

SMART ONLINE INC  
Form 8-K  
April 16, 2010

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

FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): April 13, 2010

Smart Online, Inc.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other Jurisdiction of Incorporation)

001-32634  
(Commission File Number)

95-4439334  
(IRS Employer Identification No.)

4505 Emperor Blvd., Suite 320  
Durham, North Carolina  
(Address of Principal Executive Offices)

27703  
(Zip Code)

Registrant's telephone number, including area code: 919-765-5000

Not Applicable  
(Former name or former address if changed since last report.)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
  - Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
  - Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
  - Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))
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Item 4.02 Non-Reliance on Previously Issued Financial Statements or a Related Audit Report or Completed Interim Review.

On April 13, 2010, the Audit Committee of Smart Online, Inc. (the “Company”), in consultation with Cherry, Bekaert & Holland, the Company’s independent registered public accountants, concluded that the Company’s financial statements for the fiscal year ended December 31, 2008 and for the fiscal quarters ended March 31, 2009, June 30, 2009 and September 30, 2009 should no longer be relied upon because of an error in such financial statements.

The Board of Directors unanimously approved, authorized and directed the restatements of the foregoing financial statements and the filing of this Report on Form 8-K by resolution adopted on April 15, 2010. The Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2009, as filed with the Securities and Exchange Commission (the “Commission”), is consistent with the Company’s restated financial statements.

The financial statements have been restated to include net subscription revenue as compared to the gross subscription revenue as presented in prior filings for 2009 and 2008. Subscription fees primarily consist of sales of subscriptions through private-label marketing partners to end users. We typically have a revenue-share arrangement with these marketing partners in order to encourage them to market our products and services to their customers. Subscriptions are generally payable on a monthly basis and are typically paid via credit card of the individual end user. We accrue any payments received in advance of the subscription period as deferred revenue and amortize them over the subscription period. In the past we recognized all subscription revenue on a gross basis and in accordance with our policy to periodically review our accounting policies we identified the fact that certain contracts require the reporting of subscription revenue on a gross basis and others on a net basis according to US GAAP. On that basis, we continue to report subscription revenue from certain contracts on a gross basis and others on a net basis. The net effect of this reclassification of expenses only impacts gross revenue and certain gross expenses; it does not change the net income. The effects of these reclassifications for 2009 and 2008 are presented in detail below:

|                                   | 2009           |                | 2008           |                |
|-----------------------------------|----------------|----------------|----------------|----------------|
|                                   | As Reported    | As Restated    | As Reported    | As Restated    |
| Quarter Ended March 31            |                |                |                |                |
| <b>REVENUES:</b>                  |                |                |                |                |
| Subscription fees                 | \$ 473,579     | \$ 241,783     | \$ 742,839     | \$ 479,341     |
| Professional service fees         | 118,773        | 118,773        | 504,083        | 504,083        |
| License fees                      | 11,250         | 11,250         | 100,000        | 100,000        |
| Hosting fees                      | 72,211         | 72,211         | 59,482         | 59,482         |
| Other revenue                     | 37,671         | 37,671         | 40,759         | 40,759         |
| Total revenues                    | 713,484        | 481,688        | 1,447,163      | 1,183,665      |
| <b>COST OF REVENUES</b>           | 492,601        | 492,601        | 711,667        | 711,667        |
| <b>GROSS PROFIT</b>               | 220,883        | (10,913)       | 735,496        | 471,998        |
| <b>OPERATING EXPENSES</b>         | 1,703,804      | 1,472,008      | 2,390,622      | 2,127,124      |
| <b>LOSS FROM OPERATIONS</b>       | (1,482,921)    | (1,482,921)    | (1,655,126)    | (1,655,126)    |
| <b>OTHER INCOME (EXPENSE)</b>     | (111,732)      | (111,732)      | (175,757)      | (175,757)      |
| <b>NET LOSS</b>                   | \$ (1,594,653) | \$ (1,594,653) | \$ (1,830,883) | \$ (1,830,883) |
| <b>NET LOSS PER COMMON SHARE:</b> |                |                |                |                |
| Basic and fully diluted           | \$ (0.09)      | \$ (0.09)      | \$ (0.10)      | \$ (0.10)      |



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| Quarter Ended June 30             | 2009                  |                       | 2008                  |                       |
|-----------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
|                                   | As Reported           | As Restated           | As Reported           | As Restated           |
| <b>REVENUES:</b>                  |                       |                       |                       |                       |
| Subscription fees                 | \$ 668,344            | \$ 209,819            | \$ 747,068            | \$ 464,456            |
| Professional service fees         | 79,726                | 79,726                | 932,444               | 932,444               |
| License fees                      | 11,250                | 11,250                | 3,750                 | 3,750                 |
| Hosting fees                      | 33,045                | 33,045                | 36,196                | 36,196                |
| Other revenue                     | 36,806                | 36,806                | 36,173                | 36,173                |
| <b>Total revenues</b>             | <b>829,171</b>        | <b>370,646</b>        | <b>1,755,631</b>      | <b>1,473,019</b>      |
| <b>COST OF REVENUES</b>           | <b>202,333</b>        | <b>202,333</b>        | <b>647,528</b>        | <b>647,528</b>        |
| <b>GROSS PROFIT</b>               | <b>626,838</b>        | <b>168,313</b>        | <b>1,108,103</b>      | <b>825,491</b>        |
| <b>OPERATING EXPENSES</b>         | <b>2,202,532</b>      | <b>1,744,007</b>      | <b>2,232,752</b>      | <b>1,950,140</b>      |
| <b>LOSS FROM OPERATIONS</b>       | <b>(1,575,694)</b>    | <b>(1,575,694)</b>    | <b>(1,124,649)</b>    | <b>(1,124,649)</b>    |
| <b>OTHER INCOME (EXPENSE)</b>     | <b>(158,343)</b>      | <b>(158,343)</b>      | <b>(177,410)</b>      | <b>(177,410)</b>      |
| <b>NET LOSS</b>                   | <b>\$ (1,734,037)</b> | <b>\$ (1,734,037)</b> | <b>\$ (1,302,059)</b> | <b>\$ (1,302,059)</b> |
| <b>NET LOSS PER COMMON SHARE:</b> |                       |                       |                       |                       |
| Basic and fully diluted           | \$ (0.09)             | \$ (0.09)             | \$ (0.08)             | \$ (0.08)             |

| Quarter Ended September 30        | 2009                  |                       | 2008                  |                       |
|-----------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
|                                   | As Reported           | As Restated           | As Reported           | As Restated           |
| <b>REVENUES:</b>                  |                       |                       |                       |                       |
| Subscription fees                 | \$ 908,007            | \$ 159,149            | \$ 642,880            | \$ 364,136            |
| Professional service fees         | 63,200                | 63,200                | 574,970               | 574,970               |
| License fees                      | 11,250                | 11,250                | 291,250               | 291,250               |
| Hosting fees                      | 33,751                | 33,751                | 70,856                | 70,856                |
| Other revenue                     | 26,300                | 26,300                | 31,501                | 31,501                |
| <b>Total revenues</b>             | <b>1,042,508</b>      | <b>293,650</b>        | <b>1,611,457</b>      | <b>1,332,713</b>      |
| <b>COST OF REVENUES</b>           | <b>430,967</b>        | <b>430,967</b>        | <b>409,414</b>        | <b>409,414</b>        |
| <b>GROSS PROFIT</b>               | <b>611,541</b>        | <b>(137,317)</b>      | <b>1,202,043</b>      | <b>923,299</b>        |
| <b>OPERATING EXPENSES</b>         | <b>3,309,069</b>      | <b>2,560,211</b>      | <b>2,736,424</b>      | <b>2,457,680</b>      |
| <b>LOSS FROM OPERATIONS</b>       | <b>(2,697,528)</b>    | <b>(2,697,528)</b>    | <b>(1,534,381)</b>    | <b>(1,534,381)</b>    |
| <b>OTHER INCOME (EXPENSE)</b>     | <b>(169,609)</b>      | <b>(169,609)</b>      | <b>141,962</b>        | <b>141,962</b>        |
| <b>NET LOSS</b>                   | <b>\$ (2,867,137)</b> | <b>\$ (2,867,137)</b> | <b>\$ (1,392,419)</b> | <b>\$ (1,392,419)</b> |
| <b>NET LOSS PER COMMON SHARE:</b> |                       |                       |                       |                       |
| Basic and fully diluted           | \$ (0.16)             | \$ (0.16)             | \$ (0.08)             | \$ (0.08)             |

The foregoing gross revenue and expense adjustments have no impact on the Company's net income (loss).

In addition to the restatement of subscription revenue, we restated the value of the iMart trade name as of December 31, 2008 because of a recalculation of the net royalty method of valuation. The restatement caused an increase in the amount of loss on impairment of intangible assets for the year ended December 31, 2008 in the amount of \$230,000. The restated total loss on impairment of intangible assets is \$3,702,141 as compared to the original loss of \$3,472,141. The effect of this restatement for 2008 is as follows:



| For the Year Ended            | 2008                  |                        |
|-------------------------------|-----------------------|------------------------|
|                               | As Reported           | As Restated            |
| <b>REVENUES:</b>              |                       |                        |
| Subscription fees             | \$ 2,683,770          | \$ 1,587,942           |
| Professional service fees     | 2,045,508             | 1,859,154              |
| License fees                  | 26,250                | 26,250                 |
| Hosting fees                  | -                     | 259,675                |
| Other revenue                 | 117,457               | 146,158                |
| <b>Total revenues</b>         | <b>4,872,985</b>      | <b>3,879,179</b>       |
| <b>COST OF REVENUES</b>       | <b>837,789</b>        | <b>2,021,489</b>       |
| <b>GROSS PROFIT</b>           | <b>4,035,196</b>      | <b>1,857,690</b>       |
| <b>OPERATING EXPENSES</b>     | <b>13,653,175</b>     | <b>11,705,668</b>      |
| <b>LOSS FROM OPERATIONS</b>   | <b>(9,617,979)</b>    | <b>(9,847,978)</b>     |
| <b>OTHER INCOME (EXPENSE)</b> | <b>(204,171)</b>      | <b>(204,171)</b>       |
| <b>NET LOSS</b>               | <b>\$ (9,822,150)</b> | <b>\$ (10,052,149)</b> |

The effect on the balance sheet for the affected period is as follows:

| December 31            | 2008            |                 |
|------------------------|-----------------|-----------------|
|                        | As Reported     | As Restated     |
| Intangible Assets, net | \$ 380,000      | \$ 150,000      |
| Accumulated deficit    | \$ (72,678,076) | \$ (72,908,077) |

The Company's Audit Committee and executive officers have discussed the restatement of the 2008 and 2009 financial statements and the other matters discussed in this filing with the Company's independent registered public accountants, Cherry, Bekaert & Holland and the Company has provided Cherry, Bekaert & Holland with a copy of this Report on Form 8-K. Attached as an exhibit to this Report on Form 8-K is a letter from Cherry, Bekaert & Holland addressed to the Commission stating that Cherry, Bekaert & Holland agrees with the statements made by the Company in this Item 4.02.

#### Item 9.01 Financial Statements and Exhibits

##### (d) Exhibits

The following Exhibit is furnished with this Report:

|              |  |
|--------------|--|
| Exhibit 99.1 | Letter to the Company from the Company's independent registered public accountants, Cherry, Bekaert & Holland, dated April 15, 2010. |
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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

April 15, 2010

Smart Online, Inc.

By: /s/Thaddeus J. Shalek  
Name: Thaddeus J. Shalek  
Title: Interim Chief Financial Officer

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Exhibit Index

| Exhibit No. | Description  |
|-------------|--|
| 99.1        | Letter to the Company from the Company's independent registered public accountants, Cherry, Bekaert & Holland, dated April 15, 2010. |

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