange or automated interdealer quotation system on which the common shares are then listed, at prices and on terms then prevailing at the time of sale, at prices related to the then-current market price or in negotiated transactions. Broker-dealers may use block transactions and sales to and through broker-dealers, including transactions of the nature described above. The selling shareholders may also sell the common shares in accordance with Rule 144 or Rule 144A under the Securities Act, rather than pursuant to this prospectus. In order to comply with the securities laws of some states, if applicable, the shares of common stock may be sold in these jurisdictions only through registered or licensed brokers or dealers.

From time to time, one or more of the selling shareholders may pledge, hypothecate or grant a security interest in some or all of the shares owned by them. The pledgees, secured parties or person to whom the shares have been hypothecated will, upon foreclosure in the event of default, be deemed to be selling shareholders. The number of a selling shareholder's shares offered under this prospectus will decrease as and when it takes such actions. The plan of distribution for that selling shareholder's shares will otherwise remain unchanged. In addition, a selling shareholder may, from time to time, sell the shares short, and, in those instances, this prospectus may be delivered in connection with the short sales and the shares offered under this prospectus may be used to cover short sales.

To the extent required under the Securities Act, the aggregate amount of selling shareholders' shares being offered and the terms of the offering, the names of any agents, brokers, dealers or underwriters, any applicable commission

and other material facts with respect to a particular offer will be set forth in an accompanying prospectus supplement or a post-effective amendment to the registration statement of which this prospectus is a part, as appropriate. Any underwriters, dealers, brokers or agents participating in the distribution of the common shares may receive compensation in the form of underwriting discounts, concessions, commissions or fees from a selling shareholder and/or purchasers of selling shareholders' shares, for whom they may act (which compensation as to a particular broker-dealer might be less than or in excess of customary commissions). Neither we nor any selling shareholder can presently estimate the amount of any such compensation.

The selling shareholders and any underwriters, brokers, dealers or agents that participate in the distribution of the common shares may be deemed to be underwriters within the meaning of the Securities Act, and any discounts, concessions, commissions or fees received by them and any profit on the resale of the securities sold by them may be deemed to be underwriting discounts and commissions. If a selling shareholder is deemed to be an underwriter, the selling shareholder may be subject to certain statutory liabilities including, but not limited to Sections 11, 12 and 17 of the Securities Act and Rule 10b-5 under the Exchange Act. Selling shareholders who are deemed underwriters within the meaning of the Securities Act will be subject to the prospectus delivery requirements of the Securities Act. The SEC staff is of a view that selling shareholders who are registered broker-dealers or affiliates of registered broker-dealers may be underwriters under the Securities Act. We will not pay any compensation or give any discounts or commissions to any underwriter in connection with the securities being offered by this prospectus.

A selling shareholder may enter into hedging transactions with broker-dealers and the broker-dealers may engage in short sales of the common shares in the course of hedging the positions they assume with that selling shareholder, including, without limitation, in connection with distributions of the common shares by those broker-dealers. A selling shareholder may enter into option or other transactions with broker-dealers, who may then resell or otherwise transfer those common shares. A selling shareholder may also loan or pledge the common shares offered hereby to a broker-dealer and the broker-dealer may sell the common shares offered by this prospectus so loaned or upon a default may sell or otherwise transfer the pledged common shares offered by this prospectus.

The selling shareholders and other persons participating in the sale or distribution of the common shares will be subject to applicable provisions of the Exchange Act, and the rules and regulations under the Exchange Act, including Regulation M. This regulation may limit the timing of purchases and sales of any of the common shares by the selling shareholders and any other person. The anti-manipulation rules under the Exchange Act may apply to sales of common shares in the market and to the activities of the selling shareholders and their affiliates. Regulation M may restrict the ability of any person engaged in the distribution of the common shares to engage in market-making activities with respect to the particular common shares being distributed for a period of up to five business days before the distribution. These restrictions may affect the marketability of the common shares and the ability of any person or entity to engage in market-making activities with respect to the common shares.

We have agreed to indemnify the selling shareholders who participated in our October 25, 2005 private placement (the "Private Placement Shareholders") and any brokers, dealers and agents who may be deemed to be underwriters, if any, of the common shares offered by this prospectus, against specified liabilities, including liabilities under the Securities Act.

We will not receive any proceeds from sales of any common shares by the selling shareholders. We may receive proceeds upon the exercise of the Warrants. Any net proceeds that we receive from any exercise of the Warrants will be used for general corporate purposes, including working capital for our business.

We cannot assure you that the selling shareholders will sell all or any portion of the common shares offered by this prospectus. In addition, we cannot assure you that a selling shareholder will not transfer the shares of our common stock by other means not described in this prospectus.



**DESCRIPTION OF CAPITAL STOCK**

## **Authorized Stock**

As of the date of this prospectus, our authorized capital stock consists of 100,000,000 shares of common stock, no par value, and 1,000,000 shares of preferred stock, no par value. As of December 15, 2005, our issued and outstanding shares of capital stock consists of 36,818,528 common shares, 5,291 shares of Series F Preferred stock, and 1,950 shares of Series H Preferred Stock. These numbers exclude the approximately 1,225,926 common shares issuable upon the exercise of the Warrants, 7,717,502 shares issuable under other warrants, 4,813,000 common shares issuable pursuant to outstanding options under the Company's equity compensation plans, and 2,262,962 common shares currently available for future issuance under the Company's equity compensation plans.

## **Common Shares**

The holders of common stock are entitled to one vote per share on all matters voted on by the shareholders, including elections of directors. Subject to preferences that may apply to any of our outstanding preferred stock, holders of our common stock will receive ratably any dividends our board of directors declares out of funds legally available therefore, and in the event of liquidation or dissolution of the Company, are entitled to share in all assets remaining after payment of liabilities and any liquidation preference of any of our outstanding preferred stock. Our common stock has no preemptive rights, conversion rights, or other subscription rights or redemption or sinking fund provisions. The shares of our common stock to be issued upon completion of this offering will be fully paid and non-assessable.

## **Series F Convertible 5% Preferred Stock**

On September 30, 2003, the Company issued 5,291 shares of Series F Preferred Stock (the Series F Preferred Shares) with a stated value of \$1,000 per share in consideration of the cancellation of \$5,291,000 of its debt owed to Spescom Ltd. and its subsidiary. The Series F Preferred Shares are convertible into the Company's common stock, at a stated conversion price of \$0.45 per share, representing a total of 11,757,778 shares of the Company's common stock, subject to certain adjustments to prevent dilution. Such conversion may occur at the option of the holder until September 30, 2008. On that date, any outstanding Series F Preferred Shares not previously converted are to be converted automatically.

The Series F Preferred Shares are entitled to a liquidation preference equal to \$1,000 per share, plus accrued but unpaid dividends per share and interest on all accrued but unpaid dividends. The Series F Preferred Shares are also entitled to receive dividends of 5% of the stated value of \$1,000 per share per annum, payable on a quarterly basis in cash or common stock (valued on the basis of the average per share market value on the 30 trading days immediately prior to the date on which such dividend is declared by the Board of Directors). Unpaid dividends, if any, accrue interest at the rate of 8% per annum. As part of the transaction, Spescom Ltd. and its U.K. subsidiary received certain demand and piggyback registration rights with respect to the common stock underlying the Series F Preferred Shares. Each holder of Series F Preferred Shares is entitled to the number of votes equal to the number of shares of common stock to which such holder would be entitled upon conversion of the Series F Preferred Shares held by such holder on all matters submitted to the vote of the holders of common stock, and votes as a class with the holders of common stock. In a change of control, merger or sale, the holders of Series F Preferred Shares would preserve their conversion rights and would be entitled to the same number of shares immediately prior to such transaction.

## **Series H Convertible Preferred Stock**

On the Company entered into a definitive agreement relating to a private placement with Monarch Pointe Fund, Ltd. ( Monarch ) and M.A.G. Capital, LLC ( MAG ). As further described below, the terms of the financing provide, subject to certain conditions, for the issuance by the Company at two closings of an aggregate of 2,450 shares of Series H Convertible Preferred Stock ( Series H Preferred Stock ) and warrants to purchase an aggregate of 1,851,852 shares of common stock at \$0.27 per share, at an aggregate purchase price of \$1,000,000.

The first closing of the transaction took place on October 25, 2005. At the first closing, the Company issued 1,950 shares of Series H Preferred Stock, and warrants, expiring October 25, 2008, to purchase 925,926 shares of common stock at \$0.27 per share. The preferred stock issued at the first closing is convertible into up to 26,896,552 shares of common stock. In connection with the first closing, Monarch transferred 1,450 shares of the Company s Series G Convertible Preferred Stock to the Company for cancellation. The aggregate consideration paid by the investors for



the preferred stock and warrants issued at the first closing was \$500,000 and the 1,450 shares of Series G Convertible Preferred Stock transferred by Monarch. As part of the financing the Company has agreed to use commercially reasonable efforts to register by December 31, 2005 the common shares issuable under the Series H Preferred Stock and related warrants. Monarch and MAG have agreed to extend the registration date to January 6, 2006.

Under the terms of the financing, the second closing will occur no later than January 20, 2006, provided that the investors are not obligated to consummate the second closing unless certain conditions are satisfied. The financing terms provide for the issuance by the Company at the second closing of 500 shares of Series H Preferred Stock and warrants, expiring on the third anniversary of the second closing, to purchase 925,926 shares of common stock at \$0.27 per share. The preferred stock subject to issuance at the second closing is convertible into up to 6,896,552 shares of common stock. The financing terms provide that the investors participating in the second closing will be MAG and one or more of Monarch, Mercator Momentum Fund, L.P., or Momentum Fund III, L.P., as designated by MAG. The aggregate purchase price of the preferred stock and warrants subject to issuance at the second closing is \$500,000.

If the Company has not entered into a binding agreement to consummate a consolidation, merger, reclassification of the stock of the Company (subject to certain exceptions), or disposition of all or substantially all of the assets of the Company, on or before April 30, 2006, the holders of Series H Preferred Stock may, by the vote not later than June 30, 2006 of at least two-thirds of the then-outstanding shares, elect to have all of the outstanding shares of Series H Preferred Stock redeemed by the Company. Upon such election, the Company would be obligated to redeem the Series H Preferred Stock at an amount equal to \$1000 per share plus all declared but unpaid dividends. In the event that the holders of Series H Preferred Stock exercise their redemption right but the Company does not have sufficient funds available to redeem the Series H Preferred Stock in accordance with applicable law, the holders of Series H Preferred Stock as a class will be entitled to elect the smallest number of directors of the Company constituting a majority of the authorized number of directors.

The Series H Preferred Stock shares issued at the first closing and those subject to issuance at the second closing are convertible into common stock at the conversion rate in effect at the time of conversion. The conversion price per share of the Series H Preferred Stock is equal to 85% of the market price (the volume weighted average price of the Company's common stock during the 5 immediately preceding trading days, subject to adjustment), provided that in no event shall the conversion price exceed a ceiling price of \$0.40 per share, or be less than a floor price which varies with the aggregate gross revenues of the Company during the last four fiscal quarters for which revenues have been reported by the Company prior to such time, but which will not be lower than \$0.0725 per share and not higher than \$0.16 per share. The conversion price is subject to adjustment in the case of any stock split, combination, capital reorganization, reclassification, consolidation or merger, and certain dividends. Subject to certain exceptions, the conversion price is also subject to weighted average anti-dilution adjustment in the case of an issuance of shares of common stock or securities exercisable for or convertible into common stock, at a per share price, exercise price or conversion price less than the conversion price then in effect.

### **The Warrants**

As of December 15, 2005, warrants to purchase a total of 6,443,428 shares of our common stock were outstanding. Of such shares, 925,926 are issuable under warrants issued on October 25, 2005 together with shares of preferred stock in the private offering of Series H Preferred Stock to Monarch Pointe Fund, Ltd. ( Monarch ). Of such warrants, 462,963 were issued to Monarch and 462,963 were issued to its affiliate, M. A. G. Capital, LLC ( MAG ), which was formerly named Mercator Advisory Group, LLC. Those warrants have an exercise price of \$0.27 per share and expire on October 25, 2008. The warrants prohibit any exercise thereof that would result in the holder owning beneficially more than 9.99% of the outstanding shares of Common Stock of the Company as determined under Section 13(d) of the Securities Exchange Act of 1934.

On November 15, 2005, the Company entered into an agreement with Liolios Group, Inc. ( Liolios ) for the provision of public relations services to the Company. As part of the compensation due Liolios, the Company agreed to issue to Liolios, every month the agreement is effective, a warrant to purchase up to 50,000 shares of the Company s common stock at an exercise price of \$0.10 per share. The Company granted standard piggy-back registration rights with respect to any such warrants issued. The agreement provides for a term of six months and