SOFTECH INC
Form 10QSB
January 16, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-QSB

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarter Ended November 30, 2006	Commission File Number 0-10665

SOFTECH, INC.

State of Incorporation Massachusetts	IRS Employer Identification 04-2453033

2 Highwood Drive, Tewksbury, MA 01876
Telephone (978) 640-6222

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

The number of shares outstanding of registrant's common stock at December 29, 2006 was 12,213,236 shares.

SOFTECH, INC.

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SOFTECH, INC. AND SUBSIDIARIES

CONSOLIDATED CONDENSED BALANCE SHEETS

(dollars in thousands)

	November 30, 2006	May 31, 2006
ASSETS		
Cash and cash equivalents	$ 452	$ 680
Accounts receivable, net	1,654	1,657
Prepaid and other assets	302	317
Total current assets	2,408	2,654
Property and equipment, net	133	143

Capitalized software costs, net	2,571	3,279
Goodwill, net	4,600	4,600
Notes receivable	134	134
Other assets	2	3
TOTAL ASSETS	$ 9,848	$ 10,813

LIABILITIES AND STOCKHOLDERS' DEFICIT

Accounts payable	$ 253	$ 339
Accrued expenses	1,036	913
Deferred maintenance revenue	2,770	3,423
Current portion of long term debt	608	608
Total current liabilities	4,667	5,283
Long-term debt, net of current portion	13,600	12,947
Stockholders' deficit	(8,419)	(7,417)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	$ 9,848	$ 10,813

See accompanying notes to consolidated condensed financial statements

SOFTECH, INC. AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS

(in thousands, except for per share d

	Three Months Ended	
	November 30, 2006	November 30, 2005
Revenue		
Products	$ 759	$ 878

Services	2,247	2,513
Total revenue	3,006	3,391
Cost of products sold: materials	34	69
Cost of product sold: amortization of capitalized software costs and other intangible assets	354	553
Cost of services provided	385	381
Gross margin	2,233	2,388
Research and development expenses	520	692
Selling, general and administrative	1,569	1,512
Income from operations	144	184
Interest expense	367	286
Net loss	$ (223)	$ (102)
Basic and diluted net loss per common share	$ (0.02)	$ (0.01)
Weighted average common shares outstanding	12,213	12,205

See accompanying notes to consolidated condensed financial statements.

SOFTECH, INC. AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS

(in thousands, except for per shar

	Six Months Ended	
	November 30, 2006	November 3 2005
Revenue		
Products	$ 1,147	$ 1,717
Services	4,355	4,742
Total revenue	5,502	6,459

Cost of products sold: materials	40	126
Cost of product sold: amortization of capitalized software costs and other intangible assets	708	1,164
Cost of services provided	779	781
Gross margin	3,975	4,388
Research and development expenses	1,225	1,370
Selling, general and administrative	3,004	2,925
Income (loss) from operations	(254)	93
Interest expense	707	529
Net loss	$ (961)	$ (436)
Basic and diluted net loss per common share	$ (0.08)	$ (0.04)
Weighted average common shares outstanding	12,213	12,205

See accompanying notes to consolidated condensed financial statements.

SOFTECH, INC. AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

	(dollars in thousands) Six Months Ended	
	November 30, 2006	November 30, 2005
Cash flows from operating activities:		
Net loss	$ (961)	$ (436)
Adjustments to reconcile net loss to net cash used by operating activities:		
Depreciation and amortization	730	1,197
Change in current assets and liabilities:		
Accounts receivable	3	(15)
Prepaid expenses and other assets	16	47
Accounts payable and accrued expenses	37	(27)
Deferred maintenance revenue	(653)	(977)

Total adjustments	133	225
Net cash used by operating activities	(828)	(211)
Cash flows used by investing activities:		
Capital expenditures	(12)	(18)
Net cash used by investing activities	(12)	(18)
Cash flows from financing activities:		
Borrowings under line of credit agreements, net	653	259
Net cash provided by financing activities	653	259
Effect of exchange rates on cash	(41)	5
(Decrease) increase in cash and cash equivalents	(228)	35
Cash and cash equivalents, beginning of period	680	399
Cash and cash equivalents, end of period	$ 452	$ 434

See accompanying notes to consolidated condensed financial statements.

SOFTECH, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(A) The consolidated condensed financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission from the accounts of SofTech, Inc. and its wholly owned subsidiaries (the "Company") without audit; however, in the opinion of management, the information presented reflects all adjustments which are of a normal recurring nature and elimination of intercompany transactions which are necessary to present fairly the Company's financial position and results of operations. It is recommended that these consolidated condensed financial statements be read in conjunction with the financial statements and the notes thereto included in the Company's fiscal year 2006 Annual Report on Form 10-KSB.

(B) SIGNIFICANT ACCOUNTING POLICIES

REVENUE RECOGNITION

The Company has adopted the provisions of Statement of Position No. 97-2, "Software Revenue Recognition" (SOP 97-2) as amended by SOP No. 98-9, "Modification of SOP 97-2, Software Revenue Recognition with

Respect to Certain Transactions" (SOP 98-9) in recognizing revenue from software transactions. Revenue from software license sales is recognized when persuasive evidence of an arrangement exists, delivery of the product has been made, and a fixed fee and collectibility has been determined. The Company does not provide for a right of return. For multiple element arrangements, total fees are allocated to each of the elements using the residual method set forth in SOP 98-9. Revenue from customer maintenance support agreements is deferred and recognized ratably over the term of the agreements, typically one year. Revenue from engineering, consulting and training services, primarily performed on a time and material basis, is recognized as those services are rendered.

CAPITALIZED SOFTWARE COSTS AND RESEARCH AND DEVELOPMENT:

The Company capitalizes certain costs incurred to internally develop and/or purchase software that is licensed to customers. Capitalization of internally developed software begins upon the establishment of technological feasibility. Costs incurred prior to the establishment of technological feasibility are expensed as incurred. Purchased software is recorded at cost. The Company evaluates the realizability and the related periods of amortization on a regular basis. Such costs are amortized over estimated useful lives ranging from three to ten years. The Company did not capitalize any internally developed software during the three and six month periods ended November 30, 2006 or 2005. Substantially all of the recorded balance represents software acquired from third parties. Amortization expenses related to capitalized software costs for the three and six month periods ended November 30, 2006 were $354,000 and $708,000, respectively, as compared to $553,000 and $1,164,000 for the same periods in the prior fiscal year.

ACCOUNTING FOR GOODWILL

Effective June 1, 2002, the Company adopted the provisions of SFAS No. 142, Goodwill and Other Intangible Assets. This statement requires that goodwill existing at the date of adoption be reviewed for possible impairment and that impairment tests be periodically repeated, with impaired assets written down to fair value. Additionally, existing goodwill and intangible assets must be assessed and classified within the statement's criteria. Intangible assets with finite useful lives will continue to be amortized over those periods. Amortization of goodwill ceased as of May 31, 2002.

As of May 31, 2006, the Company conducted its annual impairment test of goodwill by comparing fair value to the carrying amount of its underlying assets and liabilities. The Company determined that the fair value exceeded the carrying amount of the assets and liabilities, therefore no impairment existed as of the testing date.

LONG-LIVED ASSETS:

The Company periodically reviews the carrying value of all intangible assets with a finite life (primarily capitalized software costs) and other long-lived assets. If indicators of impairment exist, the Company compares the undiscounted cash flows estimated to be generated by those assets over their estimated economic life to the related carrying value of those assets to determine if the assets are impaired. If the carrying value of the asset is greater than the estimated undiscounted cash flows, the carrying value of the assets would be decreased to their fair value through a charge to operations. The Company does not have any long-lived assets it considers to be impaired.

STOCK BASED COMPENSATION

Effective June 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards ("SFAS") No. 123 (Revised 2004), Share-Based Payment, ("SFAS 123R") which requires all share-base payments to employees, including grants of employee stock options, to be recorded as expense in the statement of operations based on their fair value.

To adopt SFAS 123(R), we selected the modified prospective transition method. This method requires recording compensation expense prospectively over the remaining vesting period of the stock options on a straight-line basis using the fair value of the options on the date of the grant. It does not require restatement of financial results for the prior period expense related to stock option awards that were outstanding prior to adoption. The expense recorded from adoption of this Statement in the current quarter was nominal.

We calculated the fair value of the options using the Black-Scholes model. The assumptions used to value the previous grants were as follows:

Expected Life	5 Years
Assumed annual dividend growth rate	0%
Expected volatility	1.12
Risk free interest rate	2.68% - 3.35%

Prior to adoption, the Company followed SFAS 123, Accounting for Stock Based Compensation, as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure, an amendment to SFAS Statement No. 123, which required entities to recognize as expense over the vesting period the fair value of stock-based awards on the date of grant or measurement date. For employee stock-based awards, however, SFAS Nos. 123 and 148 allowed entities to continue to apply the intrinsic value method under the provisions of Accounting Principles Board ("APB") Opinion No. 25 and provide pro forma net earnings disclosures as if the fair-value based method defined in SFAS No. 123 had been applied. The Company elected to apply the provisions of APB No. 25 and provide the pro forma disclosures of SFAS Nos. 123 and 148 for periods as required prior to June 1, 2006. Had compensation cost for the Company's stock option plans been determined based on the fair value at the grant date for awards under these plans, consistent with the methodology prescribed under SFAS 123, for the comparable periods in fiscal 2006, the Company's net loss and loss per share would have approximated the pro forma amounts indicated below:

(in thousands, except per share data)	Three Month Period Ended November 30, 2005

Net loss - as reported	$ (102)
Stock-based compensation expense determined under fair value based method	(1)
Net loss - pro forma	(103)
Loss per share - diluted - as reported	(.01)
Loss per share - diluted - pro forma	(.01)

SOFTECH, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(in thousands, except per share data)	Six Month Period Ended November 30, 2005
Net loss - as reported	$ (436)
Stock-based compensation expense determined under fair value based method	(2)
Net loss - pro forma	(438)
Loss per share - diluted - as reported	(.04)
Loss per share - diluted - pro forma	(.04)

The Company's 1994 Stock Option Plan provided for the granting of stock options at an exercise price not less than fair market value of the stock on the date of the grant and with vesting schedules as determined by the Board of Directors. No new options could be granted under the Plan after fiscal 2004 but options granted prior to that time continue to vest.

The following table summarizes information for stock options outstanding and exercisable at November 30, 2006:

	Number Of Options	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life In Years	Aggregate Intrinsic Val
Outstanding at May 31, 2006	323,000	$ .58		
Granted	-	-		

Exercised	-	-		
Forfeited or expired	(31,000)	$ .98		
Outstanding at November 30, 2006	292,000	$ .60	4.92	$ 140,5
Exercisable at November 30, 2006	258,200	$ .66	4.20	$ 139,3

The following table summarizes the information related to non-vested stock option awards outstanding as of November 30, 2006:

	Number Of Options	Weighted Average Grant Date Fair Value Per Share
Non-vested at May 31, 2006	59,800	$ .03
Granted	-	
Vested	(23,000)	$ .04
Forfeited	(3,000)	$ .21
Non-vested at November 30, 2006	33,800	$ .03

As of November 30, 2006, the remaining prospective pre-tax cost of non-vested stock option employee compensation was $704 which will be expensed on a pro rata basis going forward.

SOFTECH, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

FOREIGN CURRENCY TRANSLATION:

The functional currency of the Company's foreign operations (France, Germany and Italy) is the Euro. As a result, assets and liabilities are translated at period-end exchange rates and revenues and expenses are translated at the average exchange rates. Adjustments resulting from translation of such financial statements are classified in accumulated other comprehensive income (loss). Foreign currency gains and losses arising from transactions are included in the statement of operations.

USE OF ESTIMATES:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant estimates included in the financial statements are the valuation of long term assets including intangibles (goodwill, capitalized software and other intangible assets), deferred tax assets and the allowance for doubtful accounts. Actual results could differ from those estimates.

(C) LIQUIDITY

As of November 30, 2006, the Company had cash of $452,000, a decrease of $228,000 from May 31, 2006. Operating activities used $828,000 of cash during the first six months of the fiscal year and the Company borrowed $653,000 in excess of its debt repayments from its line of credit. At November 30, 2006, the Company had available borrowings on its debt facilities of approximately $2.5 million.

The Company believes its current cost structure together with reasonable revenue run rates based on historical performance will generate positive cash flow during the remainder of fiscal 2007. The Company believes that the cash on hand together with cash flow from operations and its available borrowings under its credit facility will be sufficient for meeting its liquidity and capital resource needs for the next year.

(D) BALANCE SHEET COMPONENTS

Details of certain balance sheet captions are as follows (000's):

	November 30, 2006	May 31, 2006
Property and equipment	$ 4,004	$ 3,985
Accumulated depreciation and amortization	(3,871)	(3,842)
Property and equipment, net	$ 133	$ 143
Common stock, $.10 par value	$ 1,221	$ 1,221
Capital in excess of par value	18,037	18,037
Accumulated deficit	(27,342)	(26,381)
Accumulated other comprehensive income	(335)	(294)
Stockholders' deficit	$ (8,419)	$ (7,417)

SOFTECH, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(E) LOSS PER SHARE

Basic net loss per share is computed by dividing the net loss by the weighted-average number of common shares outstanding. Diluted net loss per share is computed by dividing net loss by the weighted-average number of common and equivalent dilutive common shares outstanding. Options to purchase shares of common stock have been excluded from the denominator for the computation of diluted earnings per share for all periods presented in fiscal 2007 and 2006 because their inclusion would be antidilutive. The weighted average shares outstanding for each of the income statements included in this filing are presented below (000's):

	Three and Six Month Periods Ended November 30, 2006	2005
Basic weighted average shares outstanding	12,213	12,205
Effect of employee stock options outstanding	---	---
	12,213	12,205

(F) COMPREHENSIVE LOSS

The Company's comprehensive loss includes accumulated foreign currency translation adjustments and unrealized gain (loss) on marketable securities the comprehensive loss was as follows (000's):

	Three Month Periods Ended November 30, 2006	2005
Net loss	$ (223)	$ (102)
Changes in:		
Foreign currency translation adjustment	(39)	1
Comprehensive loss	$ (262)	$ (101)

	Six Month Periods Ended November 30, 2006	2005
Net loss	$ (961)	$ (436)
Changes in:		
Foreign currency translation adjustment	(41)	5
Comprehensive loss	$(1,002)	$ (431)

SOFTECH, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(G) SEGMENT INFORMATION

The Company operates in one reportable segment and is engaged in the development, marketing, distribution and support of CAD/CAM and Product Data Management and Collaboration computer solutions. The Company's operations are organized geographically with foreign offices in France, Germany and Italy. Components of revenue and long-lived assets (consisting primarily of intangible assets, capitalized software and property, plant and equipment) by geographic location, are as follows (000's):

	Three Months Ended November 30, 2006	Three Months Ended November 30, 2005
Revenue:		
North America	$ 2,372	$ 2,492
Asia	238	318
Europe	576	787
Eliminations	(180)	(206)
Consolidated Total	$ 3,006	$ 3,391

	Six Months Ended November 30, 2006	Six Months Ended November 30, 2005
Revenue:		
North America	$ 4,156	$ 4,796
Asia	503	618
Europe	1,068	1,297
Eliminations	(225)	(252)
Consolidated Total	$ 5,502	$ 6,459

	November 30, 2006	May 31, 2006
Long Lived Assets:		

North America	$ 7,287	$ 8,004
Europe	153	155
Consolidated Total	$ 7,440	$ 8,159

SOFTECH, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS

The statements made below with respect to SofTech's outlook for fiscal 2007 and beyond represent "forward looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities and Exchange Act of 1934 and are subject to a number of risks and uncertainties. These include, among other risks and uncertainties, general business and economic conditions, generating sufficient cash flow from operations to fund working capital needs, continued integration of acquired entities, potential obsolescence of the Company's technologies, maintaining existing relationships with the Company's lenders, successful introduction and market acceptance of planned new products and the ability of the Company to attract and retain qualified personnel both in our existing markets and in new territories in an extremely competitive environment.

CRITICAL ACCOUNTING POLICIES AND SIGNIFICANT JUDGMENTS AND ESTIMATES

The Securities and Exchange Commission ("SEC") issued disclosure guidance for "critical accounting policies." The SEC defines "critical accounting policies" as those that require the application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

The Company's significant accounting policies are described in Note B to these financial statements. The Company believes that the following accounting policies require the application of management's most difficult, subjective or complex judgments:

REVENUE RECOGNITION

The Company has adopted the provisions of Statement of Position No. 97-2, "Software Revenue Recognition" (SOP 97-2) as amended by SOP No. 98-9, "Modification of SOP 97-2 Software Revenue Recognition with Respect to Certain Transactions" (SOP 98-9) in recognizing revenue from software transactions. Revenue from software license sales is recognized when persuasive evidence of an arrangement exists, delivery of the product has been made, and a fixed fee and collectibility has been determined. The company does not provide for a right of return. For multiple element arrangements, total fees are allocated to each of the elements using the residual method. Revenue from customer maintenance support agreements is deferred and recognized ratably over the term of the agreements. Revenue from engineering, consulting and training services, primarily performed on a time and material basis, is recognized as those services are rendered.

VALUATION OF LONG-LIVED AND INTANGIBLE ASSETS

The Company periodically reviews the carrying value of all intangible assets (primarily capitalized software costs and other intangible assets) and other long lived assets. If indicators of impairment exist, the Company compares the undiscounted cash flows estimated to be generated by those assets over their estimated economic life to the related carrying value of those assets to determine if the assets are impaired. If the carrying value of the asset is greater than the estimated undiscounted cash flows, the carrying value of the assets would be decreased to their fair value through a charge to operations. The Company does not have any long-lived assets it considers to be impaired.

VALUATION OF GOODWILL

Effective June 1, 2002, the Company adopted the provisions of SFAS No. 142, Goodwill and Other Intangible Assets. This statement affects the Company's treatment of goodwill and other intangible assets. This statement requires that goodwill existing at the date of adoption be reviewed for possible impairment and that impairment tests be periodically repeated, with impaired assets written down to fair value. Additionally, existing goodwill and intangible assets must be assessed and classified within the statement's criteria. Intangible assets with finite useful lives will continue to be amortized over those periods. Amortization of goodwill and intangible assets with indeterminable lives ceased as of June 1, 2002.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS

As of May 31, 2006, the Company conducted its annual impairment test of goodwill by comparing fair value to the carrying amount of its underlying assets and liabilities. The Company determined that the fair value exceeded the carrying amount of the assets and liabilities, therefore no impairment existed as of the testing date.

ESTIMATING ALLOWANCES FOR DOUBTFUL ACCOUNTS RECEIVABLE

We perform ongoing credit evaluations of our customers and adjust credit limits based upon payment history and the customer's current credit worthiness, as determined by our review of their current credit information. We continuously monitor collections and payments from our customers and maintain a provision for estimated credit losses based upon our historical experience and any specific customer collection issues that we have identified. While such credit losses have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. A significant change in the liquidity or financial position of any of our significant customers could have a material adverse effect on the collectibility of our accounts receivable and our future operating results.

VALUATION OF DEFERRED TAX ASSETS

We regularly evaluate our ability to recover the reported amount of our deferred income taxes considering several factors, including our estimate of the likelihood of the Company generating sufficient taxable income in future years during the period over which temporary differences reverse. The Company's deferred tax assets are currently fully reserved.

RESULTS OF OPERATIONS

Revenue for the three and six month periods ended November 30, 2006 was $3.0 million and $5.5 million, respectively, as compared to $3.4 million and $6.5 million for the same periods in the prior fiscal year. This represents a decrease of 11.4% for the second quarter of fiscal 2007 and 14.8% for the first half of fiscal 2007 as compared to the same periods in fiscal 2006.

Product revenue for the three and six month periods ended November 30, 2006 was approximately $759,000 and $1.15 million, respectively, as compared to $878,000 and $1.72 million for the same periods in the prior fiscal year. This represents a decrease of 13.6% for Q2 2007 and 33.2 % for the first half of fiscal 2007 as compared to the same periods in fiscal 2006. The majority of the product revenue decrease in the current quarter was related to reduced order flow for the Cadra product line, especially in Europe. The majority of the product revenue decrease in the first half of fiscal 2007 was related to the ProductCenter technology which experienced a temporary product revenue decline in the first quarter before recovering in Q2. The Cadra product line is a technology that has experienced steady revenue declines over the last five years or more as part of the normal lifecycle of technology. The ProductCenter decline for the first half of fiscal 2007 was related to the timing of purchase orders in Q1 2007.

Service revenue for the three and six month periods ended November 30, 2006 was approximately $2.2 million and $4.4 million, respectively, as compared to approximately $2.5 million and $4.7 million for the same period in fiscal 2006. This represents a decrease of 10.6% for Q2 2007 as compared to the same period in fiscal 2006 and a decrease of 8.2% for the first half of fiscal 2007 compared to the same period in fiscal 2006. The decrease in service revenue for the three and six month periods ended November 30, 2006 as compared to the same period in fiscal 2006 was due primarily to declines in both maintenance and other services related to our Cadra product line which declined 26% in Q2 2007 as compared to the same period in fiscal 2006 and by 18% for the first half of fiscal 2007 as compared to the same period in the prior fiscal year. As drafting technologies like Cadra are replaced by solid modeling technology, we expect that our Cadra customers will continue to reduce their investment in maintenance and other services such as consulting and training.

SOFTECH, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS

Revenue generated in the U.S. accounted for 79% and 76% of total revenue for the three and six month periods ended November 30, 2006, respectively, as compared to 74% of total revenue for each of the same periods in the previous year. Revenue generated in Europe for each of the three and six month periods ended November 30, 2006 was 19% of total revenue as compared to 23% and 20% of total revenue for the same periods in fiscal 2006, respectively. Revenue generated in Asia for the three and six month periods ended November 30, 2006 was 8% and 9% of total revenue, respectively, as compared to 10% and 9% of total revenue for the same period in fiscal 2006. Revenue generated in the U.S. decreased by about 5% and 13% for the three and six month periods ended November 30, 2006, respectively, as compared to the same periods in the prior fiscal year. Revenue generated in Europe decreased by about 27% and 18% for the three and six month periods ended November 30, 2006 and revenue generated in Asia decreased about 25% and 19% for the three and six month periods ended November 30, 2006, respectively, when compared to the same periods in fiscal 2006.

Gross margin as a percentage of revenue was 74.3% and 72.3 % for the three and six month periods ended November 30, 2006, respectively, as compared to 70.4% and 67.9% for the same periods in fiscal 2006. The improvement in gross margin for the three and the six months ended November 30, 2006 as compared to the prior fiscal year was due primarily to reduced amortization expense as the costs of acquiring the ProductCenter technology were fully amortized.

Research and development expenses ("R&D") were $520,000 and $1.225 million for the three and six month periods ended November 30, 2006, respectively, as compared to $692,000 and $1.37 million for the same periods in the prior fiscal year. This represents a decrease of 24.9% and 10.6% for the three and six month periods ended November 30, 2006, respectively, as compared to the same period in the prior fiscal year. The reduced spending was the result of reduced investment, mostly in the form of reduced headcount, on our technologies that have experienced continued revenue decline. While the Company remains committed to improving those technologies and ensuring their compatibility with current operating systems, our spending must reflect the reality of the revenue trend for these product lines.

Selling, general and administrative ("SG&A") expenses were $1.57 million and $3.0 million, respectively, for the three and six month periods ended November 30, 2006 as compared to $1.51 million and $2.93 million for the same period in fiscal 2006. This represents an increase of approximately 3.8% and 2.7% for the three and six month periods ended November 30, 2006, respectively, as compared to the same periods in the prior fiscal year. The increase for both periods is due primarily to severance costs incurred in Q2 2007 related to the reduction of certain Cadra sales and support personnel in the U.S. and Europe which totaled about $300,000.

The non-cash expenses related to the amortization of capitalized software and other intangible assets were $354,000 and $708,000 for the three and six month periods ended November 30, 2006 as compared to $553,000 and $1.164 million for the same periods in fiscal 2006. The decrease is related to the completion of the amortization related to the intangible assets acquired in the acquisition of the ProductCenter technology in December 2002.

Interest expense for the three and six month periods ended November 30, 2006 was approximately $367,000 and $707,000, respectively, as compared to $286,000 and

$529,000 for the same periods in fiscal 2006. This represents an increase of 28.3% for the second quarter of fiscal 2007 compared to the same period in the previous fiscal year and an increase of 33.7% for the six month period ended November 30, 2006 compared to the same period in the prior fiscal year. The average borrowings increased to approximately $14.1 million during the current quarter as compared to $13.3 million for the same period in fiscal 2006 and the interest rate on those borrowings increased to about 10.4% in the current quarter from 8.6% for the same period in fiscal 2006. The average borrowings increased to approximately $13.9 million during the first half of fiscal 2007 as compared to $13.3 million for the same period in fiscal 2006 and the interest rate on those borrowings increased to about 10.2% during the first half of fiscal 2007 as compared to 8.0% for the same period in fiscal 2006. The changes in the interest rate on our borrowings in fiscal 2007 as compared to 2006 is due to the increase in the prime rate.

SOFTECH, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS

The net loss for the three and six month periods ended November 30, 2006 was $(223,000) and $(961,000), respectively, as compared to a net loss of $(102,000) and $(436,000) for the same period in the prior fiscal year. The loss per share for the three and six month periods ended November 30, 2006 was $(.02) and $(.08), respectively. The loss per share for the three and six month periods ended November 30, 2005 was $(.01) and $(.04), respectively.

CAPITAL RESOURCES AND LIQUIDITY

As of November 30, 2006, the Company had cash of $452,000, a decrease of $228,000 from May 31, 2006. Operating activities used $828,000 of cash during the first six months of the fiscal year and the Company borrowed $653,000 in excess of its debt repayments from its line of credit. At November 30, 2006, the Company had available borrowings on its debt facilities of approximately $2.5 million.

The Company believes its current cost structure together with reasonable revenue run rates based on historical performance will generate positive cash flow during the remainder of fiscal 2007. The Company believes that the cash on hand together with cash flow from operations and its available borrowings under its credit facility will be sufficient for meeting its liquidity and capital resource needs for the next year.

FACTORS THAT MAY AFFECT FUTURE RESULTS

The Company's business is subject to many uncertainties and risks. This Form 10-QSB also contains certain forward-looking statements within the meaning of the Private Securities Reform Act of 1995. The Company's future results may differ materially from its current results and actual results could differ materially from those projected in the forward looking statements as a result of certain risk factors, including but not limited to those set forth below, other one-time events and other important factors disclosed previously and from time to time in the Company's other filings with the SEC.

OUR QUARTERLY RESULTS MAY FLUCTUATE. The Company's quarterly revenue and operating results are difficult to predict and may fluctuate significantly from quarter to quarter. Our quarterly revenue may fluctuate significantly for several reasons, including: the timing and success of introductions of our new products or product enhancements or those of our competitors; uncertainty created by changes in the market; difficulty in predicting the size and timing of individual orders; competition and pricing; and customer order deferrals as a result of general economic decline. Furthermore, the Company has often recognized a substantial portion of its product revenues in the last month of a quarter, with these revenues frequently concentrated in the last weeks or days of a quarter. As a result, product revenues in any quarter are substantially dependent on orders booked and shipped in the latter part of that quarter and revenues from any future quarter are not predictable with any significant degree of accuracy. We typically do not experience order backlog. For these reasons, we believe that period-to-period comparisons of its results of operations are not necessarily meaningful and should not be relied upon as indications of future performance.

WE MAY NOT GENERATE POSITIVE CASH FLOW IN THE FUTURE. During fiscal years 1998 through 2001 we generated significant cash losses from operations. The Company took aggressive cost cutting steps and reorganized its operations at the beginning of fiscal 2002. These actions have greatly reduced our fixed costs and resulted in positive cash flow from operations for the last four full fiscal years. Over the six fiscal quarters beginning in June 2005 and extending through the end of the current quarter we have generated a cash loss from operations of more than $800,000 as our maintenance renewal rates on our legacy product lines have declined. It is our expectation that we can correct the most recent problems of cash losses from operations and return to generating positive cash flows similar to the performance during fiscal years 2002 to 2005, however, there can be no assurances that the Company will continue to generate positive cash in the future.

DECLINE IN BUSINESS CONDITIONS AND INFORMATION TECHNOLOGY (IT) SPENDING COULD CAUSE A DECLINE IN REVENUE. Business conditions and the level of IT spending have improved in the recent past as evidenced by our revenue growth. However, there can be no assurance that this recent improvement will continue given the difficult to forecast economic environment. If IT spending declines the Company's revenues and profitability could be adversely impacted.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS

DECLINE IN BUSINESS CONDITIONS AND INFORMATION TECHNOLOGY (IT) SPENDING COULD CAUSE FURTHER DECLINE IN REVENUE. The level of future IT spending remains uncertain as does the prognosis for the continued economic recovery in the manufacturing sector. If IT spending declines and/or the manufacturing sector experiences economic difficulty, the Company's revenues could be adversely impacted.

THE COMPANY IS DEPENDENT ON ITS LENDER FOR CONTINUED SUPPORT. We have a strong relationship with our sole lender, Greenleaf Capital. They currently represent our sole source of financing. (See Note I to the Consolidated Financial Statements.)

THE CONTINUED INTEGRATION OF WTC MAY EXPERIENCE DIFFICULTY. Since acquiring WTC in December 2002, much progress has been made in integrating our operations and reducing redundant functions and facilities. The strategy includes more closely integrating our technologies and offering our combined customer base these solutions. The strategy also includes translating ProductCenter for users other than the U.S. English speaking market. This translation for our European customers was completed during fiscal 2006. In addition, during 2006 interfaces were created to proprietary CAD tools that have higher use in our European customer base. Our plans for 2007 include leveraging that technology investment by offering ProductCenter to our European customers based on the recent improvements. However, there can be no assurance that this continued integration of our technologies or offering ProductCenter outside the U.S. will be successful.

REVENUE DECLINE FOR CERTAIN PRODUCT LINES. We experienced revenue declines from 2005 to 2006 of 11% for our Cadra product line and 4% for our AMT product line. The declines for the same period for software maintenance revenue was about 11% for each of those product lines. While we understand that as these technologies age the revenue will decline as a normal part of the technology life cycle, double digit declines from year to year were not expected. Should this unexpected fiscal 2006 revenue decline for these product lines continue it will materially negatively impact the Company's overall financial performance.

ITEM 3. CONTROLS AND PROCEDURES

The Company's Chief Operating Officer is responsible for establishing and maintaining disclosure controls and procedures for the Company. Such officer has concluded (based upon his evaluation of these controls and procedures as of a date within 90 days of the filing of this report) that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in this report is accumulated and communicated to the Company's management, including its principal executive officers as appropriate, to allow timely decisions regarding required disclosure.

The Certifying Officer also has indicated that there were no significant changes in the Company's internal controls or other factors that could significantly affect such controls subsequent to the date of their evaluation, and there were no corrective actions with regard to significant deficiencies and material weaknesses.

PART II. OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(b) Reports on Form 8-K

None.

SIGNATURES

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

SOFTECH, INC.

Date: January 16, 2007

/s/ Joseph P. Mullaney

Joseph P. Mullaney
President and
Chief Operating Officer