

INTERNATIONAL MICROCOMPUTER SOFTWARE INC /CA/
Form 10KSB/A
September 14, 2004

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-KSB/A

- ANNUAL REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended **June 30, 2004**
- TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE EXCHANGE ACT OF 1934
For the Transition Period from _____ to _____

Commission File No. **0-15949**

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC.
(Name of Small business issuer in its charter)

CALIFORNIA
(State or other jurisdiction of incorporation or
organization)

94-2862863
(I.R.S. Employer Identification No.)

**100 ROWLAND WAY, NOVATO,
CALIFORNIA**
(Address of principal executive offices)

94945
(Zip code)

(415) 878-4000
Issuer's telephone number

Securities registered pursuant to Section 12(b) of the Act: **None**

Securities registered pursuant to Section 12(g) of the Act: **Common stock, no par value**

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

Issuer's revenues for its most recent fiscal year. **\$11,985,000.**

The aggregate market value of the voting and non-voting common stock held by non-affiliates computed by reference to the average bid and asked price of the common stock as of **September 7, 2004** was approximately **\$26,124,231**.

As of **September 7, 2004**, **27,434,956** Shares of Issuer's common stock, no par value, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

None

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC.

**FORM 10-KSB ANNUAL REPORT
FOR THE YEAR ENDED JUNE 30, 2004**

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PORTION AMENDED

This filing on Form 10-KSB/A is to amend our Form 10-KSB for the fiscal year ended June 30, 2004, as filed with the Securities and Exchange Commission on September 13, 2004. The only amendment we are making is to correct erroneous column headings in the identification of income and expenses for the years ended June 30, 2004 and 2003. As originally filed, the Form 10-KSB had the identification of the years reversed. There are no changes in any of the reported numbers or other matters other than this clerical error.

This Annual Report on Form 10-KSB/A does not reflect events occurring after the filing of the registrant's Annual Report on Form 10-KSB for the fiscal year ended June 30, 2004, or modify or update those disclosures, except as discussed above.

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PART I

Forward-Looking Information

This Annual Report of International Microcomputer Software, Inc ("IMSI" or the "Company") on Form 10-KSB contains forward-looking statements, particularly those identified with the words, "anticipates," "believes," "expects," "plans," and similar expressions. These statements reflect management's best judgment based on factors known at the time of such statements. The reader may find discussions containing such forward-looking statements in the material set forth under "Legal Proceedings" and "Management's Discussion and Analysis and Plan of Operations," generally, and specifically therein under the captions "Liquidity and Capital Resources" as well as elsewhere in this Annual Report on Form 10-KSB. Actual events or results may differ materially from those discussed herein.

Item 1- Description of Business

Business Development

Headquartered in Novato, California, IMSI was incorporated in California in November 1982. Over the next 16 years, we grew to become a leading developer and publisher of productivity software in the precision design, graphic design, and other related business applications fields. We acquired TurboCAD, our flagship product, in 1985, and developed and acquired numerous products and product categories over the years. By the end of 1998, we developed, marketed and distributed our products worldwide, primarily through the retail channel.

In 1998, we acquired ArtToday.com ("ArtToday") an Internet provider of clipart, photos and other graphics content as part of our strategy to transition from the retail channel to Internet based product distribution and to migrate our core products and content in the design and graphics categories to the Internet. This transition proved costly and we suffered large losses that threatened our survival. Beginning in 2000, we underwent a major financial restructuring that focused on the design and graphics software categories and on expanding ArtToday.com.

In August 2001, we entered into a merger agreement with Digital Creative Development Corp ("DCDC"). Upon signing of the merger agreement, Mr. Martin Wade III, a director and the CEO of DCDC, became CEO of IMSI, four of our five directors resigned and the entire board of directors of DCDC was appointed to the IMSI board of directors.

In November 2001, we acquired Keynomics, Inc ("Keynomics") from DCDC, which focused on productivity enhancement software. Keynomics develops and markets productivity and ergonomic compliance tools improvements through its proprietary software system, "The KeySoft Performance System". Keynomics' mission is to reduce corporate keyboarding costs and their related risks and provide significant long-term savings through ergonomic and productivity training and awareness.

In February 2002, we entered into a "Mutual Termination Agreement and Release" with DCDC whereby the proposed merger was terminated and each company was released from all duties, rights, claims, obligations and liabilities arising from, in connection with, or relating to, the proposed merger.

In June 2003, we sold ArtToday, our wholly owned subsidiary based in Arizona, to Jupitermedia Corporation ("JupiterMedia") for a combination of cash, restricted stock and two-year earn-outs.

The sale of ArtToday to Jupitermedia provided the Company with significant capital allowing us to accelerate the implementation of our strategy of strengthening and expanding our core businesses of precision design and consumer software. Our focus is to acquire and develop businesses and product lines which have significant revenue and cost synergies with our existing product lines as well as which utilize the internet as a primary means of distribution. To that end we have completed several acquisitions and one divestiture aimed at growing our revenues and strengthening

our financial results. The following is a description of the key transactions, in chronological order of closing, which were integral to this strategy that we completed subsequent to our divestiture of ArtToday:

DevDepot On May 11, 2004 we entered into an asset purchase agreement with DevDepot, LLC, whereby we acquired certain assets of DevDepot. The assets included inventories, customers' profiles, rights to all contracts and license agreements in addition to certain interests in intellectual properties related to the business. DevDepot is a highly focused on-line marketer of utilities and hardware and software add-ons primarily for the Macintosh market. It operates www.devdepot.com and www.radgad.com as well as being active in the sale of products at well known industry trade shows.

Allume On April 19, 2004 we completed the acquisition of all the outstanding stock of Aladdin Systems, Inc. ("Aladdin"), a developer and publisher of utility software solutions in the areas of information access, removal, recovery, security and distribution of information and data for the Windows, Linux and Macintosh platforms. We purchased Aladdin for a combination of cash, stock and notes from its parent company, Aladdin Systems Holdings, Inc. and subsequently changed the company's name to Allume Systems, Inc ("Allume"). With over 50% of its sales being generated via the internet, Allume has broadened our reach into this key distribution channel. With its strengths in product development and direct marketing as demonstrated by the award winning StuffIt product line, Allume has significantly improved the depth and breadth of our product offerings. Reflecting its development and marketing strengths, Allume is the number #1 developer of utilities for Macintosh as well as the #1 reseller of 3rd party products in the Digital River's network. With its long standing direct marketing model and extensive Macintosh user base, Allume is well suited to create revenue synergies with DevDepot. More information regarding products and services are available at www.allume.com and www.StuffIt.com.

Houseplans.com On February 23, 2004 we entered, through our wholly owned subsidiary, Houseplans, Inc. ("Houseplans"), into an asset purchase and license agreement with ULTRYX, Inc ("ULTRYX") whereby we acquired certain assets of ULTRYX. The assets included the Houseplans.com domain name, related web site assets including 2,000 stock house plans and related on-line and print content in addition to customers' profiles. The acquisition of this key domain name and related content will allow us to continue to expand our presence and improve our efficiency in the fast growing market for the sale of stock house plans via the internet. More information regarding products and services are available at www.houseplans.com and www.houseplanguys.com.

Houseplans On November 17, 2003, we acquired Planworks L.L.C. ("Planworks"), a leading on-line distributor of stock house plans. Planworks operates the Houseplanguys.com website that contains an extensive library of over 11,000 unique house plans and has more than 25,000 registered members. We also acquired ten other domain names which are used to assist individuals and designers looking for house plans and related products, further strengthening the IMSI network of on-line design and content commerce sites. We subsequently changed the company's name from Planworks to Houseplans, Inc. This business represents a new connection point for our historically strong design and content customers. More information regarding products and services are available at www.houseplans.com and www.houseplanguys.com.

CADsymbol On November 6, 2003, we entered into an asset purchase agreement with Assisto GmbH ("Assisto"), a German company, whereby we acquired title and interest in certain tangible and intangible assets of Assisto. The assets included over 30 million CAD symbols, custom developed software and all related assets including inventory, web sites and domain names. With these symbols and the related website assets, we will be able to continue to develop and deliver, via the internet, CAD content to our Architecture, Engineering and Construction customers who rely on this content to create, modify and design drawings using a variety of CAD software packages. More information regarding products and services are available at www.CADsymbol.com.

CADsymbols On October 27, 2003, we entered into an asset license and purchase agreement with Cardiff Consultants, Limited, a New York corporation ("Cardiff"), whereby we acquired from Cardiff the exclusive, non-transferable right to use the CADsymbols.com and CADsymbols.net domain names and trademarks until December 31, 2006, when

Cardiff is to assign the domain names and trademark to us subject to our payment of all amounts due Cardiff. As part of the transaction, we also entered into a license for Cardiff's CAD symbols which with the key domain name formed the basis of this business. The Cadsymbols domains, in combination with the on-line part libraries acquired from CADalog Inc and Assisto, allowed us to establish one of the CAD industry's largest subscription-based CAD content sites. More information regarding products and services are available at www.CADsymbols.com.

CADalog On September 12, 2003, we acquired from CADalog, Inc, CADalog.com, a network of websites that offers one of the largest mechanical parts symbols libraries on-line and allows members access to over eight million 2D and 3D hardware component symbols. The acquisition also included the purchase of CADalog, Inc.'s Partstxl.com, Partstwork.com and 3DModelsharing.com websites. The acquisition is a natural extension of our CAD expertise as CADalog.com and its related sites allowed us to join various parts of our businesses for a complete offering of CAD related software resources. More information regarding products and services are available at www.CADalog.com.

DesignCAD On July 28, 2003, we entered into an agreement to purchase the tangible and intangible assets of Upperspace Corporation ("Upperspace"), an Oklahoma corporation, constituting its DesignCAD line of products, several learning aids, and various smaller design programs. These products enabled us to significantly strengthen the depth and variety of our offerings to consumers and small business users in the under \$100 CAD market. More information regarding products and services are available at www.imsisoft.com.

Keynomics To further refine the focus of the company, in July 2004, we sold the assets and customer related liabilities of our wholly owned subsidiary Keynomics, Inc. The acquiring entity (Keynomics, L.L.C.) will continue to provide ergonomic and keyboard training using the KeySoft Performance System(TM) for worker-related safety, productivity, and ergonomic compliance improvements. As part of the consideration, which consisted mainly of cash with the potential for additional cash consideration based on the achievement of certain revenue targets, we acquired a ten (10%) ownership interest in Keynomics, L.L.C. As a result of this sale, we have categorized the operations of this subsidiary as discontinued and we expect, in the September 2004 quarter, to record a gain on the sale of the Keynomics, Inc. assets of approximately \$84,000.

Overview of Our Business

Principal Products and Services

We publish over 100 software titles worldwide and offer an array of services to our customers. The following is a brief description of our principal product families and selected product brands:

Business Segment	Product Family	Product Group	Product Brand
Precision Design Solutions	Precision Design Software	Professional CAD Solutions	<i>TurboCAD Professional</i> <i>TurboCADCAM</i> <i>CADalog</i> <i>CADsymbol CD</i> <i>TurboCAD Deluxe</i>
		Consumer CAD Solutions	<i>DesignCAD</i> <i>Instant Series</i> <i>FloorPlan</i> <i>Houseplans.com</i> <i>Houseplanguys.com</i> <i>CADsymbols.com</i>
	Precision Design Services	Content	
		Compression, Access and Transmission (CAT)	<i>StuffIt Delux & Standard</i> <i>iClean</i>
		Utilities	Security and Internet

		<i>Internet Cleanup</i>
		<i>SpamCatcher</i>
		<i>Spring Cleaning</i>
		<i>NetAccelerator</i>
		<i>DragStrip</i>
		<i>Ten for X</i>
	Software Compilations	<i>Creative Essentials</i>
		<i>The Big Mix</i>
		<i>FlowCharts & More</i>
		<i>FormTool</i>
	Business Solutions	<i>OrgChart Professional</i>
		<i>QuickStart</i>
		<i>TurboProject</i>
		<i>Animations & More</i>
Business Applications and Other	Graphics Solutions	<i>ClipArt & More</i>
		<i>HiJaak</i>
		<i>The Lord of the Rings</i>
		<i>Activity Studio</i>
	Consumer Solutions	<i>EazyLanguage</i>
		<i>Legacy Family Tree</i>
		<i>TurboTyping</i>

Precision Design Solutions

Precision Design Software

Professional CAD Solutions

- ***TurboCAD*** is a top-selling Computer Aided Design ("CAD") software product that allows a user to create and modify precision drawings. It offers comprehensive functionality for the technical professional combined with ease-of-use for the novice user. TurboCAD is used by architects, engineers, and contractors in small and medium-sized businesses, as well as by workgroups within many large corporations such as Pennzoil, Dow Chemical, Bechtel, Babcock & Wilcox, Houston Power & Lighting, and Motorola.
- ***TurboCADCAM*** integrates our popular, award winning computer-aided design program with powerful computer-aided machining capabilities. This seamless integration of CAD, CAM and CNC is designed to immediately increase machine shop and manufacturer profits and productivity.
- ***CADalog*** is a network of websites that offers one of the largest mechanical parts symbols libraries on-line and allows members access to over eight million 2D and 3D hardware component symbols.
- ***CADsymbol CD*** is the most extensive collection of standard parts and symbols available containing over 30 million symbol drawings and models in 2D view and freely revolving 3D models.

Consumer CAD Solutions

- ***TurboCAD Deluxe*** is an easy to use solution to design and present 2D and 3D ideas. It features over 250 2D/3D precision tools.
- ***DesignCAD*** is a group of CAD software products (including DesignCAD 3d Max and DesignCAD Express), that are targeted toward smaller contractors, DIY's (do it yourselfers) and residential homeowners.
- ***Instant Series*** is an array of CAD titles, including Instant Architect and Instant Deck Design with common easy to use features geared toward consumers.
 - ***FloorPlan*** is a software tool for residential and commercial space layout that allows a user to create, view, and walk through plans in three dimensions with photo-realistic rendering. FloorPlan 3D has received numerous industry awards such as PC Magazine's Editors Choice Award, and has sold over one million units.

Precision Design Services (Content)

- ***Houseplans.com and Houseplanguys.com*** are part of a network of websites that contain an extensive library of over 15,000 unique house plans, which are targeted to general contractors, individuals and designers. The network has more than 50,000 registered members.

CADsymbols.com is a library of content offered on-line and aimed to help graphic designers and engineers in their graphic application.

Consumer & Business Software Solutions

Utilities

This product family is substantially comprised by products obtained through our acquisition of Allume. These products are organized in three groups:

v	Compression, Access and Transmission (CAT)
v	Security and Internet
v	Software Compilations

Compression, Access and Transmission

This group is mainly comprised of the StuffIt brand. StuffIt is a leading software product that addresses the following:

- Ø Sending information in a way that is fast, safe and secure over the Internet or any network
 - Ø Accessing information received
 - Ø Archiving information
 - Ø Backing up information
 - Ø Maximizing storage capacity and bandwidth
 - Ø Automating the process of sending and receiving information

StuffIt has been adopted as a worldwide compression standard for the Macintosh platform and is distributed by Apple Computer and America Online. StuffIt products have been shipped to over 20 million users worldwide over the last three years, including approximately 13 million copies distributed by Apple Computer shipped pre-loaded on Apple Computer's products.

The StuffIt brand includes:

- ***StuffIt Deluxe*** (Windows and Macintosh)
- ***StuffIt Standard Edition*** (Windows, Macintosh and Linux)
- ***StuffIt Expander*** (Windows and Macintosh)
- ***StuffIt Express*** (Windows and Macintosh)
- ***StuffIt Installmaker*** (Macintosh)
- ***StuffIt Engine SDK*** (Windows, Linux, Solaris and Macintosh)

Security and Internet

·***iClean*** (Windows and Macintosh) - iClean allows a user to remove specific unwanted or unneeded files gathered by the Web browser. Removing these files recovers disk space and helps ensure on-line privacy. iClean is targeted at the OEM marketplace.

·***Internet Cleanup*** (Windows and Macintosh) - Internet Cleanup is a spyware, Internet cleanup and privacy solution used to remove unwanted internet files and protect users identity. Internet Cleanup also blocks pop-up and banner ads, and detects and removes Spyware.

·***SpamCatcher*** (Windows) - SpamCatcher is an anti-spam software solution published by Allume Systems. SpamCatcher is designed to catch unwanted and undesirable, unsolicited email that a person receives. It integrates with Microsoft's Outlook email client and also works with most of the popular email solution programs on the market today.

·***Spring Cleaning*** (Windows and Macintosh) - Spring Cleaning is a software "uninstaller" product that removes unwanted and unused software and their related files from a user's computer.

·***NetAccelerator*** (Windows) is enhancement tool that boosts computer performance and makes the browsing and downloading experience faster.

·***DragStrip*** (Windows and Macintosh) - DragStrip allows users to launch, find, organize and access applications and documents quickly and efficiently.

Software Compilations

The Ten for X brand was developed to take advantage of the lack in functionality in many areas of the new Macintosh OS X operating system and the many good software products that are being created by developers who do not have access, ability, desire, or the organization to expand their software offering beyond the shareware model. Ten for X allows these developers to reach a wider audience. The software is sold at Apple Computer stores and other retailers, as well as Allume Systems web sites.

- **Ten for X: Utilities Volume 1** is a collection of 11 Macintosh OS X utility software products.
- **Ten for X: Utilities Volume 2** is the second collection of utilities and includes a spam solution along with ten other popular software utilities for Macintosh OS X.
- **Ten for X: Games Volume 1** is a collection of 13 games for Macintosh OS X, including the very popular Bugdom 2.
- **GameOn Action** is a collection of six action pack games for the Macintosh. This compilation includes games like Spyhunter (TM) and Freedom Force.
- **GameOn Family** is a collection of games for the whole family, designed to provide hours of endless fun. This compilation includes Zoo Tycoon and Tony Hawk's Pro Skater 3 plus three other games.
- **Creative Essentials** is a collection of professional graphic tools for the Mac sold at an affordable price.
- **The Big Mix** is a collection of music and audio tools that allows Macintosh users to learn, create, listen and share their music.

Business Applications and Other

Our business applications and other family of products includes art images, photographs, video clips, animations and fonts stored in electronic form that enhance communication by making on-line, onscreen and printed output more visually appealing and other business graphics and general office products. Our business applications products include the following three product groups:

Business Solutions

- **FlowCharts & More** enables general business users to create a wide variety of diagrams, including flow charts, organization charts, timelines, block diagrams, geographic maps, and marketing charts.
- **FormTool** is a forms automation product that allows users to design and print personal forms quickly, or choose from over 400 pre-built templates.
- **OrgChart Professional** is an application designed for creating professional organization charts. OrgChart Professional completely automates chart creation so that no drawing or manual positioning of boxes is required.
- **QuickStart** is an application that generates professionally designed layouts, images, business cards, letterheads, greeting cards, postcards and labels for envelopes, CDs, DVD cases, file folders, bar codes, diskettes, shipping, video tapes and jewel cases.

· ***TurboProject*** is a project management tool that allows users to create and manage a project schedule, allocate resources and establish and track project budgets.

Graphics Solutions

· ***Animations & More, ClipArt & More*** are large collections of top-quality, royalty-free images, animations, videos, fonts, sounds and images in a variety of categories. The included media are useful to a wide range of customers such as individuals making printed announcements in their home, and professional graphic artists designing brochures for clients.

· ***HiJaak*** is a professional graphics toolkit that allows users to convert, manage and view over 115 graphics file formats including 3D and full Postscript files.

Consumer Solutions

- *The Lord of the Rings Activity Studio* allows the user to experience the movie magic of J.R.R. Tolkien's best selling Fellowship of the Ring books. The software includes movie stills, and lets the user print themed calendars, posters, party kits, and more.
- *EazyLanguage* is a tool for learning over 16 languages, including Spanish, French, German, Russian, English, Italian, Japanese, Korean, and more. Perfect for beginners, business travelers, and others wishing to learn a new language or sharpen existing skills.
- *Legacy Family Tree* is a powerful and easy-to-use family history software designed to easily produce and share family trees.
- *TurboTyping*, geared toward home users, business users and students, is a fast way to improve typing skills. This application improves the user's typing skills by a factor of three to five times.

Distribution Methods

Depending on the product and the customer, we deliver our products either as Electronic Software Download (ESD) or as physical products. Our distribution methods are comprised of the following three major channels:

Direct Marketing:

- o *Direct to Consumer-* We conduct direct mail campaigns, both postal and email, for our existing and new products in addition to upgrades of existing products, as well as third-party offers. These mailings generally offer a specially priced product, as well as complementary or enhanced products for a further charge. We maintain e-commerce websites and employ a sales force internally and through strategic partnerships:
- § *On-line-* A key emphasis of our sales strategy is to significantly increase the marketing of our products via the Internet. We sell from our own websites, as well as through strategic partnerships with on-line resellers and service bureaus.
- § *Telesales-* We sell certain of our products and services through our sales force as well as through external call centers.
- o *Direct to Businesses-* We believe that certain of our products and services, particularly TurboCAD, StuffIt, TurboProject, OrgChart Professional and HiJaak, are well suited for use within large corporations. Over the past year, we have sold site licenses to large companies, including Fortune 100 companies. We market to these corporations through a combination of telemarketing, direct mail, and e-mailing.
- **Retail / Distribution-** We are increasing our presence in the retail software market utilizing selected distributors and partners for a number of our products in order to reach a wider range of end users. However, intense price competition along with the intermittent unfavorable retail conditions, including erosion of margins from competitive marketing and high rates of product returns, make this distribution channel increasingly challenging.
- **Republishing-** We have republishing agreements domestically and internationally which typically include minimum guaranteed royalty payments.

Competitive Business Conditions

The software industry and the Internet are highly competitive and characterized by several key factors:

- **Rapid changes in technology and customer requirements** - New opportunities for existing and new competitors can quickly render existing technologies less valuable.
- **Relatively low barriers to entry** - Startup capital requirements for software companies can be very small, and software distribution over the Internet is inexpensive and easily outsourced.
- **Significant price competition** - Direct distribution of competing products over the Internet may cause prices and margins to decrease in traditional sales channels.
- **Consolidations and mergers** - Software companies and their individual products have a high rate of mergers, product line sales, and other transfers and consolidation.

These factors could have a material adverse effect on our future operating results, including reduced profit margins and potential loss of market share.

Each of our major software products competes with one or more products from other major independent software vendors. Our main products and their primary competition are listed in the following table:

<u>IMSI Product</u>	<u>Competing products</u>	<u>Competitor</u>
TurboCAD	AutoCAD	Autodesk Inc.
FloorPlan	3D Architect Home Architect Home Design Suite	Broderbund Sierra Online Punch Software
ClipArt & More, Animations & More	ArtExplosion Photo ClipArt Big Box of Art Designer ClipArt	Nova Development Hemera Hemera GlobalStar Software
OrgChart Professional	Visio OrgPlus	Microsoft Human Concepts
StuffIt	WinZip	WinZip Computing, Inc
SpamCatcher	MailShield	Lyris
Internet Cleanup	SpyBot Search and Destroy	SpyBot

Dependence on Major Customers

No single customer accounted for greater than 10% of our revenues in fiscal year 2004 or 2003.

Proprietary Rights and Licenses

We acquired the technology for TurboCAD in 1985, FloorPlan Design Suite in 1990, HiJaak in 1995, DesignCAD in 2003 and StuffIt in 2004.

We use the following trademarks and service marks in our business: Allume, CADalogSM, CADsymbolsSM, FloorPlan®, FormTool®, Gobar®, HiJaak®, HouseplansTM, HomePlan SM, iClean®, IMSI®, Installermaker® , Internet CleanupTM, MasterClips®, OrgChart®, SpamCatcherTM, Spring Cleaning®, StuffIt®, StuffIt Deluxe®, Ten for XTM , Turboviewer®, TurboCAD®, TurboProject®, ZipFolders®, Zipmagic®.

Our ability to compete effectively depends in part on our ability to develop and maintain the proprietary aspects of our technology. We take certain steps to protect our technology including:

- We rely on a combination of copyrights, patents, trademarks, trade secret laws, restrictions on disclosure, and transferring title and other methods.
- We enter into confidentiality or license agreements with our employees and consultants, and control access to and distribution of our documentation and other proprietary information.
- We provide our products to end users under non-exclusive licenses, which generally are non-transferable and have a perpetual term.

Software companies face a number of risks relating to proprietary rights and licenses. In particular, we have identified several factors that present the greatest technology risk to us:

- We make source code available for some products. The provision of source code may increase the likelihood of misappropriation or other misuse of our intellectual property.
- We license all of our products pursuant to shrink-wrap licenses or Internet click-wrap licenses that are not signed by licensees and therefore may be unenforceable or difficult to enforce under the laws of certain jurisdictions.
 - It may be possible for a third-party to copy or otherwise obtain and use our products or technologies without authorization, or to develop similar technologies independently.

There can be no assurance that the steps taken by us will prevent misappropriation or infringement of our technology. In addition, litigation may be necessary to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. Litigation presents several additional risk factors to us:

- Litigation could result in substantial costs and diversion of resources that could have a material adverse effect on our business, operating results and financial condition.
- As the number of software products in the industry increases and the functionality of these products further overlaps, software developers and publishers may increasingly become subject to infringement claims.
- If any valid claims or actions were asserted against us, we might seek to obtain a license under a third party's intellectual property rights. There can be no assurance, however, that under such circumstances a license would be available on commercially reasonable terms, or at all.

From time to time we have received, and may receive in the future, notice of claims of infringement of other parties' proprietary rights. Although we investigate claims and respond as we deem appropriate and believe we do not infringe upon the intellectual property rights of others, there can be no assurance that infringement claims (or claims for indemnification resulting from infringement claims) will not be asserted or prosecuted against us.

Governmental Regulation

Our products are not subject to approval from the United States government with the exception of export restrictions to certain countries. Our business operations do not fall under Federal, State, or local environmental regulations. We do not anticipate current or future government regulation will have a material adverse effect on our capital expenditures, earnings, or competitive position.

Product Development

The majority of our development costs are focused in the TurboCAD, StuffIt and FloorPlan product lines, all of which are internally developed. Other products which we bring to market are primarily comprised of technology that is licensed from third parties.

We generally create product specifications and manage the product development and quality assurance process from our offices in Novato and Watsonville, California. Program coding and quality testing for internally developed products is either performed in-house or by using contract programmers in development centers in Russia and India depending on the product and its complexity. Contract programmers located outside the United States are usually

dedicated on a full-time basis to our products.

Our research and development expenses consist primarily of salaries and benefits for research and development employees and payments to independent contractors. We spent approximately \$2.5 million and \$1.4 million on research and development in the twelve-month periods ended June 30, 2004 and 2003, respectively. We will continue to invest in existing and new products which reflects our commitment to developing our core products as well as maintaining strong relationships with our internal and contract development teams.

Employees

As of June 30, 2004 we had 105 employees, all of whom are located in the United States with the exception of one employee in Australia and one employee in Germany. In addition, we have development contracts with two companies in Russia and one in India. None of our employees are represented by a labor union and we have experienced no work stoppages. Our success depends to a significant extent upon the performance of our executive officers, key technical personnel, and other employees.

Item 2- Description of Property

Our principal offices are located in Novato, CA occupying approximately 10,000 square feet of office space. The lease term expires in March 2007. We also occupy approximately 17,000 square feet of leased office space in Watsonville, CA, where our wholly owned subsidiary Allume Systems conducts its business, and 7,500 square feet of warehouse space in Vacaville, CA.

We believe the space is adequate for our immediate needs. Additional space may be required as we expand our activities. We do not foresee any significant difficulties in obtaining any required additional facilities.

Item 3- Legal Proceedings

From time to time, we may be involved in litigation relating to claims arising out of our operations in the normal course of business. We know of no material, existing or pending legal proceedings against us, nor are we involved as a plaintiff in any material proceeding or pending litigation. There are no proceedings in which any of our directors, officers or affiliates, or any registered or beneficial shareholder, is an adverse party or has a material interest adverse to our interest.

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

On February 23, 2004, we filed with the Securities and Exchange Commission a Definitive Proxy Statement on Schedule 14-A pursuant to section 14(A) of the Securities Exchange Act Of 1934 in connection with the solicitation of proxies by the board of directors of IMSI for use at the annual meeting of the shareholders.

The annual meeting of the shareholders of IMSI was held on March 17, 2004 and the following proposals were approved by the shareholders:

The election of seven directors for a term of one year:

NAME	AGE	OCCUPATION	DIRECTOR SINCE	Votes cast for	Votes Withheld
Bruce Galloway	45	Chairman of the Board of Directors	2001	18,430,101	28,729
Martin Wade, III	54	Chief Executive Officer	2001	18,435,351	23,479
Evan Binn	64	Director	2001	17,677,611	781,219
Donald Perlyn	60	Director	2001	17,677,161	781,669
Robert Mayer	49	Executive Vice President	2000	17,673,911	784,919
Robert S. Falcone	57	Director, Chairman of the Audit Committee	2002	18,443,051	15,779
	61	Director	2002	18,442,901	15,929

Richard J.
Berman

·The approval of the 2004 Incentive Stock Option Plan. This proposal was approved according to the votes as cast below:

o	For: 17,980,913
o	Against: 197,951
o	Abstain: 279,966

The authorization of the issuance of options aggregating up to 49.0% of the outstanding capitalization. This proposal was approved according to the votes as cast below:

<input type="radio"/>	For: 17,877,261
<input type="radio"/>	Against: 321,777
<input type="radio"/>	Abstain: 259,792

The ratification of the appointment of Grant Thornton LLP as IMSI's independent auditors for the fiscal year ending June 30, 2004. This proposal was approved according to the votes as cast below:

<input type="radio"/>	For: 18,329,509
<input type="radio"/>	Against: 5,266
<input type="radio"/>	Abstain: 124,055

PART II

Item 5- Market for Common Equity and Related Stockholder Matters

The following table sets forth the quarterly high and low sales prices of the common stock for fiscal 2004 and 2003, as quoted on the OTCBB. This information represents prices between dealers and does not include retail mark-ups, markdowns or commissions and may not represent actual transactions.

	High	Low
Fiscal Year 2003		
First Quarter	\$ 1.01	\$ 0.64
Second Quarter	0.79	0.51
Third Quarter	0.67	0.43
Fourth Quarter	\$ 0.85	\$ 0.40
Fiscal Year 2004		
First Quarter	\$ 1.45	\$ 0.73
Second Quarter	1.50	1.00
Third Quarter	1.77	1.10
Fourth Quarter	\$ 1.72	\$ 1.11

On September 7, 2004, there were approximately 1,068 registered holders of record of the common stock. We believe that additional beneficial owners of our common stock hold shares in street names.

We have not paid any cash dividends on our common stock and do not plan to pay any such dividends in the foreseeable future. Our Board of Directors will determine our future dividend policy on the basis of many factors, including results of operations, capital requirements and general business conditions.

Item 6- Management's Discussion and Analysis or Plan of Operation

Overview

IMSI has established a tradition of providing the professional and home user with innovative technology and easy-to-use, high-quality software products at affordable prices. We are a developer and publisher of precision design and consumer and business software solutions which we market and sell to individuals and small business users. We offer a variety of software products and services, primarily precision design and utilities offerings that we market

through an array of distribution channels including direct to consumer and businesses, retail and through republishers.

Strategy and Growth

We believe that consistent growth of both the revenues and operating earnings can be achieved through internally developed products and services and through acquisition. Management believes that good value target companies are present in the marketplace and that business combinations with these entities would help us achieve our growth potential in addition to providing synergies that would improve profitability.

Acquisitions during Fiscal 2004

DevDepot On May 11, 2004 we entered into an asset purchase agreement with DevDepot, LLC, whereby we acquired certain assets of DevDepot. The assets included inventories, customers' profiles, rights to all contracts and license agreements in addition to certain interests in intellectual properties related to the business. DevDepot is a highly focused on-line marketer of utilities and hardware and software add-ons primarily for the Macintosh market. It operates www.devdepot.com and www.radgad.com as well as being active in the sale of products at well known industry trade shows. With its long standing direct marketing model and extensive Macintosh user base, DevDepot is well suited to create revenue synergies with Allume. The consideration for the acquisition was paid in a combination of cash and 112,000 unregistered common shares, a portion of which are subject to an escrow period.

Allume On April 19, 2004 we completed the acquisition of all the outstanding stock of Aladdin, a developer and publisher of utility software solutions in the areas of information access, removal, recovery, security and distribution of information and data for the Windows, Linux and Macintosh platforms. We purchased Aladdin for a combination of cash, stock and notes from its parent company, Aladdin Systems Holdings, Inc. and subsequently changed the company's name to Allume Systems, Inc. With over 50% of its sales being generated via the internet, Allume has broadened our reach into this key distribution channel. With its strengths in product development and direct marketing as demonstrated by the award winning StuffIt product line, Allume has significantly improved the depth and breadth of our product offerings. Reflecting its development and marketing strengths, Allume is the number #1 developer of utilities for Macintosh as well as the #1 reseller of 3rd party products in the Digital River's network.

The consideration paid to Aladdin Systems Holdings, Inc. ("Aladdin Holdings") for the acquisition consisted of a combination of cash in the amount of \$1,500,000, subject to a 10% escrow, 2,317,881 unregistered shares of IMSI common stock and two three-year convertible notes in the aggregate amount of \$3,000,000. These notes are secured by the Allume common stock. Under the terms of the original purchase agreement, additional cash earn-out payments could have been earned, up to an aggregate of \$2,000,000, based on net revenues derived from Aladdin for the three consecutive twelve-month periods following the Closing Date.

In early September 2004, IMSI and Aladdin Holdings amended the portion of the agreement which called for earn-outs to be paid based on the achievement of certain revenue targets. The payments were converted from contingent obligations to contractual obligations as follows;

- The first earn out payment of \$666,667 which could have been due on April 19, 2005 became fully earned and payable on June 2, 2005
- The second and third earn-out payments were terminated in consideration of the issuance of shares of the common stock of IMSI priced as of the closing bid price on the date of the amendment. As a result, IMSI will issue an additional 1,065,807 of its common stock to Aladdin Holdings. These shares will be included in the registration statement to be filed on Form SB-2 pursuant to the Registration Rights Agreement between Aladdin Holdings and IMSI, as contemplated below.