

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

CT HOLDINGS ENTERPRISES INC
Form 10QSB
November 20, 2006

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

FORM 10-QSB

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF
THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2006

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES
EXCHANGE ACT OF 1934

COMMISSION FILE NUMBER: 0-18718

CT HOLDINGS ENTERPRISES, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE
(STATE OR OTHER JURISDICTION OF
INCORPORATION OR ORGANIZATION)

75-2242792
(I.R.S. EMPLOYER
IDENTIFICATION NO.)

TWO LINCOLN CENTRE, SUITE 1600, 5420 LBJ FREEWAY, DALLAS, TEXAS 75240
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)
(214) 520-9292
(REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE)

Indicate by check mark whether the issuer (1) has 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 the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes No

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date.

Class	Outstanding at November 17, 2006
Common Stock, Par value \$.01 per share	58,545,928

Transitional Small Business Disclosure Format Yes No

CT HOLDINGS ENTERPRISES, INC.
FORM 10-QSB
QUARTERLY REPORT
FOR THE QUARTERLY PERIOD ENDED
SEPTEMBER 30, 2006

Table of Contents

Page

PART I - FINANCIAL INFORMATION

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

Item 1	Financial Statements	3
	Unaudited Balance Sheets as of September 30, 2006 and December 31, 2005	3
	Unaudited Statements of Operations for the three and nine months ended September 30, 2006 and 2005	4
	Unaudited Statements of Cash Flows for the nine months ended September 30, 2006 and 2005	5
	Notes to Unaudited Interim Financial Statements	6
Item 2.	Management's Discussion and Analysis or Plan of Operation	11
Item 3.	Controls and Procedures	19
PART II - OTHER INFORMATION		
Item 1	Legal Proceedings	19
Item 3	Defaults Upon Senior Securities	21
Item 6.	Exhibits	21
	Signatures	22

2

PART I FINANCIAL INFORMATION
Item 1. Financial Statements

CT HOLDINGS ENTERPRISES, INC.
UNAUDITED BALANCE SHEETS

	SEPTEMBER 30, 2006	DECEMBER 31, 2005
	-----	-----
ASSETS		

CURRENT ASSETS		
Cash	\$ 197	\$
	-----	-----
TOTAL ASSETS	\$ 197	\$
	=====	=====
LIABILITIES AND STOCKHOLDERS' DEFICIT		

CURRENT LIABILITIES		
Accounts payable and accrued expenses	\$ 464,640	\$
Convertible secured note payable to related party including accrued interest of \$772 and net of deferred debt discount of \$250,290 at December 31, 2005		-
Demand note payable to Citadel including accrued interest of \$97,644 and \$76,784		322,644
Payable to Citadel		680,000

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

Advance from an officer	30,000
Note payable to shareholder including accrued interest of \$7,379 and \$6,128	16,379
Accrual for litigation including accrued interest of \$1,404,590 at December 31, 2005	1,250,000
Total current liabilities	2,763,663
COMMITMENTS AND CONTINGENCIES	
STOCKHOLDERS' DEFICIT	
Preferred stock, \$0.01 stated value per share; 1,000,000 shares authorized; no shares issued or outstanding	-
Common stock, \$.01 par value per share; 60,000,000 shares authorized; 58,545,928 shares issued and outstanding	585,460
Common stock pending issuance	600,000
Additional paid-in capital	57,661,749
Accumulated deficit	(61,610,675)
Total stockholders' deficit	(2,763,466)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	\$ 197

The accompanying notes are an integral part of these financial statements.

3

CT HOLDINGS ENTERPRISES, INC.
UNAUDITED STATEMENTS OF OPERATIONS

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS EN SEPTEMBER 30	
	2006	2005	2006	2005
Revenue	\$ -	\$ -	\$ -	\$ -
General and administrative expense	14,426	19,154	136,986	136,986
Reversal of litigation accrual	(3,333,852)		(3,333,852)	
Interest expense	48,760	106,695	460,102	460,102
Debt settlement gain	-	-	(280,359)	(280,359)
Income (loss) before income taxes	3,270,666	(125,849)	3,017,123	(125,849)
Provision for income taxes	-	-	-	-
Net income (loss)	\$ 3,270,666	\$ (125,849)	\$ 3,017,123	\$ (125,849)
Net income (loss) per share - basic and diluted	\$ 0.05	\$ 0.00	\$ 0.04	\$ 0.00
Weighted average common shares outstanding - basic and diluted	67,245,928	67,245,928	67,245,928	67,245,928

The accompanying notes are an integral part of these financial statements.

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

4

CT HOLDINGS ENTERPRISES, INC.
UNAUDITED STATEMENTS OF CASH FLOWS

	NINE MONTHS ENDED SEPTEMBER 30,	
	2006	2005
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income(loss)	\$ 3,017,123	\$ (441,691)
Adjustments to reconcile net income(loss) to net cash used in operating activities:		
Debt forgiveness gain	(280,359)	-
Amortization of deferred debt discount	250,290	75,000
Accrual for litigation and related interest	179,262	208,770
Reversal of litigation accrual	(3,333,852)	-
Changes in operating assets and liabilities:		
Accounts payable and accrued expenses	137,536	87,950
Payable to Citadel	30,000	55,000
	-----	-----
NET CASH USED IN OPERATING ACTIVITIES	-	(14,971)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from advances and notes payable to related parties	-	11,000
	-----	-----
NET CASH PROVIDED BY FINANCING ACTIVITIES	-	11,000
Net change in cash	-	(3,971)
Cash and cash equivalents at the beginning of the period	197	4,168
	-----	-----
Cash and cash equivalents at the end of the period	\$ 197	\$ 197
	=====	=====
Supplemental cash flow information:		
Non-cash financing items:		
Payment of liability by officer recorded as an advance	\$ 30,000	\$ -
	=====	=====

The accompanying notes are an integral part of these financial statements.

5

CT HOLDINGS ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2006

NOTE A - NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Interim Financial Statements and Basis of Presentation

These unaudited interim financial statements have been prepared on the historical cost basis in accordance with accounting principles generally accepted in the United States and in the opinion of management, reflect all

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

adjustments (consisting of normal, recurring adjustments) necessary to present fairly, the financial position, results of operations and cash flows of CT Holdings Enterprises, Inc. ("CT Holdings" or the "Company"). On March 13, 2006 the Company changed its name from CT Holdings, Inc. to CT Holdings Enterprises, Inc.

Some information and footnote disclosures normally included in the financial statements prepared in accordance with generally accepted accounting principles in the United States have been condensed or omitted pursuant to rules and regulations promulgated by the Securities and Exchange Commission (the "Commission"). The results of operations for the interim periods shown herein are not necessarily indicative of the results to be expected for any future interim period or for the entire year. These statements should be read together with the audited financial statements and notes thereto included in the Company's Form 10-KSB for the year ended December 31, 2005 on file with the Commission.

Description of Business

CT Holdings provides management expertise including consulting on operations, marketing and strategic planning and a single source of capital to early stage technology companies. The Company was incorporated in Delaware in 1992. The business model is designed to enable the companies with whom the Company acquires or invests to become market leaders in their industries. The strategy over the years has led to the development, acquisition and operation of technology based businesses with compelling valuations and strong business models. The goal is to realize the value of these investments for the Company's shareholders through a subsequent liquidity event such as a sale, merger or initial public offering of the investee companies.

At December 31, 2005 the Company held investments in two companies, Parago, Inc. ("Parago") and River Logic, Inc. ("River Logic"). On May 22, 2006 the Company and CITN Investment Inc. ("CII"), an affiliate of the Company's CEO, entered into a settlement, pursuant to which CII agreed to release the Company from indebtedness and accrued interest under the Amended and Restated Secured Convertible Promissory Note (the "Amended Note") of \$271,148 plus accrued interest of \$9,211 through May 22, 2006, in exchange for the delivery to CII of the shares of Parago and River Logic owned by the Company. The carrying value of these shares was zero at the settlement date as the investments had been written off in prior periods due to continuing operating losses, lack of cash flows generated from the investments and other factors. The Company, therefore, has recorded a \$280,359 gain on debt settlement for the nine months ended September 30, 2006. CII has agreed to return to the Company the excess, if any, of the proceeds realized from a future sale of the shares over the amounts owed at May 22, 2006 under the Amended Note plus any costs related to the sale of the shares or collection of the proceeds. While CII has agreed to return the excess, if any, of the proceeds realized from a future sale of the shares over amounts owed under the Amended Note plus any costs of sale of the shares or collection of the proceeds, there can be no assurance that a future sale will occur, nor that the Company will receive any proceeds following the sale of the shares. In addition CII has an option to purchase 51% of the Company's fully diluted shares of common stock pursuant to the terms of the settlement for a period ending the earlier of May 18, 2011 or the 60th day after a reverse stock split is implemented.

Liquidity

The Company has incurred recurring operating losses and has a significant stockholders' deficit at September 30, 2006 of approximately \$3 million. At September 30, 2006 there is a cash balance of \$197 and current liabilities total approximately \$3 million. The Company has limited access to capital at September 30, 2006, no plans to raise capital,

and management has not identified sources of capital at September 30, 2006. Past funding needs of the business have been provided by financings through notes payable, cash advances and additional investments from related parties, including the Company's CEO and CII, an affiliate of the Company's CEO, however there can be no assurance that such funds will be available from these related parties in the future. The Company has been and continues to be dependent upon outside financing to perform its business development activities, make investments in new technology companies and to fund operations.

The Company will continue to require working capital to fund operating expenses. At September 30, 2006 the Company has not identified sources of capital nor does the Company have any plans to raise sufficient amounts of capital to settle liabilities or to fund business development activities.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

Net Income/Loss per Common Share

Basic net income/loss per common share is computed by dividing net income/loss to common shareholders by the weighted average number of shares of common stock outstanding during the period.

Included in the weighted average number of common shares outstanding for the three and nine months ended September 30, 2006 and 2005 are 2,700,000 shares that would have been issued when a shareholder exercised his right to convert a note payable to common stock and 6,000,000 shares that would have been issued to the Company's CEO when he exercised his right to exchange Parago shares for CT Holdings' shares if the Company had the available authorized shares. These shares have been included in the computation from the dates that they would have been issued. The effect of stock options for 2,917,500 shares of common stock outstanding at September 30, 2006 and 2005, have been excluded from the weighted average shares computations as they are antidilutive. At September 30, 2006 and 2005, the Company does not have any outstanding stock options or warrants that have an exercise price below market value.

Stock-Based Compensation

On January 1, 2006, the Company adopted the modified prospective method of SFAS No. 123 (revised 2004), "Share-Based Payment" ("SFAS No. 123R"), which is a revision of SFAS No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123). SFAS No. 123R supersedes APB Opinion No. 25, and amends SFAS No. 95, "Statement of Cash Flows". SFAS No. 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values. Pro forma disclosure is no longer an alternative. Under the modified prospective application, SFAS No. 123R is applied to new awards and to awards modified, repurchased or cancelled after the effective date. Compensation cost for the portion of awards for which requisite service has not been rendered that are outstanding as of the effective date is recognized as the requisite service is rendered on or after the effective date. The compensation cost for that portion of awards is based on the grant date fair value of those awards as calculated for pro-forma disclosures under SFAS No.

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

123. All awards outstanding at September 30, 2006 had been fully vested in periods prior to the first quarter of 2006 and therefore, the financial statements do not reflect any compensation expense related to stock-based compensation.

The Company does not have any employees or significant operations and does not anticipate issuing any share-based payments in the future, therefore the SFAS 123R is not expected to have a significant effect on the Company's financial condition, cash flows or results of operations. However should the Company's operations change, and include the issuance of share-based payments, SFAS No. 123R would require the recording of stock compensation expense in the future.

7

Prior to January 1, 2006, the Company accounted for stock-based employee compensation arrangements in accordance with provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and complied with the disclosure provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" as amended by SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure, an amendment of FASB Statement No. 123". Under APB Opinion No. 25, compensation expense for employees is based on the excess, if any, on the date of grant, of the fair value of the Company's stock over the exercise price and is recognized on a straight-line basis over the vesting term of the option.

The Company accounts for equity instruments issued to non-employees in accordance with the provisions of SFAS No. 123 and SFAS No. 148 and Emerging Issues Task Force Issue No. 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services." All transactions in which goods or services are the consideration received for the issuance of equity instruments are accounted for based on the fair value of the consideration received or the fair value of the equity instrument issued, whichever is more reliably measurable. The measurement date of the fair value of the equity instrument issued is the earlier of the date on which the counterparty's performance is complete or the date on which it is probable that performance will occur.

If the Company had recognized compensation expense in accordance with SFAS No. 123R for the three and nine months ended September 30, 2005, the pro forma effect on net loss would not have differed from reported net loss.

NOTE B - NOTES PAYABLE TO SHARHOLDERS

The Company has presented \$600,000 as "Common stock pending issuance", a separate component of Stockholders' Deficit at September 30, 2006 and December 31, 2005. This represents 2,700,000 shares of CT Holdings that were to be issued upon the conversion of a note payable to a shareholder in 2003. Due to the lack of available authorized shares, the shareholder has waived his right to receive these shares until such time as the shares become authorized.

The Company has a note payable which was originally due June 30, 2002 for \$9,000 to a shareholder which was in default at September 30, 2006 and December 31, 2005 and because it is in default, bears interest at 18% per annum. Accrued interest on the note payable was \$7,379 and \$6,128 at September 30, 2006 and December 31, 2005, respectively.

NOTE C - RELATED PARTY TRANSACTIONS

On May 24, 2004, the Company was advanced \$200,000 by CII pursuant to a loan agreement and evidenced by a Secured Convertible Promissory Note (the "Note"). In December 2005, the Company and CII entered into the Amended Note. Pursuant to

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

the Amended Note, the principal was increased to \$271,148 resulting from the combination of the principal and accrued interest from the original note with CII and advances of \$43,800 plus accrued interest of \$1,222 through the issue date of the Amended Note. The Amended Note accrued interest at 8% per annum, was due the earlier of May 24, 2006 or demand by CII.

The conversion price of the Amended Note of approximately \$0.00113 per share was below the fair value per share of the common stock at the date the note was issued. Accordingly, the Company recorded the fair value of the beneficial conversion feature of the note payable of \$271,148 as debt discount. The amortization of the debt discount is a component of interest expense on the statements of operations. The debt discount was amortized over the life of the Amended Note through its settlement and was fully amortized in May 2006. As a result, no amortization expense was recorded during the three months ended September 30, 2006 which compares to \$25,000 of amortization expense recorded for the three months ended September 30, 2005. Debt discount amortization was \$250,920 and \$75,000 for the nine months ended September 30, 2006 and 2005, respectively. The Amended Note was recorded net of deferred debt discount of \$250,290 at December 31, 2005.

8

On May 22, 2006 the Company and CII entered into a settlement, pursuant to which CII agreed to release the Company from indebtedness and accrued interest under the Amended Note of \$271,148 plus accrued interest of \$9,211 through May 22, 2006, in exchange for the delivery to CII of the shares of Parago and River Logic owned by the Company. The Company recorded a debt forgiveness gain related to this transaction in the amount of \$280,359 in the second quarter of 2006. CII has agreed to return to the Company the excess, if any, of the proceeds realized from a future sale of the shares over the amounts owed at May 22, 2006 under the Amended Note plus any costs related to the sale of the shares or collection of the proceeds. While CII has agreed to return the excess, if any, of the proceeds realized from a future sale of the shares over amounts owed under the Amended Note plus any costs of sale of the shares or collection of the proceeds, there can be no assurance that a future sale will occur, nor that the Company will receive any proceeds following the sale of the shares.

During the nine months ended September 30, 2006, the CEO advanced the Company \$30,000 which is presented on the balance sheet at September 30, 2006 as an advance from an officer.

In April 2003, CT Holdings obtained \$225,000 from Citadel to pay a legal settlement for an unsecured Note Payable to Citadel due on demand and bearing interest at 12% per year. The accrued interest on the note payable at September 30, 2006 and December 31, 2005, was \$97,644 and \$76,784, respectively.

During 2005, the Company's CEO advanced \$38,800 and in December 2005, this amount plus a \$5,000 note due to the Company's CEO were converted to principle in the Amended Note previously discussed. In October 2004, the Company obtained a \$5,000 90-day note, bearing interest at 5% per year, from the CEO of the Company. In December 2005, these amounts were converted into the Amended Note previously discussed.

Pursuant to the terms of the transition services agreement with Citadel Security Software Inc., ("Citadel") the Company has agreed to pay Citadel \$10,000 per quarter (reduced in July 2005 from \$7,500 per month) for the services of its CEO, CFO and accounting and information management staff, as well as office rent and indirect overhead expenses. The Company has a liability recorded for \$680,000 and \$650,000 for amounts payable to Citadel under this agreement at September 30, 2006 and December 31, 2005, respectively. The transition services agreement expired in May 2006. Currently, Citadel provides services to CT

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

Holdings on a month-to-month basis.

In June 2001, the Company's CEO and a director funded and guaranteed CT Holdings' participation in the Parago bridge loan. In consideration for this funding and guarantees, CT Holdings has agreed to permit the CEO to exchange up to 5,000,000 (pre 1:1000 reverse stock split) Parago shares into up to 6,000,000 shares of CT Holdings' common stock. The CEO exercised the exchange right in February 2004. The CEO waived his right to receive the shares of CT Holdings until the authorized shares become available.

NOTE D - COMMITMENTS AND CONTINGENCIES

In August 1998, Janssen-Meyers Associates L.P. (JMA) filed a lawsuit against the Company arising out of an alleged 1995 contract with the Company's predecessor (Old Citadel). The suit alleged that Old Citadel breached a letter of intent dated September 1995 and/or a Placement Agency Agreement dated November 1995 between JMA and Old Citadel. As its damages, JMA claimed that it was entitled to, among other things, the cash value of warrants to purchase 1.8 million shares of CT Holdings common stock at an exercise price of \$0.89 per share, valued during May 1996. According to JMA's valuation of those warrants, potential damages were alleged to exceed \$40 million. The Company vigorously disputes that it breached either the letter of intent or the Placement Agency Agreement or that it is liable to JMA. The lawsuit was styled Janssen-Meyers Associates, L.P. v. Citadel Technology, Inc., and was filed in the Supreme Court of the State of New York, County of New York. The Company removed the case to federal court in the Southern District of New York.

Following mediation in July 2000, the Company entered into a settlement term sheet, to attempt to resolve the disputes between it and JMA, pursuant to which the Company and JMA agreed in principle to settle the lawsuit for an

9

aggregate of \$3 million, in a combination of \$1.5 million in cash and 300,000 shares of the Company's common stock with a guaranteed value of \$5 per share as of January, April and October 2001 (with respect to 100,000 of the shares for each period). The settlement was subject to execution of definitive settlement documents and approval of the boards of directors of both parties.

However, the Company and JMA were unable to negotiate the final definitive settlement agreement. The case was dismissed in August 2000 without any resolution of this issue. On March 27, 2001, JMA attempted to reopen this matter, but the Court hearing the JMA lawsuit issued a Summary Order denying JMA's motion to enforce the settlement term sheet and confirmed the prior dismissal of the lawsuit. The Court further ruled that JMA would either have to bring an action on the proposed settlement or move to re-open the dismissed case. The Court stated that it did not express any view with respect to the merits of the settlement that brought about the dismissal of the case. There was no activity on the case from March 2001 through August 2001. On August 27, 2001 JMA refiled its lawsuit with a federal court in New York, and the Company filed its motion to dismiss the case because the plaintiffs lacked the required diversity jurisdiction to pursue the claims in federal court. On October 31, 2001 the case was dismissed in federal court. In December 2001, the plaintiffs refiled the lawsuit in the state court seeking to enforce the proposed settlement term sheet. The case was filed in Supreme Court of New York, that state's trial court, in a case styled Roan Meyers v. CT Holdings. CT Holdings has filed counterclaims for breach of the term sheet as well as breach of the placement agency agreement. Cross motions for partial summary judgments have been argued but on June 9, 2004 the court entered judgment in favor of Roan-Meyers in the amount of \$3,000,000 and granted interest at the rate of 9% from October 31, 2000 through the date of final judgment, and thereafter at the

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

statutory rate allowed by law. The Company appealed the final judgment but the appellate court affirmed the trial court's decision. The Company is assessing its alternatives and intends to vigorously defend this case.

On April 8, 2005, Meyers Associates, L.P. f/k/a Roan/Meyers Associates, L.P. and f/k/a Janssen-Meyers Associates, L.P. ("Meyers") filed a lawsuit in the Court of Chancery of the State of Delaware, in New Castle County, against the Company, Citadel Security Software, Inc. (Citadel) including Steven B. Solomon, the Chief Executive and a Director of the Company, Chris A. Economou, a Director of the Company, Lawrence Lacerte, a former Director of the Company, and Phillip J. Romano, a former Director of the Company (the "Individual Defendants"). The suit alleges that in connection with an action filed in the Supreme Court of New York, New York County, to enforce a Settlement Term Sheet executed on July 7, 2000 by Meyers and CT Holdings, Meyers was awarded a judgment against CT Holdings in the amount of \$3 million plus interest on the judgment at the rate of 9% from October 31, 2000 until the date of entry of that judgment and thereafter at the statutory rate (the "Judgment"). The suit alleges that CT Holdings' May 2002 spin-off of its interests in Citadel to CT Holdings' shareholders rendered CT Holdings insolvent and constituted a fraudulent conveyance to defraud CT Holdings' creditors, including Meyers. The suit asserts fraudulent conveyance claims against Citadel and CT Holdings pursuant to Delaware statutory and common law. The suit also asserts a claim against Citadel for successor liability as the alleged successor in interest or alter ego of CT Holdings. The suit alleges that the Individual Defendants who were officers and/or directors of CT Holdings at the time of the spin-off breached fiduciary duties allegedly owed to creditors of CT Holdings, including Meyers, by approving and allowing the spin-off transaction. The suit seeks to void the spin-off transaction or alternatively to hold Citadel liable for the Judgment including interest, to recover damages against the Individual Defendants in an amount not less than the Judgment including interest, plus an unspecified amount of punitive, consequential and incidental damages, as well as attorneys' fees and costs.

On August 23, 2006, CT Holdings and certain other parties entered into a Release and Settlement Agreement ("Agreement") by and among Meyers and their related parties (collectively, the "Meyers Released Parties") on the one hand and defendants CT Holdings Enterprises, Citadel Security Software Inc., Steven B. Solomon, Chris A. Economou, Lawrence Lacerte, Mark Rogers, Phillip J. Romano, Axel Sawallich, George Sharp and Gilbert Gertner (collectively "Defendants") on the other hand. The Agreement provides for the settlement of litigation filed by Meyers Associates against defendants Citadel, CT Holdings Enterprises, certain of Citadel's current and former directors and officers Steven B. Solomon, Chris E. Economou, Lawrence Lacerte, Mark Rodgers, Phillip J. Romano and Axel Sawallich in the Court of Chancery of the State of Delaware in and for New Castle County (the "Delaware Action") asserting

10

various claims, and other litigation against CT Holdings and its former officers and directors (the "Actions"). Pursuant to the Agreement, Citadel Security Software shall pay the sum of \$1,250,000 to Meyers Associates in two payments, the first payment of \$250,000 upon signing of the Agreement the second payment of \$1,000,000 no later than November 1, 2006. The Defendants will be released by the Plaintiffs from all claims in the actions 91 days after receipt of the payments, subject to the terms and conditions of the agreement. The first payment of \$250,000 was made by Citadel in August 2006. If Citadel fails to make the second payment of \$1,000,000 the defendants are not entitled to offset or reduce the settlement by the initial payment of \$250,000. Accordingly, the Company reduced its liability for this legal claim to \$1,250,000 at September 30, 2006. The second payment of \$1,000,000 was made by Citadel on November 1, 2006 therefore pursuant to the Agreement, the Company is expected to be released

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

from any further claims under this lawsuit.

The Company may become involved from time to time in litigation on various matters which are routine to the conduct of our business. The Company believes that none of these actions, individually or in the aggregate, will have a material adverse effect on our financial position or results of operations, though any adverse decision in these cases or the costs of defending or settling such claims could have a material adverse effect on our business.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS' OR PLAN OF OPERATIONS

The following discussions should be read in conjunction with our audited financial statements and related notes included in our Annual Report on Form 10-KSB for the year ended December 31, 2005. Our year ends on December 31, and each of our quarters end on the final day of a calendar quarter (March 31, June 30, and September 30). The following discussions contain forward-looking statements. Please see Cautionary Statement Regarding Forward-Looking Statements and Risk Factors for a discussion of uncertainties, risks and assumptions associated with these statements.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This report on Form 10-QSB contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. CT Holdings Enterprises, Inc. ("CT Holdings" or the "Company") bases these forward-looking statements on its expectations and projections about future events, which CT Holdings has derived from the information currently available to it. In addition, from time to time, CT Holdings or its representatives may make forward-looking statements orally or in writing. Furthermore, forward-looking statements may be included in CT Holdings' filings with the Securities and Exchange Commission or press releases or oral statements made by or with the approval of one of CT Holdings' executive officers. For each of these forward-looking statements, CT Holdings claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements relate to future events or CT Holdings' future performance, including but not limited to:

- possible or assumed future results of operations;
- future revenue and earnings; and
- business and growth strategies.

Forward-looking statements are those that are not historical in nature, particularly those that use terminology such as may, could, will, should, likely, expects, anticipates, contemplates, estimates, believes, plans, projected, predicts, potential or continue or the negative of these or similar terms. The statements contained in this Report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including statements regarding the Company's expectations, beliefs, intentions or strategies regarding the future. Forward-looking statements are subject to certain known and unknown risks and uncertainties that could cause actual results to differ materially from those expressed in any forward-looking statements. These risks and uncertainties include, but are not limited to, the following important factors with respect to CT Holdings:

- the uncertainty of general business and economic conditions;
- the financial performance of our investments;
- adverse developments, outcomes and expenses in legal proceedings; and

- those described under Risk Factors included in this document.

Forward-looking statements are only predictions as of the date they are made and are not guarantees of performance. All forward-looking statements included in this document are based on information available to CT Holdings on the date of this Report on Form 10-QSB. Readers are cautioned not to place undue reliance on forward-looking statements. The forward-looking events discussed in this Report on Form 10-QSB and other statements made from time to time by CT Holdings or its representatives may not occur, and actual events and results may differ materially and are subject to risks, uncertainties and assumptions about CT Holdings including without limitation those discussed elsewhere in this Form 10-QSB under the heading Risk Factors as well as those discussed elsewhere in this Form 10-QSB, and the risks discussed in our Securities and Exchange Commission filings. Except for their ongoing obligations to disclose material information as required by the federal securities laws, CT Holdings is not obligated to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this Report on Form 10-QSB and in other statements made from time-to-time by CT Holdings or its representatives might not occur.

RISK FACTORS

Investing in our common stock involves a high degree of risk. Any of the following risks could materially adversely affect our business, operating results and financial condition and could result in a complete loss of your investment.

In addition to the other information in this Report, the following factors should be considered carefully in evaluating the Company and its business. This disclosure is for the purpose of qualifying for the safe harbor provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. It contains factors that could cause results to differ materially from such forward-looking statements. These factors are in addition to any other cautionary statements, written or oral, which may be made or referred to in connection with any such forward-looking statement.

The following matters, among other things, may have a material adverse effect on the business, financial condition, liquidity, or results of operations of the Company. Reference to these factors in the context of a forward-looking statement or statements shall be deemed to be a statement that any one or more of the following factors may cause actual results to differ materially from those in such forward-looking statement or statements. Before you invest in our common stock, you should be aware of various risks, including those described below. Investing in our common stock involves a high degree of risk. You should carefully consider these risk factors, together with all of the other information included in this Report, before you decide whether to purchase shares of our common stock. Our business and results of operations could be seriously harmed by any of the following risks. The trading price of our common stock could decline due to any of these risks, and you may lose part or all of your investment.

GENERAL RISKS

WE HAVE RECEIVED A GOING CONCERN REPORT FROM OUR INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM, HAVE A HISTORY OF NET LOSSES AND WILL NEED ADDITIONAL FINANCING TO CONTINUE AS A GOING CONCERN.

We received a report from our independent registered public accounting firm for

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

our year ended December 31, 2005 containing an explanatory paragraph that describes the uncertainty regarding our ability to continue as a going concern due to our recurring operating losses and our significant working capital deficiency. Historically, we have incurred recurring operating losses and have a significant stockholders' deficit at September 30, 2006 of approximately \$3 million. We had a cash balance of \$197 at September 30, 2006 and current liabilities total approximately \$3 million. We have limited access to capital, no plans to raise capital, and we have not identified sources of capital at September 30, 2006. Our past funding needs of the business have been provided by financings through short-term notes payable and additional investments from related parties, including our CEO and CITN Investment Inc. ("CII"), an entity of

12

which our CEO is an officer, director and 50% shareholder, however there can be no assurance that such funds will be available from these related parties in the future. The Company has been and continues to be dependent upon outside financing to perform its business development activities, make investments in new technology companies and to fund operations.

OUR BUSINESS FOCUS IS THE DEVELOPMENT AND ACQUISITION OF EARLY STAGE COMPANIES; HENCE, WE WILL ENCOUNTER NUMEROUS RISKS ASSOCIATED WITH OUR BUSINESS FOCUS AND OUR PRIOR OPERATING HISTORY MAY NOT BE A MEANINGFUL GUIDE TO EVALUATING OUR FUTURE PERFORMANCE.

Our business model is designed to enable the companies in whom we invest or acquire to become market leaders in their industries. Our strategy over the years has led to the development, acquisition and operation of technology based businesses with strong business models and compelling valuations. We believe that the anticipated growth in technology creates strong opportunities for us to increase shareholder value by investing in early stage ventures well positioned for growth in their respective marketplaces. Our business strategy seeks to increase the value of each investee by providing management, marketing and financial expertise along with financial capital and then realize this new value through a subsequent liquidity event such as a sale, merger or initial public offering of the investee companies. However, the impact of any advice and expertise may be limited due to a lack of a significant ownership percentage in any of our investees and the lack of available capital.

In May 2002, we were successful in spinning off of Citadel Security Software Inc. ("Citadel") into a standalone company through the pro-rata dividend distribution of Citadel common stock to shareholders of CT Holdings. At the time of the spin-off, which was first considered in November 2001, Citadel was losing substantial amounts of money and the investee assets of CT Holdings were more valuable than the assets in Citadel. At December 31, 2005 we held investments in two companies, Parago and River Logic. The respective carrying values of the investments in Parago and River Logic were written down in prior periods and have no carrying value at December 31, 2005 and were transferred to CII following a settlement in May 2006. See Note C to the financial statements for a description of the transaction. The lack of availability of private and public capital available to us has prevented us from making any additional investments and there can be no assurance that the availability of capital will improve so that we can execute our business plan.

We have a limited history in executing our business strategy. As a consequence, our prior operating history may not provide a meaningful guide to our prospects in emerging markets. Moreover, our business model and prospects must be considered in light of the risk, expense and difficulties frequently encountered by companies in early stages of development, particularly companies in new and rapidly evolving markets. We may be unable to execute our strategy of developing

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

our business due to numerous risks, including the following:

- We may be unable to identify or develop relationships with emerging companies.
- Any companies that we are able to attract may not succeed and the value of our assets and the price of our common stock could consequently decline.
- Our business model is unproven and depends on the willingness of companies to participate in our business development model and collaborate with each other and us.
- Our expenses may increase as we build the infrastructure necessary to implement this model.
- We face competition from other incubators, some of which are publicly traded companies, venture capital companies and large corporations; many of these competitors have greater financial resources and brand name recognition than we do, which may make it difficult for us to effectively compete.

13

- We will require additional capital resources in order to implement our business model and we may not be able to obtain these resources on attractive terms, if at all.

WE MAY INCUR SIGNIFICANT COSTS TO AVOID INVESTMENT COMPANY STATUS AND MAY SUFFER OTHER ADVERSE CONSEQUENCES IF WE ARE DEEMED TO BE AN INVESTMENT COMPANY.

We may incur significant costs to avoid investment company status and may suffer other adverse consequences if we are deemed to be an investment company under the Investment Company Act of 1940. Some of our contemplated equity investments in other businesses may constitute investment securities under the 1940 Act. A company may be deemed to be an investment company if it owns investment securities with a value exceeding 40% of its total assets, subject to certain exclusions. Investment companies are subject to registration under, and compliance with, the 1940 Act unless a particular exclusion or Securities and Exchange Commission safe harbor applies. If we were to be deemed an investment company, we would become subject to the requirements of the 1940 Act. As a consequence, we would be prohibited from engaging in some businesses or issuing our securities and might be subject to civil and criminal penalties for noncompliance. In addition, certain of our contracts might be voided, and a court-appointed receiver could take control of us and liquidate our business. Following the Distribution of Citadel, we may be deemed to be an investment company unless we qualify for a safe harbor within the time permitted under the 1940 Act.

Unless an exclusion or safe harbor was available to us, we would have to attempt to reduce our investment securities as a percentage of our total assets. This reduction could be accomplished in a number of ways, including the disposition of investment securities and the acquisition of non-investment security assets. If we were required to sell investment securities, we may sell them sooner than we may otherwise have preferred. These sales may be at depressed prices and we might never realize anticipated benefits from, and may incur losses on, these investments. Some investments may not be sold due to contractual or legal restrictions or the inability to locate a suitable buyer. Moreover, we may incur tax liabilities when we sell assets. We may also be unable to purchase additional investment securities that may be important to our operating strategy. If we decide to acquire non-investment security assets, we may not be able to identify and acquire suitable assets and businesses.

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

OUR STOCK IS TRADED IN THE OVER THE COUNTER MARKET.

Our common stock was de-listed from the NASDAQ SmallCap Market on May 17, 2001, because we did not meet the NASDAQ's requirements for continued listing. Our common stock now trades on the OTC Bulletin Board. The OTC Bulletin Board is generally considered to be a less efficient market, and our stock price, as well as the liquidity of our common stock, may be adversely impacted as a result. The OTC Bulletin Board requires that listed companies remain current in their filings with the Securities and Exchange Commission. If we are unable to remain current in our SEC filings, due to lack of funds or personnel or otherwise, we could be delisted from the OTC Bulletin Board, and our stock would trade, if at all, on the pink sheets.

WE ARE INVOLVED IN LEGAL PROCEEDINGS THAT COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR BUSINESS

We are involved in legal proceedings as described in PART II Item 1. Legal Proceedings and from time to time, we may be subject to other legal proceedings, including but not limited to claims that we have infringed the intellectual property rights of others, product liability claims, or other claims incidental to our business. While we intend to defend such lawsuits, adverse decisions or settlements, and the costs of defending such suits, could have a material adverse effect on our business.

14

IF WE LOSE THE SERVICES OF CITADEL UNDER THE TRANSITION SERVICES AGREEMENT, OUR BUSINESS WILL SUFFER.

We are dependent on the services provided by employees of Citadel under a transition services agreement. Our business would be negatively impacted if we were to lose the availability of these services. Citadel has entered into an asset purchase agreement pursuant to which Citadel has agreed to sell substantially all of its assets and wind down its operations subject to certain closing conditions. There can be no assurance that Citadel will continue to provide services to us if the closing occurs under the asset purchase agreement.

MEMBERS OF OUR BOARD OF DIRECTORS MAY HAVE INTERCOMPANY CONFLICTS OF INTEREST AFTER OUR SPIN-OFF.

Members of the board of directors and management of CT Holdings own shares of both Citadel and CT Holdings common stock after the spin-off of Citadel to our shareholders. In addition, following the spin-off, three of the four directors of CT Holdings are also directors of Citadel, and the Chief Executive Officer and Chief Financial Officer of CT Holdings also continue to serve as Chief Executive Officer and Chief Financial Officer of Citadel. These relationships could create, or appear to create, potential conflicts of interest when our directors and executives are faced with decisions that could have different implications for Citadel and CT Holdings. Examples of these types of decisions might include the resolution of disputes arising out of the agreements governing the relationship between CT Holdings and Citadel following the spin-off. Also, the appearance of conflicts, even if such conflicts do not materialize, might adversely affect the public's perception of CT Holdings following the spin-off.

OUR EARNINGS AND STOCK PRICE ARE SUBJECT TO SIGNIFICANT FLUCTUATIONS.

Due to the factors noted in this Report, our earnings and stock price have been and may continue to be subject to significant volatility, particularly on a quarterly basis. We have experienced no revenue or earnings which have had an immediate and significant adverse effect on the trading price of our common

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

stock. This may occur again in the future.

FAILURE TO QUALIFY AS A TAX-FREE TRANSACTION COULD RESULT IN SUBSTANTIAL LIABILITY

In May 2002, CT Holdings effected a pro rata distribution of the common stock of Citadel to Stockholders of CT Holdings in a ratio of one (1) share of Citadel common stock for every four (4) shares of CT Holdings common stock. CT Holdings and Citadel intend for the Distribution to be tax-free for U.S. federal income tax purposes. Neither CT Holdings nor Citadel has requested an advance ruling from the Internal Revenue Service, or any opinion of their tax advisors, as to the tax consequences of the Distribution. No assurance can be given that the Internal Revenue Service or the courts will agree that the Distribution is tax-free.

If the Distribution does not qualify for tax-free treatment, a substantial corporate tax would be payable by the consolidated group of which CT Holdings is the common parent measured by the difference between (1) the aggregate fair market value of the Citadel Shares on the Distribution Date and (2) CT Holdings' adjusted tax basis in the Citadel Shares on the Distribution Date. The corporate level tax would be payable by CT Holdings. However, Citadel has agreed under certain circumstances to indemnify CT Holdings for all or a portion of this tax liability. In addition, under the applicable treasury regulations, each member of CT Holdings' consolidated group (including Citadel) is severally liable for such tax liability.

Furthermore, if the Distribution does not qualify as tax-free, each CT Holdings stockholder who received Citadel Shares in the Distribution would be taxed as if he had received a cash dividend equal to the fair market value of his Citadel Shares on the Distribution Date.

Even if the Distribution qualifies as tax-free, CT Holdings could nevertheless incur a substantial corporate tax liability under Section 355(e) of the Internal Revenue Code of 1986, as amended (the Internal Revenue Code or the Code), if CT Holdings or Citadel were to undergo a change in control (whether by acquisition, additional share issuance or otherwise) pursuant to a plan or series of related transactions which include the Distribution. Any transaction which occurs within the four-year period beginning two years prior to the Distribution is presumed to be part of a plan or series of related transactions which includes the Distribution unless CT Holdings establishes otherwise. Under certain

15

circumstances, Citadel would be obligated to indemnify CT Holdings for all or a portion of this substantial corporate tax liability under the tax disaffiliation agreement.

OUR BUSINESS

CT Holdings Enterprises, Inc. provides management expertise and sources of capital to early stage companies. We were incorporated in Delaware in 1992. On March 13, 2006 the Company changed its name to CT Holdings Enterprises, Inc. Our business model is designed to enable the companies in which we invest or acquire to become market leaders in their industries. Our strategy is expected to lead to the development, acquisition and operation of technology based businesses with compelling valuations and strong business models. We believe that the anticipated growth in technology creates strong opportunities for us to increase shareholder value by investing in well-positioned early stage ventures. Our goal is to realize the value of our investments for our shareholders through a subsequent liquidity event such as a spin-off, sale, merger or initial public offering of the investee companies.

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

At September 30, 2006 our lack of available capital has limited our ability to raise sufficient capital to invest in additional companies and technologies that could offer us and our shareholders a reasonable rate of return on their investment in the foreseeable future. We expect that if and when capital becomes available to us, we may continue our business development and investment activities, however there can be no assurance that any capital will be available to us. Until such time as capital becomes available the Company's business activities will be limited to reviewing investment opportunities, filing of compliance documents and defending the lawsuits disclosed in Part II, Item 1 - Legal Proceedings.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to our investments in our investee companies and commitments and contingencies. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies are most important to the presentation of our financial statements and require the most difficult, subjective and complex judgments.

IMPAIRMENT CHARGES

We periodically evaluate the carrying value of our ownership interests in our investee companies for possible impairment based on achievement of business plan objectives and milestones, the value of each ownership interest in the investee company relative to carrying value, the financial condition and prospects of the investee company, and other relevant factors. The business plan objectives and milestones we consider include, among others, those related to financial performance such as achievement of planned financial results or completion of capital raising activities, and those that are not primarily financial in nature such as obtaining key business relationships or the hiring of key employees. If an indication of impairment exists with respect to the carrying value of an investee company, we perform an evaluation by comparing the estimated fair value of the asset with its carrying value. Fair value is determined by estimating the cash flows related to the asset, including estimated proceeds on disposition, if any. If the fair value is less than the carrying value a loss is recorded.

16

COMMITMENTS AND CONTINGENCIES

From time to time, we are a defendant or plaintiff in various legal actions. We are also a guarantor of various third-party obligations and commitments. We are required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. A determination of the amount of reserves required for these contingencies, if any, which would be charged to earnings, is made after careful analysis of each individual issue. The required reserves may change in the future due to new developments in each

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

matter or changes in circumstances, such as a change in settlement strategy. Changes in required reserves could increase or decrease our earnings in the period the changes are made.

RESULTS OF OPERATIONS FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2006 AS COMPARED WITH THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2005

Our operations consist of costs and expenses for providing services to our investee companies and the activities to identify additional technologies and companies, in which we might invest, as well as legal defense costs and costs associated with SEC reporting. We do not generate any direct revenue and because our investee companies are not consolidated, we do not report revenue from investee businesses.

GENERAL AND ADMINISTRATIVE EXPENSE

During the three and nine months ended September 30, 2006, general and administrative ('G&A") expenses were \$14,426 and \$136,986, respectively, compared to G&A expenses of \$19,154 and \$123,940 for the three and nine months ended September 30, 2005. The \$4,728, or 25%, decrease in G&A expense for third quarter 2006 compared to third quarter 2005 is primarily due to a decline in professional fees in the third quarter of 2006. The \$13,046, or 11%, increase in G&A expense for the nine months ended September 30, 2006 compared to the same period in 2005 is primarily due to higher investor relations fees and higher legal fees in the nine months ended September 30, 2006.

LITIGATION ACCRUAL

On August 27, 2001 JMA refiled its lawsuit with a federal court in New York, and the Company filed its motion to dismiss the case because the plaintiffs lacked the required diversity jurisdiction to pursue the claims in federal court. On October 31, 2001 the case was dismissed in federal court. In December 2001, the plaintiffs refiled the lawsuit in the state court seeking to enforce the proposed settlement term sheet. The case was filed in Supreme Court of New York, that state's trial court, in a case styled Roan Meyers v. CT Holdings. CT Holdings filed counterclaims for breach of the term sheet as well as breach of the placement agency agreement. Cross motions for partial summary judgments have been argued but the court entered judgment in favor of Roan-Meyers in the amount of \$3,000,000 and granted interest at the rate of 9% from October 31, 2000 through the date of final judgment, and thereafter at the statutory rate allowed by law.

On August 23, 2006, CT Holdings and certain other parties entered into a Release and Settlement Agreement ("Agreement") by and among Meyers and their related parties (collectively, the "Meyers Released Parties") on the one hand and defendants CT Holdings Enterprises, Citadel Security Software Inc., Steven B. Solomon, Chris A. Economou, Lawrence Lacerte, Mark Rogers, Phillip J. Romano, Axel Sawallich, George Sharp and Gilbert Gertner (collectively "Defendants") on the other hand. The Agreement provides for the settlement of litigation filed by Meyers Associates against defendants Citadel, CT Holdings Enterprises, certain of Citadel's current and former directors and officers Steven B. Solomon, Chris E. Economou, Lawrence Lacerte, Mark Rodgers, Phillip J. Romano and Axel Sawallich in the Court of Chancery of the State of Delaware in and for New Castle County (the "Delaware Action") asserting various claims, and other litigation against CT Holdings and its former officers and directors (the "Actions").

Pursuant to the Agreement, Citadel Security Software shall pay the sum of \$1,250,000 to Meyers Associates in two payments, the first payment of \$250,000

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

upon signing of the Agreement the second payment of \$1,000,000 no later than November 1, 2006. The Defendants will be released by the Plaintiffs from all claims in the actions 91 days after receipt of the payments, subject to the terms and conditions of the agreement. The first payment of \$250,000 was made by Citadel in August 2006. If Citadel fails to make the second payment of \$1,000,000 the defendants are not entitled to offset or reduce the settlement by the initial payment of \$250,000. Accordingly, the Company reduced its liability for this legal claim to \$1,250,000 at September 30, 2006. The second payment of \$1,000,000 was made by Citadel on November 1, 2006 therefore pursuant to the Agreement, the Company is expected to be released from any further claims under this lawsuit.

DEBT SETTLEMENT GAIN

On May 22, 2006 the Company and CII, an affiliate of the Company's CEO, entered into a settlement, pursuant to which CII agreed to release the Company from indebtedness and accrued interest under the Amended Note of \$271,148 plus accrued interest of \$9,211 through May 22, 2006, in exchange for the delivery to CII of the shares of Parago and River Logic owned by the Company. The carrying value of these shares was zero at the settlement date as the investments had been written off in prior periods due to continuing operating losses, lack of cash flows generated from the investments and other factors. As a result, in the second quarter of 2006, the Company recorded a \$280,359 gain on debt settlement.

INTEREST EXPENSE

Interest expense for the three and nine months ended September 30, 2006 was \$48,760 and \$460,102, respectively representing interest expense on litigation accrual, advances and notes payable to officers and shareholders, the demand note payable to Citadel and the convertible note payable to CITN Investment Inc. ("CII"). Interest expense of \$41,311 and \$179,262 related to the judgment entered by the court for JMA in June 2004 was recorded in the three and nine months ended September 30, 2006, respectively. Interest expense also includes amortization of the beneficial conversion feature associated with the CII note and amended note settled in May 2006. Amortization of the beneficial conversion feature was \$250,290 for the nine months ended September 30, 2006. The remaining interest expense is associated with the advances and the notes payable and was \$7,449 and \$30,550 in the three and nine months ended September 30, 2006, respectively.

Interest expense for the three and nine months ended September 30, 2005 was \$106,695 and \$317,751, respectively, representing interest expense on litigation accrual, advances and notes payable to officers and shareholders, the demand note payable to Citadel and the convertible note payable to CII. Interest expense of \$70,082 and \$208,033 related to the judgment entered by the court for JMA in June 2004 was recorded in the three and nine months ended September 30, 2005, respectively. Interest expense also includes amortization of the beneficial conversion feature associated with the CII note and amended note which totaled \$25,000 and \$75,000 for the three and nine months ended September 30, 2005, respectively. The remaining interest expense is associated with the advances and the notes payable and was \$11,613 and \$34,718 in the three and nine months ended September 30, 2005, respectively.

LIQUIDITY AND CAPITAL RESOURCES

We received a report from our independent registered public accounting firm for our year ended December 31, 2005 containing an explanatory paragraph that describes the uncertainty regarding our ability to continue as a going concern due to our recurring operating losses and our significant working capital deficiency. Historically, we have incurred recurring operating losses and have a significant stockholders' deficit at September 30, 2006 of approximately \$3

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

million. We had a cash balance of \$197 at September 30, 2006 and current liabilities total approximately \$3 million. We have limited access to capital, no plans to raise capital and we have not identified sources of capital at September 30, 2006. Our past funding needs of the business have been provided by financings through short-term notes payable and additional investments from related parties, including our CEO, and CII however there can be no assurance that such funds will be available from these related parties in the future. The Company has been and continues to be dependent upon outside financing to perform its business development activities, make investments in new technology companies and to fund operations.

18

Our plans to continue to support and expand our business development activities are limited due to a lack of identification and availability of near term capital. As a result, it is unlikely that the implementation of the Company's business strategy will generate positive cash flow in the foreseeable future. We have no plans at September 30, 2006 to raise additional capital to invest in new business opportunities. To do so we estimate that we will need to raise up to \$3 million to settle recorded liabilities at September 30, 2006 after which we may then need to raise additional funds to support our incubator and business development activities. However there can be no assurance that we will raise additional funds needed to settle our liabilities.

There can be no assurance that management's plans will be successful or what other actions may become necessary. There can be no assurance that the Company will ever achieve liquidity for its investments. Until we are able to create liquidity from an additional inflow of new capital, we will continue to require external sources of working capital to fund our operating expenses. Our inability to raise capital could have a material adverse effect on our business and operations that could be material to our results of operations.

Cash Used in Operating Activities

Net cash used in operating activities was \$0 for the nine months ended September 30, 2006 resulting from net income of \$3,017,123 offset by the non-cash net impact of the reversal of the Company's litigation accrual of \$3,154,590 (\$3,333,852 reversal of the litigation accrual net of \$179,262 current year interest) and by a \$280,359 gain related to the settlement of the Amended Note with CII. Cash used in operating activities also included the non-cash amortization of deferred debt discount of \$250,290 recorded as interest expense and a change in operating liabilities of \$167,536.

For the nine months ended September 30, 2005 the net cash used in operating activities was \$14,971. This is the result of a net loss of \$441,691 for the nine months ended September 30, 2005 and non-cash adjustments for the amortization of debt discount of \$75,000 recorded as interest expense and an accrual for interest related to litigation of \$208,770 and an increase in operating liabilities of \$142,950.

Cash Used by Financing Activities

Net cash provided by financing activities for the nine months ended September 30, 2005 was \$11,000 representing proceeds from an interest free demand note from the CEO of the Company for payment of audit fees.

CONTRACTUAL OBLIGATIONS

At September 30, 2006 we have a demand note payable to Citadel of \$225,000 plus accrued interest of \$97,644, and a \$9,000 unsecured note payable plus accrued interest of \$7,379 to a shareholder which is in default at September 30, 2006.

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

There are no other long-term debt obligations, capital lease obligations, operating lease obligations or long-term capital purchase commitments. However at September 30, 2006 we have accrued for payments to Citadel under the transition services agreement and demand note payable, none of which may be paid until such time as the Company has sufficient cash to pay these obligations. The asset purchase agreement that Citadel has entered into contemplates, that we will enter into a release agreement with Citadel, pursuant to which we would be released from the amount we owe to Citadel (approximately \$1 million dollars).

ITEM 3. CONTROLS AND PROCEDURES

The Company's management, including the Company's principal executive officer and principal financial officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13(a) - 15(e) and 15(d) - 15(e) under the Securities Exchange Act of 1934) as of the nine months ended September 30, 2006, the period covered by the Form 10-QSB. Based upon that evaluation, the Company's principal executive officer and principal financial officer have concluded that the disclosure controls and procedures were effective as of September 30, 2006 to provide reasonable assurance that material information relating to the Company is made known to management including the CEO and CFO.

19

There were no changes in the Company's internal control over financial reporting that occurred during the Company's last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

INHERENT LIMITATION ON THE EFFECTIVENESS OF INTERNAL CONTROLS

The effectiveness of any system of internal control over financial reporting, including CT Holdings', is subject to inherent limitations, including the exercise of judgment in designing, implementing, operating, and evaluating the controls and procedures, and the inability to eliminate misconduct completely. Accordingly, any system of internal control over financial reporting, including CT Holdings', can only provide reasonable, not absolute assurances. In addition, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. We intend to continue to monitor and upgrade our internal controls as necessary or appropriate for our business, but cannot assure you that such improvements will be sufficient to provide us with effective internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Set forth below are litigation matters to which we are a party. We believe that we have meritorious defenses and will vigorously defend ourselves. However, an unfavorable resolution of, settlement, or defense costs related to one or more of these lawsuits could have a material adverse effect on our business, results of operations or financial condition.

In August 1998, Janssen-Meyers Associates L.P. ("JMA") filed a lawsuit against the Company arising out of an alleged 1995 contract with the Company's predecessor ("Old Citadel"). The suit alleged that Old Citadel breached a letter of intent dated September 1995 and/or a Placement Agency Agreement dated November 1995 between JMA and Old Citadel. As its damages, JMA claimed that it was entitled to, among other things, the cash value of warrants to purchase 1.8

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

million shares of CT Holdings common stock at an exercise price of \$0.89 per share, valued during May 1996. According to JMA's valuation of those warrants, potential damages were alleged to exceed \$40 million. The Company vigorously disputes that it breached either the letter of intent or the Placement Agency Agreement or that it is liable to JMA. The lawsuit was styled Janssen-Meyers Associates, L.P. v. Citadel Technology, Inc., and was filed in the Supreme Court of the State of New York, County of New York. The Company removed the case to federal court in the Southern District of New York.

Following mediation in July 2000, the Company entered into a settlement term sheet, to attempt to resolve the disputes between it and JMA, pursuant to which the Company and JMA agreed in principle to settle the lawsuit for an aggregate of \$3 million, in a combination of \$1.5 million in cash and 300,000 shares of the Company's common stock with a guaranteed value of \$5 per share as of January, April and October 2001 (with respect to 100,000 of the shares for each period). The settlement was subject to execution of definitive settlement documents and approval of the boards of directors of both parties. However, the Company and JMA were unable to negotiate the final definitive settlement agreement. The case was dismissed in August 2000 without any resolution of this issue. On March 27, 2001, JMA attempted to reopen this matter, but the Court hearing the JMA lawsuit issued a Summary Order denying JMA's motion to enforce the settlement term sheet and confirmed the prior dismissal of the lawsuit. The Court further ruled that JMA would either have to bring an action on the proposed settlement or move to re-open the dismissed case. The Court stated that it did not express any view with respect to the merits of the settlement that brought about the dismissal of the case. There was no activity on the case from March 2001 through August 2001. On August 27, 2001 JMA refiled its lawsuit with a federal court in New York, and the Company filed its motion to dismiss the case because the plaintiffs lacked the required diversity jurisdiction to pursue the claims in federal court. On October 31,

20

2001 the case was dismissed in federal court. In December 2001, the plaintiffs refiled the lawsuit in the state court seeking to enforce the proposed settlement term sheet. The case was filed in Supreme Court of New York, that state's trial court, in a case styled Roan Meyers v. CT Holdings. CT Holdings has filed counterclaims for breach of the term sheet as well as breach of the placement agency agreement. Cross motions for partial summary judgments have been argued but on June 9, 2004 the court entered judgment in favor of Roan-Meyers in the amount of \$3,000,000 and granted interest at the rate of 9% from October 31, 2000 through the date of final judgment, and thereafter at the statutory rate allowed by law. The \$3,000,000 judgment as well as the interest from October 2000 through September 30, 2006 of \$1,612,623 has been accrued. The Company has appealed the final judgment, and the appellate court affirmed the trial court's decision. The Company intends to vigorously defend this case.

On April 8, 2005, Meyers Associates, L.P. f/k/a Roan/Meyers Associates, L.P. and f/k/a Janssen-Meyers Associates, L.P. ("Meyers") filed a lawsuit in the Court of Chancery of the State of Delaware, in New Castle County, against the Company, Citadel Security Software, Inc. (Citadel) including Steven B. Solomon, the Chief Executive and a Director of the Company, Chris A. Economou, a Director of the Company, Lawrence Lacerte, a former Director of the Company, and Phillip J. Romano, a former Director of the Company (the "Individual Defendants"). The suit alleges that in connection with an action filed in the Supreme Court of New York, New York County, to enforce a Settlement Term Sheet executed on July 7, 2000 by Meyers and CT Holdings, Meyers was awarded a judgment against CT Holdings in the amount of \$3 million plus interest on the judgment at the rate of 9% from October 31, 2000 until the date of entry of that judgment and thereafter at the statutory rate (the "Judgment"). The suit alleges that CT Holdings' May 2002 spin-off of its interests in Citadel to CT Holdings'

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

shareholders rendered CT Holdings insolvent and constituted a fraudulent conveyance to defraud CT Holdings' creditors, including Meyers. The suit asserts fraudulent conveyance claims against Citadel and CT Holdings pursuant to Delaware statutory and common law. The suit also asserts a claim against Citadel for successor liability as the alleged successor in interest or alter ego of CT Holdings. The suit alleges that the Individual Defendants who were officers and/or directors of CT Holdings at the time of the spin-off breached fiduciary duties allegedly owed to creditors of CT Holdings, including Meyers, by approving and allowing the spin-off transaction. The suit seeks to void the spin-off transaction or alternatively to hold Citadel liable for the Judgment including interest, to recover damages against the Individual Defendants in an amount not less than the Judgment including interest, plus an unspecified amount of punitive, consequential and incidental damages, as well as attorneys' fees and costs.

On August 23, 2006, CT Holdings and certain other parties entered into a Release and Settlement Agreement ("Agreement") by and among Meyers and their related parties (collectively, the "Meyers Released Parties") on the one hand and defendants CT Holdings Enterprises, Citadel Security Software Inc., Steven B. Solomon, Chris A. Economou, Lawrence Lacerte, Mark Rogers, Phillip J. Romano, Axel Sawallich, George Sharp and Gilbert Gertner (collectively "Defendants") on the other hand. The Agreement provides for the settlement of litigation filed by Meyers Associates against defendants Citadel, CT Holdings Enterprises, certain of Citadel's current and former directors and officers Steven B. Solomon, Chris E. Economou, Lawrence Lacerte, Mark Rodgers, Phillip J. Romano and Axel Sawallich in the Court of Chancery of the State of Delaware in and for New Castle County (the "Delaware Action") asserting various claims, and other litigation against CT Holdings and its former officers and directors (the "Actions"). Pursuant to the Agreement, Citadel Security Software shall pay the sum of \$1,250,000 to Meyers Associates in two payments, the first payment of \$250,000 upon signing of the Agreement the second payment of \$1,000,000 no later than November 1, 2006. The Defendants will be released by the Plaintiffs from all claims in the actions 91 days after receipt of the payments, subject to the terms and conditions of the agreement. The first payment of \$250,000 was made by Citadel in August 2006. If Citadel fails to make the second payment of \$1,000,000 the defendants are not entitled to offset or reduce the settlement by the initial payment of \$250,000. Accordingly, the Company reduced its liability for this legal claim to \$1,250,000 at September 30, 2006. The second payment of \$1,000,000 was made by Citadel on November 1, 2006 therefore pursuant to the Agreement, the Company is expected to be released from any further claims under this lawsuit.

The Company may become involved from time to time in litigation on various matters which are routine to the conduct of our business. The Company believes that none of these actions, individually or in the aggregate, will have a material adverse effect on our financial position or results of operations, though any adverse decision in these cases or the costs of defending or settling such claims could have a material adverse effect on our business.

21

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

At September 30, 2006 and December 31, 2005, the Company was in default on the following indebtedness:

- \$9,000, an 8% note payable to shareholder. The note continues to bear interest at 8% with accrued interest at September 30, 2006 of \$7,379.

ITEM 6. EXHIBITS

Edgar Filing: CT HOLDINGS ENTERPRISES INC - Form 10QSB

EXHIBIT NUMBER	DESCRIPTION
31.1	Certification of Principal Executive Officer, filed herewith.
31.2	Certification of Principal Financial Officer, filed herewith.
32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, filed herewith.

22

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Quarterly Report on Form 10-QSB to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: November 17, 2006

CT HOLDINGS ENTERPRISES, INC.

By:/s/ STEVEN B. SOLOMON

Steven B. Solomon, President and Chief
Executive Officer (Duly Authorized
Signatory and Principal Executive
Officer)

By:/s/ RICHARD CONNELLY

Richard Connelly, Chief Financial
Officer (Duly Authorized Signatory and
Principal Accounting and Financial
Officer)

23