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SOFTECH INC  
Form 10KSB  
August 29, 2007

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

Form 10-KSB

ANNUAL REPORT  
PURSUANT TO SECTION 13 or 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended May 31, 2007

Commission file number 0-10665

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

|   |  |
|---|--|
| Massachusetts<br>-----<br>(State or other jurisdiction of<br>Incorporation or organization) | 04-2453033<br>-----<br>(IRS Employer<br>Identification Number) |
|---|--|

|   |                              |
|---|------------------------------|
| 2 Highwood Drive, Tewksbury, Massachusetts<br>-----<br>(Address of principal executive offices) | 01876<br>-----<br>(Zip Code) |
|---|------------------------------|

Registrant's telephone number, including area code: (978) 640-6222

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

Securities registered pursuant to Section 12(g) of the Act:  
Common Stock, \$.10 par value  
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(Title of Class)

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  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part II of this Form 10-KSB or any amendment to this Form 10-KSB.

State the aggregate market value of the voting stock held by non-affiliates of the registrant: \$641,226 as of August 17, 2007. On August 17, 2007 the registrant had outstanding 12,213,236 shares of common stock of \$.10 par value, which is the registrant's only class of common stock.

PART I

## Edgar Filing: SOFTECH INC - Form 10KSB

### ITEM 1 - DESCRIPTION OF BUSINESS

#### THE COMPANY

SofTech, Inc. was formed in Massachusetts on June 10, 1969. The Company had an initial public offering in August 1981 and a subsequent offering in December 1982. From inception until the disposition of the Government Systems Division in December 1993, the Company's primary business was that of custom software development for the U.S. Government, primarily the Department of Defense.

After the sale of the Company's Government Systems Division through the end of calendar year 1996, the Company's only business was reselling hardware and software products of third parties and offering services related to such products (the "Reseller Model"). Between December 1996 and December 2002, the Company acquired eight entities involved in developing, supporting and/or marketing software products and/or services to the Computer Aided Design and Manufacturing ("CAD/CAM") and Product Data Management ("PDM") marketplace. The three most significant acquisitions during that time period were the purchases of Workgroup Technology Corporation ("WTC") in December 2002, Adra Systems, Inc. in May 1998, and the Advanced Manufacturing Technology ("AMT") in November 1997. The aggressive acquisition strategy that was funded primarily through debt, substantially increased the Company's risk profile but was required in order to create a viable and sustainable business.

#### PRODUCTS AND SERVICES

The Company operates in one reportable segment and is engaged in the development, marketing, distribution and support of computer software solutions that serve the Product Lifecycle Management ("PLM") industry. These solutions include software technology offerings for Computer Aided Design ("CAD"), Computer Aided Manufacturing ("CAM") as well as Product Data Management ("PDM") and Collaboration technologies, all of which fit under the broadly defined PLM industry. The Company's operations are organized geographically with U.S. and European sales and customer support 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 outlined in Note G to the financial statements.

A description of the Company's primary product offerings is as follows:

Cadra(TM) is a drafting and design technology for the professional mechanical engineer. The CADRA family of CAD/CAM products includes CADRA Design Drafting, a fast and highly productive mechanical design documentation tool; CADRA NC, a comprehensive 2 through 5 axis NC programming application; and CADRAWorks, an integration with SolidWorks providing for an integrated drawing production system and 3D solid modeler. The CADRA family is rounded out by an extensive collection of translators and software options that make it a seamless fit into today's multi-platform and multi-application organizations.

ProductCenter(TM) is a proven enterprise-wide, collaborative PLM solution delivering a unique and powerful combination of document management, design integration, configuration control, change management, bill of materials management and

integration capability with other enterprise-wide systems, which helps companies rapidly optimize the product development process. ProductCenter provides for the secure management of product information and allows engineers and the entire design chain to manage, share, modify and track product data and documents

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throughout the product development lifecycle. ProductCenter supports engineering change management and bill of materials management for automating business processes. ProductCenter's web-based collaboration capabilities allow employees, customers, suppliers, and other globally dispersed team members to securely exchange product information while maintaining a centralized database of critical product data. ProductCenter also enables integration with other business applications, such as ERP, SCM, or CRM, for continuous data exchange across the product lifecycle.

The ProductCenter family of products is a suite of modules that, when combined, offer a unified collaborative product data management software solution. ProductCenter modules may be deployed in various combinations to meet the specific needs of a customer.

The AMT group has three primary products. Prospector(TM) is a knowledge-based NC programming package for complex tool production. This Windows based, easy-to-use package gives full flexibility for generating and editing NC toolpaths while utilizing the power of the industry's best knowledge base of tools, speeds, feeds, and cutting paths. ToolDesigner(TM) is a software package for developing and designing complex molds and dies. Core and cavity splits, parting line placement, wireframe design and drafting, photorealistic rendering, surface modeling, trimmed surfaces, injection and cooling line placement are aptly handled with this professional package. ExpertCAD(TM) is a drafting technology designed specifically for the Tool & Die industry.

The Company markets and distributes its products and services primarily through a direct sales force and through its service organization in North America and Europe. The majority of the Company's sales in Asia are in Japan. The Company markets and distributes its products and services in Japan primarily through authorized resellers. The Company has signed resellers in Europe to reach areas not covered by its direct sales presence and supplement its existing sales force, however, to date, the revenue generated from this indirect distribution has not been material.

### COMPETITION

The Company competes against much larger entities in an extremely competitive market for all of its software and service offerings. The 2D software technologies acquired in the acquisitions in fiscal 1998 compete directly with the offerings of such companies as AutoDesk and UGS. This 2D technology is also marketed as a complementary offering to many 3D products offered by companies such as Parametric Technology Corporation, Dassault, UGS, AutoDesk and SolidWorks that all possess some level of 2D drafting capability. These companies all have financial resources far in excess of those of the Company.

The Company's PLM and collaborative technology offerings compete against offerings of the companies listed in the paragraph above and against other companies that have focused on PLM and collaborative offerings as well.

The Company's CAM technology, Prospector, is marketed to the Plastic Injection Mold and Tool & Die industries. The large CAD companies such as Parametric Technology Corporation, Dassault, UGS, and AutoDesk have modules that compete in this market.

The service offerings of the Company which include consulting, training and discreet engineering services compete with offerings by all of the large CAD companies noted above, small regional engineering services companies and the in-house capabilities of its customers.

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### PERSONNEL

As of August 17, 2007, the Company employed 51 persons, 48 on a full time basis and 3 part time. These employees were distributed over functional lines as follows: Sales = 10; Product Development Engineers = 14; Engineers = 20; General and Administrative = 7.

The ability of the Company to attract qualified individuals with the necessary skills is currently, and is expected to continue to be, a constraint on future growth.

### BACKLOG

Product backlog as of May 31, 2007 and 2006 was insignificant. Deferred revenue, which represents primarily software maintenance services to be performed during the following year, totaled approximately \$3,568,000 and \$3,423,000 at May 31, 2007 and 2006, respectively. In addition, as of May 31, 2007 the Company had a backlog of consulting orders totaling approximately \$.3 million, a decrease from the \$.6 million at May 31, 2006. Given the short time period between receipt of order and delivery of product revenue, on average less than 30 days, the Company does not believe that product revenue backlog is an important measure as to the relative health of the business.

### RESEARCH AND DEVELOPMENT

The Company has approximately 14 product development engineers in its research and development groups located in Michigan and Massachusetts. In fiscal 2007 and 2006 the Company incurred research and development expense of \$2.2 million and \$2.8 million, respectively, related to the continued development of technology. The Company also uses third-party offshore engineering companies to perform some product development as well as quality assurance testing of its technology developed in the United States.

### CUSTOMERS

No single customer accounted for more than 10% of the Company's revenue in fiscal 2007 or 2006. The Company is not dependent on a single customer, or a few customers, the loss of which would have a material adverse effect on the business.

### SEASONALITY

The first quarter, which begins June 1 and ends August 31, has historically been the slowest quarter of the Company's fiscal year. Management believes this weakness is due primarily to the buying habits of the customers and the fact that the quarter falls during prime vacation periods.

### ITEM 2 - DESCRIPTION OF PROPERTY

The Company leases office space in Troy, Michigan; Tewksbury, Massachusetts; Munich, Germany, Grenoble, France and Milan, Italy. The liability related to office space in Burlington, Massachusetts (which lease expired in December 2002) was assumed by our lessor for our headquarters in Tewksbury, Massachusetts as a concession for extending our lease term at our headquarters. Such concession is being amortized as a reduction of rent expense over the extended term of the lease. The Company believes that the current office space is adequate for current and anticipated levels of business activity.

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### ITEM 3 - LEGAL PROCEEDINGS

The Company, from time to time, is a party to various legal proceedings and claims that arise in the ordinary course of business. At May 31, 2007 there are no material outstanding claims and therefore no amounts have been accrued.

### ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

## PART II

### ITEM 5 - MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's common stock are traded on the NASDAQ's Over-the-Counter Exchange under the symbol "SOFT.OB".

At May 31, 2007, there were approximately 236 holders of record of the Company's common stock. The table below sets forth quarterly high and low close prices of the common stock for the indicated fiscal periods as provided by the National Quotation Bureau. These quotations reflect inter-dealer prices without retail mark-up, markdown, or commission and may not necessarily represent actual transactions.

|                | 2007 |     | 2006 |     |
|----------------|------|-----|------|-----|
|                | High | Low | High | Low |
| First Quarter  | .20  | .13 | .41  | .23 |
| Second Quarter | .20  | .09 | .30  | .18 |
| Third Quarter  | .13  | .08 | .29  | .16 |
| Fourth Quarter | .11  | .09 | .29  | .17 |

The Company has not paid any cash dividends since 1997 and it does not anticipate paying cash dividends in the foreseeable future.

The table below details information regarding equity compensation plans of the Company as of May 31, 2007:

| Plan category               | Number of shares<br>to be issued upon<br>exercise of<br>outstanding options,<br>warrants and rights | Weighted average<br>exercise price<br>of outstanding options,<br>warrants and rights | Number of shares<br>securities<br>available for<br>future issuances |
|-----------------------------|---|--|---|
| Approved by<br>Shareholders | 238,000   | \$.43  | --  |

### ITEM 6 - MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

This Form 10-KSB contains forward-looking statements. The words "believe", "expect," "anticipate," "intend," "estimate," and other expressions which are predictions of, or indicate future events and trends and which do not relate to historical matters identify forward-looking statements. These financial statements include statements regarding the Company's intent, belief or current

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expectations. You are cautioned that any forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties that may cause the Company's actual results to differ materially from the results discussed in the forward-looking statements. Among the factors that could cause actual results to differ materially from those indicated by such forward-looking statements include, but are not limited to, market acceptance of the Company's technologies, fluctuations in quarterly results, continued integration and market expansion of our acquired technologies and the ability of the Company to attract and retain qualified personnel both in our existing markets and in new office locations.

### DESCRIPTION OF THE BUSINESS

SofTech, Inc. was formed in Massachusetts on June 10, 1969. The Company had an initial public offering in August 1981 and a subsequent offering in December 1982. From inception until the disposition of the Government Systems Division in December 1993, the Company's primary business was that of custom software development for the U.S. Government, primarily the Department of Defense.

After the sale of the Company's Government Systems Division through the end of calendar year 1996, the Company's only business was reselling hardware and software products of third parties and offering services related to such products (the "Reseller Model"). Between December 1996 and May 1999, the Company acquired seven entities involved in developing, supporting and/or marketing software products and/or services to the Computer Aided Design and Manufacturing ("CAD/CAM") marketplace. The two most significant acquisitions during that time period were the purchases of Adra Systems, Inc. in May 1998 and the Advanced Manufacturing Technology ("AMT") in November 1997. In December 2002 the Company acquired Workgroup Technology Corporation (WTC) thereby obtaining complementary technology. The acquisition of WTC is expected to be a key element in the Company's growth strategy. The aggressive acquisition strategy that was funded primarily through debt, substantially increased the Company's risk profile but was required in order to create a viable and sustainable business.

### INCOME STATEMENT ANALYSIS

The table below presents the relationship, expressed as a percentage, between income and expense items and total revenue, for each of the two years ended May 31, 2007. In addition, the change in those items, again expressed as a percentage, for each of the two years ended May 31, 2007 is presented.

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|               | Items as a percentage<br>of revenue |       | Percentage change<br>year to year |
|---------------|-------------------------------------|-------|-----------------------------------|
|               | 2007                                | 2006  | 2006 to 2007                      |
| Revenue       |                                     |       |                                   |
| Products      | 23.6%                               | 27.5% | (24.2)%                           |
| Services      | 76.4                                | 72.5  | (6.6)                             |
|               | -----                               | ----- |                                   |
| Total revenue | 100.0                               | 100.0 | (11.5)                            |
| Cost of sales |                                     |       |                                   |
| Products      | 13.6                                | 16.7  | (27.6)                            |
| Services      | 14.6                                | 12.7  | 1.8                               |
|               | -----                               | ----- |                                   |

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|                          |        |        |        |
|--------------------------|--------|--------|--------|
| Total cost of sales      | 28.2   | 29.4   | (14.9) |
|                          | -----  | -----  |        |
| Total gross margin       | 71.8   | 70.6   | (10.0) |
| Research and development | 19.6   | 22.6   | (23.2) |
| S.G.& A.                 | 50.0   | 49.0   | (9.6)  |
| Interest expense         | 13.1   | 9.7    | 20.1   |
|                          | -----  | -----  |        |
| Loss before income tax   | (11.0) | (10.6) | (8.4)  |
|                          | =====  | =====  | =====  |

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 are 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. Revenue from engineering, consulting and training services is recognized as those services are rendered.

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.

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### Valuation of Long-Lived and Intangible Assets

The Company periodically reviews the carrying value of all intangible (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 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.

As of May 31, 2007, 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.

### 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

Total revenue for fiscal year 2007 was \$11.0 million, a decrease of \$1.5 million or 11% from fiscal year 2006 revenue of \$12.5 million. The revenue by product line for fiscal 2007 as compared to fiscal 2006 is as follows (in thousands, except percent):

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| PRODUCT LINE  | FY 2007  | FY 2006  | \$ CHANGE | % CHANGE |
|---------------|----------|----------|-----------|----------|
|               | -----    | -----    | -----     | -----    |
| ProductCenter | \$ 5,642 | \$ 6,523 | \$ (881)  | (13.5%)  |
| Cadra         | 4,514    | 4,651    | (137)     | (3.0)    |
| AMT           | 893      | 1,304    | (411)     | (31.5)   |
|               | -----    | -----    | -----     | -----    |
| Total         | 11,049   | 12,478   | (1,429)   | (11.5)   |

Product revenue decreased \$.8 million or 24% during the current year as compared to the prior year. The change from year to year in product revenue among our three product lines was as follows (in thousands, except percent):



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| PRODUCT LINE  | FY 2007  | FY 2006  | \$ CHANGE | % CHANGE |
|---------------|----------|----------|-----------|----------|
|               | -----    | -----    | -----     | -----    |
| ProductCenter | \$ 1,010 | \$ 1,876 | \$ (866)  | (46.2)%  |
| Cadra         | 1,390    | 1,086    | 304       | 28.0%    |
| AMT           | 202      | 470      | (268)     | (57.0)   |
|               | -----    | -----    | -----     | -----    |
| Total         | 2,602    | 3,432    | (830)     | (24.2)   |

The decrease in product revenue for our ProductCenter technology was primarily attributed to delays of customer orders during Fiscal Year 2007. While some of the opportunities that were expected to close in FY2007 continue to be pursued in FY2008, we cannot determine if the delays and customer decisions to not move forward with their PLM initiatives will continue into FY2008. The increase in Cadra revenue was mainly attributed to certain customers in the U.S. and Asia taking advantage of company upgrade incentives and/or upgrading their hardware which required the latest versions of our Cadra product. The decrease in AMT revenue was attributed to the distressed economic climate of the Tool and Die industry.

Service revenue decreased about \$.6 million or 6.6% from fiscal 2006 to 2007. The change from year to year in service revenue among our three product lines was as follows (in thousands, except percent):

| PRODUCT LINE  | FY 2007  | FY 2006  | \$ CHANGE | % CHANGE |
|---------------|----------|----------|-----------|----------|
|               | -----    | -----    | -----     | -----    |
| ProductCenter | \$ 4,632 | \$ 4,647 | \$ (15)   | (.3%)    |
| Cadra         | 3,124    | 3,565    | (441)     | (12.4)   |
| AMT           | 691      | 834      | (143)     | (17.1)   |
|               | -----    | -----    | -----     | -----    |
| Total         | 8,447    | 9,046    | (599)     | (6.6)    |

The .3% decrease in ProductCenter service revenue was attributed to our decreased license revenue. ProductCenter maintenance revenue increased by 1% in 2007 and Consulting revenue decreased by 3% due to a reduced number of new customer installations in fiscal year 2007.

Consulting/training is a very minor component of our Cadra and AMT product lines.

The 12.4% decline in service revenue for our Cadra product line was due to the continued migration of the CAD marketplace from 2D CAD tools such as Cadra to 3D technologies. This migration has been going on for some time and is expected to continue. With the continued market acceptance of 3D technologies, our customers are reducing their utilization of Cadra and reducing their maintenance coverage or opting not to renew at all. For 2007 we experienced double digit decreases in maintenance revenue across all geographies with the exception of Germany which decreased 7%.

The 17.1% decline in service revenue for our AMT product line was part of the continued downward trend over the last five years for this technology. AMT's customers are primarily North American vendors to the major parts suppliers to the

American automotive industry. Our customers have experienced severe financial difficulty as the North American automotive industry has struggled with foreign competition, loss of market share, increasing costs and a myriad of other problems. These events have had a substantial detrimental impact on the revenue generated from this product line.

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Product gross margin was 42.1% in fiscal 2007 as compared to 39.4% in fiscal 2006. This increase in product gross margin is the result of lower amortization in fiscal 2007 as the intangible costs related to our purchase of the ProductCenter technology were fully amortized. Product revenue decreased by 24% and cash expenses decreased by 9% in fiscal 2007 as compared to fiscal 2006.

Service gross margin was 80.9% in fiscal 2007 as compared to 82.5% in fiscal 2006. This decrease in service gross margin is a result of lower maintenance revenue in our Cadra and AMT productlines.

Research and Development expenditures totaled approximately \$2.2 million in fiscal 2007 as compared to \$2.8 million in fiscal 2006, a decrease of about 23%. These development expenditures were 19.6% of revenue in fiscal 2007 as compared to 22.6% in fiscal 2006. This decrease in total R&D expenditures was a result of the reduced headcount and salaries in order to keep expenses in line with our current revenue trends.

Selling and General and Administrative expenses for fiscal 2007 decreased by about \$.6 million or about 9.6% from fiscal 2006. This decrease in expenses was a result of reduced headcount in order to keep expenses in line with our current revenue trends.

Interest expense in fiscal 2007 increased by approximately \$242,000 or 20.5% from fiscal 2006. This was the direct result of continuous increases in the prime rate throughout the year. In fiscal 2007, our average outstanding debt was \$13.9 million as compared to about \$13.4 million in 2006, an increase of about 3.7%. The average interest rate for the current year on those borrowings was 10.5% as compared to about 9.0% in fiscal 2006, an increase of 16.7%.

The net loss for fiscal 2007 was about \$(1.2) million as compared to approximately \$(1.3) million in fiscal 2006. The net loss per share for fiscal 2007 was \$(.10) as compared to \$(.11) in fiscal 2006. The weighted average number of shares outstanding was 12.2 million in fiscal 2007 and 2006.

### CAPITAL RESOURCES AND LIQUIDITY

The Company's cash position as of May 31, 2007 was \$1,048,000. This represents an increase of \$368,000 from the fiscal 2006 year-end balance of \$680,000.

Included in the Company's results of operations are significant non-cash expenses related to amortization of intangibles resulting from prior year acquisitions, which totaled approximately \$1.4 million in fiscal 2007 and \$1.9 million in fiscal 2006.

For fiscal 2007, operating activities generated \$313,000, investing activities used about \$12,000 and financing activities provided about \$112,000.

The Company's cash flow from operating activities in fiscal 2007 increased from 2006. The net loss together with non-cash expenses related to amortization of

intangibles and depreciation generated cash of approximately \$247,000; an increase in deferred revenue generated cash of \$145,000; and all other changes had a net cash usage of \$79,000. The increase in deferred revenue is the result of maintenance contracts being renewed in a more timely manner.

Investing activities utilized cash of \$12,000 during fiscal 2007 related to normal capital expenditures. Lastly, during fiscal 2007 the Company utilized its

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credit facility to fund operations by borrowing \$122,000 in excess of repayments.

At May 31, 2007, long-term obligations related exclusively to our outstanding debt totaled approximately \$13.1 million. The Company is dependent on availability under its debt facilities and its cash flow from operations to meet its near term working capital needs and to make debt service payments. The monthly principal and interest payments are approximately \$212,000 on these borrowings.

The Company currently funds its operations through a combination of cash flow from operations and its debt facilities with Greenleaf Capital. In fiscal 2007, the Company generated \$313,000 from operations and it is management's intention to manage the business in order to achieve positive cash flows from operations in fiscal 2008. The Company has a \$3.0 million Line of Credit through Greenleaf Capital which expires annually in June. As of May 31, 2007, approximately \$579,000 was available under this facility which has been extended an additional year through June 2008. (See Note G to the Consolidated Financial Statements.)

The Company currently believes that cash flow from operations together with the availability of capital under its line of credit is sufficient to meet its obligations for at least the next year.

### MARKET RISK DISCLOSURE

The Company has assets and liabilities outside the United States that are subject to fluctuations in foreign currency exchange rates. The Company's primary exposure is related to local currency revenue and operating expenses in Europe. However, the Company does not engage in forward foreign exchange or similar contracts to reduce its economic exposure to changes in exchange rates as the associated risk is not considered significant. Because the Company markets, sells and licenses its products throughout the world, it could be significantly affected by weak economic conditions in foreign markets that could reduce demand for its products.

The Company is exposed to changes in interest rates primarily as a result of its long-term debt requirements. The Company's interest rate risk management objectives are to limit the effect of interest rate changes on earnings and cash flows and to lower overall borrowing costs. Based on the debt balance at May 31, 2007, a hypothetical change in the interest rate of +2% or -2% would result in a hypothetical change to interest expense of about \$271,000 and \$(271,000), respectively.

The Company does not enter into contracts for speculative or trading purposes, nor is it a party to any leveraged derivative instruments.

### FACTORS THAT MAY AFFECT FUTURE RESULTS

The Company's business is subject to many uncertainties and risks. This Form 10-KSB 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

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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; 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 five of our last six fiscal years. It is our expectation that we can continue to improve on our recent success, 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 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. Greenleaf Capital is the company's largest shareholder owning 44.6% and has been the company's sole debt provider since 1996. (See Note I to the Consolidated Financial Statements.)

The Company utilizes partnerships with various third party vendors and relies upon certain of their software and utilities to continue to develop and support ProductCenter customers with their integrations from ProductCenter to their respective CAD solution. These agreements are subject to termination at will by the vendor and would require the Company to seek alternative methods of providing continuing support for it's existing customers and an alternative solution to meet the needs of prospective customers which could have a material effect on future performance. On July 20, 2007, the Company was informed that it's agreement with one such vendor, Parametric Technology Corporation (PTC) will not be extended beyond its renewal date of January 31, 2008. The Company is investigating and validating viable alternatives for our current and future customers who would require a Pro/ENGINEER integrator solution and we are also assessing the impact that this non-renewal will have on our current and future business. Approximately 60% of our current ProductCenter customer base utilizes our current Pro/ENGINEER integrator solution.

REVENUE DECLINE FOR CERTAIN PRODUCT LINES. We experienced revenue declines from 2006 to 2007 of 3.0% for our Cadra product line and 31.5% for our AMT product line. The declines for the same period for software maintenance revenue was

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about 12% and 17% respectively 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.

### ITEM 7 - FINANCIAL STATEMENTS

Financial statements are included herein.

### ITEM 8 - CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

### Item 8A. - CONTROLS AND PROCEDURES

The Company's Chief Financial Officer is responsible for establishing and maintaining disclosure controls and procedures for the Company. Such officer has concluded (based upon their 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 III

### ITEM 9 - DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT

Set forth below is certain information regarding the Directors and executive officers of SofTech, Inc. (the "Company") as of August 15, 2007, based on information furnished by them to the Company.

#### DIRECTORS

Ronald A. Elenbaas, 54, term expired in 2006; Mr. Elenbaas is currently Chairman of the Board of Humanex, LLC, a human resource strategic planning firm and am also the Chairman of the Board of the Ocean Reef Club. Mr. Elenbaas also serves on the Board of the Ocean Reef Medical Center as well as director of Greenleaf Trust. From 1975 to 2000, Mr. Elenbaas was employed by Stryker Corporation in various positions, most recently as President of Stryker Surgical Group, a division of Stryker Corporation. Mr. Elenbaas was appointed a Director of the Company in September 1996.

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William D. Johnston, 60, term expires in 2008; Mr. Johnston serves as Chairman of the Company and has been a Director since 1996. Mr. Johnston is President, Chairman and CEO of the Greenleaf Companies. Included in the Greenleaf Companies are Greenleaf Trust, a Michigan chartered bank, Greenleaf Capital, Inc. a venture capital company and lender to SofTech, Greenleaf Hospitality Group, Inc. a management company delivering management services to the host industry and Catalyst Development Co., L.L.C., a commercial real estate development company. Mr. Johnston has served as President, Chairman and CEO of the Greenleaf

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Companies since 1991.

Timothy L. Tyler, 53, term expires in 2007; Mr. Tyler has served since 1995 as President of Borroughs Corporation, a privately held, Michigan-based business that designs, manufactures and markets industrial and library shelving units, metal office furniture and check out stands primarily in the United States. Mr. Tyler served as President and General Manager of Tyler Supply Company from 1979 to 1995. Mr. Tyler was appointed a Director of the Company in September 1996.

Michael Elliston, 45, term expires in 2008; Mr. Elliston has served as Chief Accounting Officer of the Greenleaf Companies since June 2005. Prior to joining Greenleaf, Mr. Elliston was the Chief Financial Officer for Holly's, Inc. and GR Hospitality, Inc., Michigan based Companies that owned and managed hotels, since July 1991. Mr. Elliston was appointed a Director of the Company in March of 2007

Frederick A. Lake, 71, term expired in 2006; Mr. Lake is a partner in the law firm of Lake, Stover & Schau, PLC, a Michigan based law firm. Mr. Lake has been with Lake, Stover & Schau, PLC, and its predecessors for more than five years. Mr. Lake's firm also serves as corporate counsel to the Greenleaf Companies. Mr. Lake was appointed a Director of the Company in July 2000.

Each member of the Board of Directors also serves on the Audit Committee of the Board of Directors. The Audit Committee recommends the engagement of the Company's independent accountants. In addition, the Audit Committee reviews comments made by the independent accountants with respect to internal controls and considers any corrective action to be taken by management; reviews internal accounting procedures and controls within the Company's financial and accounting staff; and reviews the need for any non-audit services to be provided by the independent accountants. Michael Elliston has been designated as the audit committee financial expert. Michael Elliston is independent of management.

Each member of the Board of Directors also serves on the Compensation Committee of the Board of Directors. The Compensation Committee recommends salaries and bonuses for officers and general managers and establishes general policies and procedures for salary and performance reviews and the granting of bonuses to other employees. It also administers the Company's 1994 Stock Option Plan (the "Plan") and the SofTech Employee Stock Purchase Plan.

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### EXECUTIVE OFFICERS

The current executive officers of the Company are as follows:

| Name            | Age | Position                    |
|-----------------|-----|-----------------------------|
| Jean J. Croteau | 51  | President                   |
| Victor G. Bovey | 50  | Vice President, Engineering |
| Amy E. McGuire  | 32  | Chief Financial Officer     |

Executive officers of the Company are elected at the first Board of Directors meeting following the Stockholders' meeting at which the Directors are elected.

The following provides biographical information with respect to the Executive Officers not identified in Item 10 of this Annual Report on Form 10-KSB:

Jean Croteau was appointed President in January of 2007. He was formerly the Vice President, Operations from July 2001 to January 2007. He started with the Company in 1981 as Senior Contracts Administrator and was promoted to various

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positions of greater responsibilities until his departure in 1995. Mr. Croteau rejoined SofTech in 1998. From 1995 through 1998 he served as the Director of Business Operations for the Energy Services Division of XENERGY, Inc.

Victor G. Bovey was appointed Vice President of Engineering of the Company in March 2000. He started with the Company in November 1997 as Director of Product Development. Prior to his employment with SofTech he was employed for thirteen years with CIMLINC Incorporated in various engineering and product development positions.

Amy E. McGuire was appointed Chief Financial Officer in January of 2007. She joined SofTech in 2002 when Workgroup Technology Corporation ("WTC") was acquired and became Corporate Controller on August 1, 2004. She was employed by WTC for 5 years prior to that acquisition.

Joseph P. Mullaney was appointed President and Chief Operating Officer in June 2001. Previously he served as Vice President, Treasurer, and Chief Financial Officer of the Company from November 1993 to June 2001. He joined the Company in May 1990 as Assistant Controller and was promoted to Corporate Controller in June 1990. Prior to his employment with SofTech he was employed for seven years at the Boston office of Coopers & Lybrand LLP (now PriceWaterhouseCoopers LLP) as an auditor in various staff and management positions. Joseph Mullaney resigned his position January of 2007.

### COMPLIANCE WITH SECTION 16(a) OF THE SECURITIES EXCHANGE ACT OF 1934

Section 16(a) of the Securities Exchange Act of 1934, as amended ("Section 16(a)") requires the Company's Directors and executive officers, and persons who own more than ten percent of a registered class of the Company's equity securities (collectively, "Section 16 reporting persons"), to file with the Securities and Exchange Commission ("SEC") initial reports of ownership and reports of changes in ownership of Common Stock and other equity securities of the Company. Section 16 reporting persons are required by SEC regulations to furnish the Company with copies of all Section 16(a) forms they file.

To the Company's knowledge, based solely on a review of the copies of such reports furnished to the Company and on written representations that no other reports were required, during the fiscal year ended May 31, 2007, the Section 16 reporting persons complied with all Section 16(a) filing requirements applicable to them.

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### ITEM 10 - EXECUTIVE COMPENSATION

#### COMPENSATION OF DIRECTORS

Directors were not paid any fees or additional compensation for service as members of the Board of Directors or any committee thereof.

Pursuant to the Company's 1994 Stock Option Plan (the "1994 Stock Option Plan"), non-employee Directors may be granted non-qualified options to purchase shares of Common Stock of the Company. The Compensation Committee of the Board of Directors administers the 1994 Stock Option Plan. Stock options typically terminate upon a Director leaving his or her position for any reason other than death or disability. No option may be exercised after the expiration of ten years from its date of grant. No new options could be granted under this Plan after 2004. No option awards were made in fiscal 2007.

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### SUMMARY COMPENSATION TABLE

The following table summarizes the compensation paid to the President and Chief Executive Officer of the Company and each of the Company's two other most highly compensated executive officers (the "Named Executives") during or with respect to fiscal 2005, 2006 and 2007 fiscal years for services in all capacities to the Company.

| Name and<br>Principal Fiscal<br>Position Year               | Annual Compensation |           | Long Term Compensation Awards        |  |                                      |
|---|---------------------|-----------|--------------------------------------|--|--------------------------------------|
|   | Salary(\$)          | Bonus(\$) | Other Annual<br>Compensation<br>(\$) | Securities<br>Underlying<br>Options(#) | All Other<br>Compensation<br>(1) (2) |
| Jean Croteau -<br>President                                 |                     |           |                                      |  |                                      |
| 2007  | 186,437             | 53,330    | --                                   | --                                     | 4,219                                |
| 2006  | 170,321             | 65,972    | --                                   | --                                     | 4,245                                |
| 2005  | 163,770             | 45,000    | --                                   | --                                     | 1,558                                |
| Victor G. Bovey -<br>Vice President, Research & Development |                     |           |                                      |  |                                      |
| 2007  | 120,800             | --        | --                                   | --                                     | 2,416                                |
| 2006  | 142,744             | --        | --                                   | --                                     | 2,736                                |
| 2005  | 137,917             | --        | --                                   | --                                     | 2,758                                |
| Amy E. McGuire -<br>Chief Financial Officer                 |                     |           |                                      |  |                                      |
| 2007  | 85,667              | 3,500     | --                                   | --                                     | 1,783                                |

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|  |         |        |    |    |            |
|--|---------|--------|----|----|------------|
| Joseph P. Mullaney(4)-<br>Former President and COO (Resigned January 2007) |         |        |    |    |            |
| 2007   | 156,240 |        |    |    | (3) 12,500 |
| 2006   | 234,000 | 21,000 | -- | -- | (3) 16,007 |
| 2005   | 225,300 | 60,000 | -- | -- | (3) 13,489 |

(1) Includes amounts deferred by Messrs. Mullaney, Bovey, Croteau and McGuire under the Company's 401(k) plan.

(2) Except as otherwise noted, amounts listed in this column reflect the Company's contributions to each of the Named Executive's accounts under the Company's 401(k) plan.

(3) Includes imputed compensation related to the non-interest bearing note receivable described in Note K to the financial statements.

#### OPTION GRANTS IN THE LAST FISCAL YEAR

No stock appreciation rights ("SARs") or options to purchase Company stock have been granted to the Named Executive Officers of the Company during fiscal year 2007.



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AGGREGATE OPTION EXERCISES IN THE LAST FISCAL YEAR AND OPTION VALUE AT MAY 31, 2007.

The following table sets forth certain information concerning the number and value of unexercised options held by the President and each Named Executive.

| NAME               | NUMBER OF<br>SHARES ACQUIRED<br>ON EXERCISE | VALUE<br>REALISED (\$) | NUMBER OF UNEXERCISED<br>OPTIONS AT MAY 31, 2007<br>EXERCISABLE/UNEXERCISABLE | VALUE OF UNEXERCISED   |
|--------------------|---|------------------------|---|--|
|                    |   |                        |   | IN-THE-MONEY OPTION<br>AT MAY 31, 2007 (\$<br>EXERCISABLE/UNEXERCISABLE) |
| JOSEPH P. MULLANEY | --  | --                     | 60,000/40,000   | 600/400  |
| VICTOR G. BOVEY    | --  | --                     | 15,000/0  | 150/0  |
| JEAN CROTEAU       | --  | --                     | 50,000/0  | 500/0  |

(1) Market value of underlying securities at May 31, 2007 based on a per share value of \$.10 less the aggregate exercise price.

### EMPLOYMENT CONTRACTS

The Company does not have employment contracts with its Named Executives.

### COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

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Each of the members of the Board of Directors served as members of the Compensation Committee of the Company's Board of Directors during the fiscal year ended May 31, 2007.

### ITEM 11 - SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

#### SECURITY OWNERSHIP OF MANAGEMENT AND PRINCIPAL STOCKHOLDERS

Information concerning beneficial ownership of the Company's Common Stock, as of August 17, 2007, for (i) each person named in the "Summary Compensation Table" below as a Named Executive of the Company during the fiscal year ended May 31, 2007, (ii) each Director and each of the Company's nominees to the Board of Directors and (iii) all Directors and executive officers of the Company as a group is set forth below.

| Name of Beneficial Owner    | Shares of Common Stock<br>Beneficially Owned as<br>of August 17, 2007 (1) | Percentage of<br>Outstanding Common<br>Stock Beneficially<br>Owned as of<br>August 17, 2007 (2) |
|-----------------------------|---|---|
| Joseph P. Mullaney          | 174,319(3)  | 1.4%  |
| Jean Croteau                | 50,000(3)   | *   |
| Victor G. Bovey             | 35,350(3)   | *   |
| William Johnston            | 5,441,443(3) (4)  | 44.5  |
| Timothy L. Tyler            | 13,200(3)   | *   |
| Ronald Elenbaas             | 55,900(3)   | *   |
| Frederick Lake              | 14,200(3)   | *   |
| All Directors and executive |   |   |

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officers as a group (8 persons) 5,784,412 46.6%

\* Less than one percent (1%).

- (1) Based upon information furnished by the persons listed. Except as otherwise noted, all persons have sole voting and investment power over the shares listed. A person is deemed, as of any date, to have "beneficial ownership" of any security that such person has the right to acquire within 60 days after such date.
- (2) There were 12,213,236 shares outstanding on August 17, 2007. In addition, 198,800 shares issuable upon exercise of stock options held by certain Directors and executive officers of the Company are deemed to be outstanding as of August 17, 2007 for purposes of certain calculations in this table. See notes 3, 4 and 5 below.
- (3) Includes shares issuable under stock options as follows: Mr. Mullaney - 80,000; Mr. Croteau - 50,000; Mr. Bovey - 15,000; Mr. Johnston - 13,200; Mr. Tyler - 13,200; Mr. Elenbaas - 13,200; and Mr. Lake - 14,200.
- (4) Mr. Johnston's business address is Greenleaf Capital, 100 West Michigan Ave., Kalamazoo, Michigan, 49007.
- (5) Includes 198,800 shares issuable upon exercise of stock options held by all Directors and executive officers as a group.

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### ITEM 12 - CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

As disclosed in Note H and I to the Company's 2007 Annual Report on Form 10-KSB, the Company has entered into various financing arrangements with Greenleaf Capital over the last several years. Greenleaf Capital is the Company's primary source of capital. William D. Johnston, a director of SofTech since September 1996, is the President and sole principal of Greenleaf Companies. The Company paid Greenleaf Capital approximately \$1.6 million and \$1.7 million in fiscal 2007 and 2006, respectively, in finance charges and management fees. Greenleaf Trust also serves as the trustee and investment advisor for the Company's 401-K Plan.

### ITEM 13 - EXHIBITS AND REPORTS ON FORM 8-K

The following items are filed as part of this report:

(a) Exhibits:

(2)(i) Asset Purchase Agreement by and among SofTech, Inc., Information Decisions, Inc., System Constructs, Inc., and Data Systems Network Corporation filed as Exhibit 2.1 to Form 8-K, dated September 12, 1996, is incorporated by reference.

(2)(ii) Stock Purchase Agreement dated as of December 31, 1996 by and among SofTech, Inc., Information Decisions, Inc., Computer Graphics Corporation, and the Stockholders of Computer Graphics Corporation, filed as Exhibit 2.1 to Form S-3, dated June 30, 1997, is incorporated by reference.

(2)(iii) Stock Purchase Agreement dated as of February 27, 1997 by and among SofTech, Inc., Information Decisions, Inc., Ram Design and Graphics Corporation, and the Stockholders of Ram Design and Graphics Corp., filed as Exhibit 2.2 to Form S-3, dated June 30, 1997, is incorporated by reference.

(2)(iv) Asset Purchase Agreement by and among SofTech, Inc., Information Decisions, Inc., CIMLINC Incorporated and CIMLINC GmbH, filed as Exhibit 2.1 to Form 8-K, dated November 10, 1997, is incorporated by reference.

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(2) (v) Asset Purchase Agreement by and among SofTech, Inc., Adra Systems, Inc., Adra Systems, GmbH, and MatrixOne, Inc., filed as Exhibit 2.1 for Form 8-K, dated May 7, 1998, is incorporated by reference.

(2) (vi) Agreement and Plan of Merger by and among SofTech, Inc., SofTech Acquisition Corporation, and Workgroup Technology Corporation dated November 13, 2002, filed as Exhibit 6 to Form SC 13D/A, dated November 15, 2002, is incorporated by reference.

(3) (i) Articles of Organization filed as Exhibit 3(a) to Registration Statement No. 2-73261 are incorporated by reference. Amendment to the Articles of Organization filed as Exhibit (19) to Form 10-Q for the fiscal quarter ended November 28, 1986 is incorporated by reference.

(3) (ii) By-laws of the Company, filed as Exhibit (3) (b) to 1990 Form 10K are incorporated herein by reference. Reference is made to Exhibit (3) (a) above, which is incorporated by reference. Form of common stock certificate, filed as Exhibit 4(A), to Registration statement number 2-73261, is incorporated by reference.

(10) (i) Greenleaf Capital \$11.0 million Promissory Note, filed as Exhibit 10.2 to the Form 10-K for the fiscal year ended May 31, 2001, is incorporated by reference.

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(10) (ii) Greenleaf Capital \$3.0 million Revolving Line of Credit, filed as Exhibit 10.3 to the Form 10-K for the fiscal year ended May 31, 2001, is incorporated by reference.

(10) (iii) Amendment to Promissory Note dated November 8, 2002, filed as Exhibit 4 to Form SC 13D/A filed November 15, 2002, is incorporated by reference.

(14) Code of Ethics for Officers, filed as Exhibit 14 to the Form 10-KSB for the year ended May 31, 2004, is incorporated by reference.

(21) Subsidiaries of the Registrant, filed herewith.

(23) (i) Consent of Vitale, Caturano & Company Ltd., filed herewith.

(31) Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

(32) Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K

The Company filed a Form 8-K on April 16, 2007 regarding its press release of third quarter fiscal 2007 results.

### ITEM 14 - PRINCIPAL ACCOUNTANT FEES AND SERVICES

#### AUDIT FEES

The following table presents the aggregate fees of the principal accountants for professional services rendered for the audit of the Company's annual financial statements and review of financial statements included in the

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Company's Form 10-QSB's for the years ended May 31, :

|                                     | 2007      | 2006      |
|-------------------------------------|-----------|-----------|
| Audit and quarterly review fees (1) | \$ 98,000 | \$ 96,000 |
| Tax related fees (2)                | 20,000    | 20,000    |
| Total fees                          | \$118,000 | \$116,000 |

- (1) Audit and quarterly review fees consists of audit work performed in the preparation of the financial statements to be included in the Company's Form 10-KSB and reviews of the Company's financials statements to be included in the Company's Form 10-QSB's filed with the Securities and Exchange Commission for the respective years.
- (2) Tax related fees consisted of preparation of the Company's tax returns for each of the fiscal years.

The Company's Audit Committee (the "Committee") is solely responsible for the nomination, approval, compensation, evaluation and discharge of the independent public accountants. The independent public accountants report directly to the Committee and the Committee is responsible for the resolution of disagreements between management and the independent public accountants. Consistent with the Securities and Exchange Commission requirements, the Committee has adopted a policy to pre-approve all audit and permissible non-audit services provided by the independent public accountants. The Company's independent public accountants for the current fiscal year have been appointed by the Committee.

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### REPORT OF REGISTERED INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors and Stockholders of SofTech, Inc.

We have audited the accompanying consolidated balance sheet of SofTech, Inc. and subsidiaries as of May 31, 2007 and the related consolidated statements of operations, changes in stockholders' deficit and comprehensive loss and cash flows for the years ended May 31, 2007 and 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of SofTech, Inc. and subsidiaries as of May 31, 2007, and the consolidated results

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of its operations and its consolidated cash flows for the years ended May 31, 2007 and 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note B to the financial statements, effective June 1, 2006 the Company adopted the provisions of Statement of Financial Accounting Standard No. 123R " Share-Based Payment".

/s/ Vitale, Caturano & Company LTD.

Boston Massachusetts  
July 20, 2007

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### SOFTECH, INC. CONSOLIDATED STATEMENTS OF OPERATIONS For Fiscal Years Ended May 31,

|  | 2007<br>----- | 2006<br>----- |
|--|---------------|---------------|
| (in thousands, except per share data)  |               |               |
| Revenue:   |               |               |
| Products   | \$ 2,602      | \$ 3,432      |
| Services   | 8,447         | 9,046         |
|  | -----         | -----         |
| Total Revenue  | 11,049        | 12,478        |
|  | -----         | -----         |
| Cost of Revenue:   |               |               |
| Cost of products sold: materials   | 90            | 208           |
| Cost of product sold: amortization of<br>capitalized software costs and<br>other intangible assets | 1,416         | 1,872         |
| Cost of services provided  | 1,615         | 1,586         |
|  | -----         | -----         |
| Total Cost of Revenue  | 3,121         | 3,666         |
|  | -----         | -----         |
| Gross margin   | 7,928         | 8,812         |
| Research and development   | 2,164         | 2,816         |
| Selling, general and administrative  | 5,526         | 6,111         |
|  | -----         | -----         |
| Income (Loss) from operations  | 238           | (115)         |
| Interest expense, net  | 1,449         | 1,207         |
|  | -----         | -----         |
| Loss before income taxes   | (1,211)       | (1,322)       |
| Provision for income<br>taxes  | 11            | 10            |
|  | -----         | -----         |
| Net Loss   | \$ (1,222)    | \$ (1,332)    |

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|   | =====    | =====    |
|---|----------|----------|
| Per Common Share Data:                                    |          |          |
| Net Loss - basic and diluted                              | \$ (.10) | \$ (.11) |
|   | =====    | =====    |
| Weighted Average Shares Outstanding,<br>basic and diluted | 12,213   | 12,205   |
|   | =====    | =====    |

The accompanying notes are an integral part of the consolidated financial statements.

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SOFTECH, INC.  
CONSOLIDATED BALANCE SHEET  
AS OF MAY 31, 2007

(in thousands, except share and per share data)

Assets:

Current assets:

|   |          |
|---|----------|
| Cash and cash equivalents   | \$ 1,048 |
| Accounts receivable (less allowance for<br>uncollectible accounts of \$4) | 1,496    |
| Prepaid expenses and other assets   | 476      |
|   | -----    |
| Total current assets  | 3,020    |

Property and equipment, at cost:

|                           |       |
|---------------------------|-------|
| Data processing equipment | 3,392 |
| Office furniture          | 553   |
| Leasehold improvements    | 189   |
|                           | ----- |

|  |         |
|--|---------|
| Total property and equipment                   | 4,134   |
| Less accumulated depreciation and amortization | (3,909) |
|  | -----   |

|                             |       |
|-----------------------------|-------|
| Property and equipment, net | 225   |
|                             | ----- |

Other assets:

|  |       |
|--|-------|
| Capitalized software costs, net of amortization of<br>\$13,566 | 1,863 |
| Goodwill   | 4,600 |
| Other assets   | 136   |
|  | ----- |

|              |       |
|--------------|-------|
| Total Assets | 9,844 |
|              | ===== |

Liabilities and Stockholders' Deficit:

Current liabilities:

|                  |     |
|------------------|-----|
| Accounts payable | 300 |
| Accrued expenses | 869 |

|                  |       |
|------------------|-------|
| Deferred revenue | 3,568 |
|------------------|-------|

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|  |        |
|--|--------|
| Current portion of long term debt<br>with related party    | 610    |
| Current portion of capital lease                           | 31     |
|  | -----  |
| Total current liabilities                                  | 5,378  |
| Long-term liabilities:                                     |        |
| Long term debt with related party,<br>less current portion | 13,078 |
| Long-term capital lease,<br>Less current portion           | 82     |
|  | -----  |
| Total long-term liabilities                                | 13,160 |
| Total liabilities  | 18,538 |
|  | -----  |
| Commitments and Contingencies (Note J)                     |        |

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|   |          |
|---|----------|
| Stockholders' deficit:  |          |
| Common stock, \$.10 par value; authorized 20,000,000<br>shares; issued 12,213,236 | 1,221    |
| Capital in excess of par value  | 18,037   |
| Accumulated deficit   | (27,603) |
| Accumulated other comprehensive income (loss)                                     | (349)    |
|   | -----    |
| Total stockholders' deficit   | (8,694)  |
|   | -----    |
| Total Liabilities and Stockholders' Deficit                                       | \$ 9,844 |
|   | =====    |

The accompanying notes are an integral part of the consolidated financial statements.

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SOFTECH, INC.  
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS'  
DEFICIT AND COMPREHENSIVE LOSS  
For Fiscal Years Ended May 31,

|                                   | 2007     | 2006     |
|-----------------------------------|----------|----------|
|                                   | -----    | -----    |
| (in thousands, except share data) |          |          |
| Common Stock:                     |          |          |
| Balance at beginning of year      | \$ 1,221 | \$ 1,220 |
| Shares issued                     | 0        | 1        |
|                                   | -----    | -----    |

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|   |            |            |
|---|------------|------------|
| Balance at end of year                        | 1,221      | 1,221      |
|   | -----      | -----      |
| Capital in Excess of Par Value:               | 18,037     | 18,037     |
|   | -----      | -----      |
| Accumulated Deficit:                          |            |            |
| Balance at beginning of year                  | (26,381)   | (25,049)   |
| Net loss                                      | (1,222)    | (1,332)    |
|   | -----      | -----      |
| Balance at end of year                        | (27,603)   | (26,381)   |
|   | -----      | -----      |
| Accumulated other comprehensive loss:         |            |            |
| Balance at beginning of year                  | (294)      | (283)      |
| Foreign currency translation adjustments      | (55)       | (11)       |
|   | -----      | -----      |
| Balance at end of year                        | (349)      | (294)      |
|   | -----      | -----      |
| Total stockholders' deficit at<br>end of year | \$ (8,694) | \$ (7,417) |
|   | =====      | =====      |
| Comprehensive Loss                            |            |            |
| Net loss                                      | \$ (1,222) | \$ (1,332) |
| Foreign currency translation adjustments      | (55)       | (11)       |
|   | -----      | -----      |
| Total comprehensive loss                      | \$ (1,277) | \$ (1,343) |
|   | =====      | =====      |
| Outstanding Shares:                           |            |            |
| Balance at beginning of year                  | 12,213     | 12,205     |
| Shares issued                                 | 0          | 8          |
|   | -----      | -----      |
| Balance at end of year                        | 12,213     | 12,213     |
|   | -----      | -----      |

The accompanying notes are an integral part of the consolidated financial statements.

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SOFTECH, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
For Fiscal Years Ended May 31,

|  | 2007       | 2006       |
|--|------------|------------|
|  | -----      | -----      |
| (in thousands)   |            |            |
| Cash flows from operating activities:  |            |            |
| Net loss   | \$ (1,222) | \$ (1,332) |
| Adjustments to reconcile net loss to net<br>cash provided by operating activities: |            |            |
| Depreciation and amortization  | 1,469      | 1,936      |
| Change in operating assets and liabilities:  |            |            |
| Accounts receivable  | 161        | (39)       |
| Prepaid expenses and other assets  | (158)      | 31         |
| Accounts payable and accrued expenses  | (82)       | (1)        |



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|   |          |         |
|---|----------|---------|
| Deferred revenue                                    | 145      | (596)   |
|   | -----    | -----   |
| Total adjustments                                   | 1,535    | 1,331   |
|   | -----    | -----   |
| Net cash provided by (used in) operating activities | 313      | (1)     |
|   | -----    | -----   |
| Cash flows from investing activities:               |          |         |
| Payments for WTC shares tendered during this period | --       | (18)    |
| Capital expenditures                                | (12)     | (39)    |
|   | -----    | -----   |
| Net cash used in investing activities               | (12)     | (57)    |
|   | -----    | -----   |
| Cash flows from financing activities:               |          |         |
| Borrowings under debt agreements                    | 1,750    | 2,100   |
| Repayments under debt agreements                    | (1,628)  | (1,746) |
| Repayments under capital lease                      | (10)     | --      |
|   | -----    | -----   |
| Net cash provided by financing activities           | 112      | 354     |
|   | -----    | -----   |
| Effect of exchange rates on cash                    | (45)     | (15)    |
|   | -----    | -----   |
| Net increase in cash and cash equivalents           | 368      | 281     |
| Cash and cash equivalents, beginning of year        | 680      | 399     |
|   | -----    | -----   |
| Cash and cash equivalents, end of year              | \$ 1,048 | \$ 680  |
|   | =====    | =====   |

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Supplemental disclosures of cash flow information:

|                                       |         |         |
|---------------------------------------|---------|---------|
| Interest paid                         | \$1,448 | \$1,186 |
| Non-cash acquisition on capital lease | \$ 123  | --      |
| Income taxes paid                     | \$ 1    | \$ 10   |

The accompanying notes are an integral part of the consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. DESCRIPTION OF THE BUSINESS AND BASIS OF PRESENTATION

SofTech, Inc. (the "Company") was formed in Massachusetts on June 10, 1969. The Company had an initial public offering in August 1981 and a subsequent offering in December 1982. The Company is engaged in the development, marketing,

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distribution and support of computer software solutions that serve the Product Lifecycle Management ("PLM") industry. These solutions include software technology offerings for Computer Aided Design ("CAD"), Computer Aided Manufacturing ("CAM") as well as Product Data Management and Collaboration ("PDM") technologies, all of which fit under the broadly defined PLM industry. The Company's operations are organized geographically with European sales and customer support offices in France, Germany and Italy.

The consolidated financial statements of the Company include the accounts of SofTech, Inc. and its wholly-owned subsidiaries, Information Decisions, Inc. ("IDI"), Workgroup Technology Corporation ("WTC") acquired in December 2002, SofTech Technologies Ltd., SofTech, GmbH, Adra Systems, Srl, Adra Systems, Sarl, Compass, Inc. ("COMPASS"), System Constructs, Inc. ("SCI"), SofTech Investments, Inc. ("SII"), RAM Design and Graphics Corp. ("RAM"), AMG Associates, Inc. ("AMG") and SofTech Acquisition Corporation. SCI, SII, RAM, AMG and SofTech Technologies Ltd. are all inactive subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

The Company's revenue is derived almost entirely from technology acquisitions completed between 1997 and 2002. As of May 31, 2007 approximately 66% of its assets are composed of intangible assets related to these acquisitions. For the fiscal year ended May 31, 2007, the amortization of these intangible assets was approximately 53% of its total expenses and 70% of its revenue.

Although the Company has incurred operating losses during each of the last six years, we have generated positive cash flow from operations in five out of the six years. The year we failed to generate positive cash flow, we were break even.

Based on our year end cash balance of more than \$1 million, our long history of generating positive cash flow from operations, available borrowings on our existing line of credit, our solid relationship with our lender and our budget for 2008, we believe we have sufficient liquidity to meet our obligations for at least the next year.

### B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### 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 pertain to revenue recognition, the allowance for doubtful accounts receivable, the valuation of long term assets including intangibles (goodwill, capitalized software costs and other intangible assets) and deferred tax assets. Actual results could differ from those estimates.

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#### CASH AND CASH EQUIVALENTS:

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash held in foreign bank accounts at May 31, 2007 totaled \$253,000.

#### CONCENTRATION OF RISK:

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The Company believes there is no concentration of risk with any single customer or small group of customers whose failure or nonperformance would materially affect the Company's results. No customer exceeds ten percent of net sales. The Company generally does not require collateral on credit sales. Management evaluates the creditworthiness of customers prior to delivery of products and services and provides allowances at levels estimated to be adequate to cover any potentially uncollectible accounts. Bad debts are written off against the allowance when identified. The changes in the accounts receivable reserve are as follows:

| For the Years<br>Ended May 31, | Balance,<br>Beginning<br>of Period | Charged<br>to Costs<br>and<br>Expenses | Bad Debt<br>Write-offs | Balance,<br>End of<br>Period |
|--------------------------------|------------------------------------|--|------------------------|------------------------------|
| 2006                           | \$45,000                           | 23,000                                 | \$ 42,000              | \$ 26,000                    |
| 2007                           | 26,000                             | --                                     | 22,000                 | 4,000                        |

### PROPERTY AND EQUIPMENT:

Property and equipment is stated at cost. The Company provides for depreciation and amortization on a straight-line basis over the following estimated useful lives:

|                           |  |
|---------------------------|--|
| Data processing equipment | 2-5 years                              |
| Office furniture          | 5-10 years                             |
| Leasehold improvements    | Lesser of useful life or life of lease |

Depreciation expense, including amortization of assets under capital lease, was approximately \$53,000 and \$64,000, for fiscal 2007 and 2006, respectively.

Maintenance and repairs are charged to expense as incurred; betterments are capitalized. At the time property and equipment are retired, sold, or otherwise disposed of, the related costs and accumulated depreciation are removed from the accounts. Any resulting gain or loss on disposal is credited or charged to income.

### INCOME TAXES:

The provision for income taxes is based on the earnings or losses reported in the consolidated financial statements. The Company recognizes deferred tax liabilities and assets for the expected future tax consequences of events that have been recognized in the Company's financial statements or tax returns. Deferred tax liabilities and assets are determined based on the difference between the financial statement carrying amounts and tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to

reverse. The Company provides a valuation allowance against deferred tax assets if it is more likely than not that some or all of the deferred tax assets will not be realized.

### REVENUE RECOGNITION:

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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 are 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 is recognized as those services are rendered using a proportional performance model.

### CAPITALIZED SOFTWARE COSTS AND RESEARCH AND DEVELOPMENT:

The Company capitalizes certain costs incurred to internally develop and/or purchase software that it then licenses 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 in fiscal 2006 or 2007. Substantially all of the recorded balance represents software acquired from third parties. Amortization expense related to capitalized software costs for the year ended May 31, 2007 and 2006 was \$1,416,000 and \$ 1,872,000, respectively.

Research and development expense for the years ended May 31, 2007 and 2006 was \$2,164,000 and \$2,816,000, respectively.

### 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 continue to be amortized over those periods. Amortization of goodwill ceased as of May 31, 2002.

As of May 31, 2007, 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 (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

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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.

### FINANCIAL INSTRUMENTS:

The Company's financial instruments consist of cash, accounts receivable, notes receivable, accounts payable, and short and long term debt. The Company's estimate of the fair value of these financial instruments approximates their carrying amounts at May 31, 2007. The interest rate on the Company's debt facilities are variable and fluctuate with changes in the prime rate. In addition, the Company considers the premium in excess of the prime rate on its debt facilities to be reasonable based on the Company's revenue, current cash flow and near term prospects. For these reasons the Company considers the fair value of the debt to approximate the carrying value.

The Company sells its products to a wide variety of customers in numerous industries. A large portion of the Company's revenue is derived from customers for which the Company has an existing relationship and established credit history. For new customers for which the Company does not have an established credit history, the Company performs evaluations of the customer's credit worthiness prior to accepting an order. The Company does not require collateral or other security to support customer receivables. The Company's provision for uncollectible accounts has been nominal for both fiscal year 2007 and 2006.

### FOREIGN CURRENCY TRANSLATION:

The functional currency of the Company's foreign operations (England, France, Germany and Italy) is the local currency. 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 were included in operations in fiscal 2007 and 2006, but were not significant.

### COMPREHENSIVE INCOME:

Financial Accounting standards No. 130, "Reporting Comprehensive Income" ("SFAS 130") requires the reporting of comprehensive income in addition to net income from operations. Comprehensive income is a more inclusive reporting methodology that includes disclosure of certain financial information that historically has not been recognized in the calculation of net income. To date, the Company's comprehensive income items include foreign translation adjustments and unrealized gains and losses on marketable securities. Comprehensive income has been included in the consolidated Statement of Changes in Stockholders' Deficit and Comprehensive Loss for all periods.

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### NET INCOME (LOSS) PER COMMON SHARE:

The basic and diluted weighted average shares outstanding used in the computation of basic and diluted earnings per share calculated in accordance with Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings per Share" were 12,213,236 and 12,213,236 during fiscal years 2007 and 2006, respectively.

After the application of assumed proceeds, options to purchase shares of common stock of 19,060 and 130,128 respectively, have been excluded from the

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denominator for the computation of diluted earnings per share in fiscal 2007 and 2006, respectively, because their inclusion would be antidilutive.

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-based 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 year 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 No. 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)  | May 31, 2006 |
| -----  |              |
| Net loss - as reported   | \$ (1,332)   |
| Stock-based compensation expense determined<br>under fair value based method | (3)          |
|  | -----        |

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|  |         |
|--|---------|
| Net loss - pro forma                   | (1,335) |
|  | =====   |
| Loss per share - diluted - as reported | (.11)   |
| Loss per share - diluted - pro forma   | (.11)   |

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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 May 31, 2007:

|                                | NUMBER OF<br>OPTIONS | WEIGHTED<br>WEIGHTED AVERAGE<br>EXERCISE PRICE<br>PER SHARE | AVERAGE<br>REMAINING<br>CONTRACTUAL<br>LIFE IN YEARS | AGGREGATE<br>INTRINSIC VALUE |
|--------------------------------|----------------------|---|--|------------------------------|
| Outstanding at<br>May 31, 2006 | 323,000              | \$ .58  | 4.65   | \$ 152,070                   |
| Granted                        | -                    | -   |  |                              |
| Exercised                      | -                    | -   |  |                              |
| Forfeited or<br>expired        | (85,000)             | \$.98   |  |                              |
| Outstanding at<br>May 31, 2007 | 238,000              | \$.45   | 4.61   | \$ 84,594                    |
| Exercisable at<br>May 31, 2007 | 210,800              | \$.49   | 4.49   | \$ 83,840                    |

The following table summarizes the information related to non-vested stock option awards outstanding as of May 31, 2007:

|                            | NUMBER OF OPTIONS | WEIGHTED AVERAGE GRANT DATE<br>FAIR VALUE PER SHARE |
|----------------------------|-------------------|---|
| Non-vested at May 31, 2006 | 59,800            | \$ .03  |
| Granted                    | -                 |   |
| Vested                     | (27,800)          | \$.04   |

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|                            |         |        |
|----------------------------|---------|--------|
| Forfeited                  | (4,800) | \$ .08 |
| -----                      |         |        |
| Non-vested at May 31, 2007 | 27,200  | \$ .05 |
| -----                      |         |        |

As of May 31, 2007, the remaining prospective pre-tax cost of non-vested stock option employee compensation was \$1 which will be expensed on a pro rata basis over the next two years.

NEW ACCOUNTING PRONOUNCEMENTS:

In July 2006, the Financial Accounting Standards Board ("FASB") issued Financial Accounting Standards Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes". FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprises' financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes". FIN 48 prescribes a recognition threshold and measurement attributable for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. Management does not expect that the adoption of this standard will have a material effect on the Company's financial position, results of operations or cash flows.

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In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements," which provides enhanced guidance for using fair value to measure assets and liabilities. SFAS No. 157 establishes a common definition of fair value, provides a framework for measuring fair value under U.S. generally accepted accounting principles and expands disclosure requirements about fair value measurements. SFAS No. 157 is effective for financial statements issued in fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact, if any, the adoption of SFAS No. 157 will have on the consolidated financial statements.

In February 2007, the FASB issued Statement of Financial Standards No. 159 ("FASB 159"), "The Fair Value Option for Financial Assets and Financial Liabilities -- Including an Amendment of FASB Statement No. 115". This Statement provides companies with an option to measure, at specified election dates, many financial instruments and certain other items at fair value that are not currently measured at fair value. A company that adopts SFAS 159 will report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. This Statement also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. This Statement is effective for fiscal years beginning after November 15, 2007. The Company does not believe that the adoption of SFAS 159 will have a material impact on our results of operations or financial condition.

C. LIQUIDITY

The Company generated \$313,000 flow from operations in fiscal 2007 and has generated a total of \$2.6 million of cash from operations in the six previous



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fiscal years after restructuring its operation at the beginning of fiscal 2002. The fiscal 2002 restructuring was necessitated by significant cash losses from operations for four consecutive fiscal years from 1998 through 2001 which totaled approximately \$4.5 million.

While the improved performance detailed above represents significant operational improvement, the Company remains a highly leveraged operation that is dependent on cash flow from operations and its debt facilities with Greenleaf Capital to fund operations.

Although the Company believes its current cost structure together with reasonable revenue run rates based on historical performance will continue to generate positive cash flow through at least fiscal 2008, the current economic environment especially in the manufacturing sector makes forecasting revenue based on historical models difficult and somewhat unreliable. The Company is continuing to seek out market opportunities by expanding the reach of its technology to new markets to grow its revenue base.

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D. INCOME TAXES:

The provision for income taxes includes the following:

| For Years ended May 31, (in thousands) | 2007  | 2006  |
|--|-------|-------|
| Federal                                | \$ -- | \$ -- |
| Foreign                                | --    | --    |
| State and Local                        | 11    | 10    |
|  | ----  | ----  |
|  | 11    | 10    |
| Deferred                               | --    | --    |
|  | ----  | ----  |
|  | \$ 11 | \$ 10 |
|  | ===== | ===== |

The domestic and foreign components of loss from operations before income taxes of the consolidated companies were as follows (in thousands):

|          | 2007      | 2006      |
|----------|-----------|-----------|
|          | -----     | -----     |
| Domestic | \$(1,295) | \$(1,155) |
| Foreign  | 84        | (167)     |
|          | -----     | -----     |
|          | \$(1,211) | \$(1,322) |
|          | =====     | =====     |

At May 31, 2007, the Company had net operating loss carryforwards of \$21.5 million that begin expiring in 2013, And are available to reduce future taxable income. The Company also has an alternative minimum tax credit of approximately \$200,000 that has no expiration date that was available as of May 31, 2007.

The Company's effective income tax rates can be reconciled to the federal statutory income tax rate as follows:

| For the Years ended May 31, | 2007  | 2006  |
|-----------------------------|-------|-------|
|                             | ----- | ----- |

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|                    |       |       |
|--------------------|-------|-------|
| Statutory rate     | (34)% | (34)% |
| Valuation reserve  | 34    | 34    |
|                    | --    | --    |
| Effective tax rate | 0%    | 0%    |
|                    | ===   | ===   |

Deferred tax assets (liabilities) were comprised of the following at May 31:

| (in thousands)  | 2007     | 2006     |
|---|----------|----------|
| -----   |          |          |
| Deferred tax assets (liabilities):                                    |          |          |
| Net operating loss carryforwards                                      | \$ 7,319 | \$ 6,776 |
| Tax credit carryforwards  | 200      | 200      |
| Receivable allowances   | 1        | 1        |
| Vacation pay accrual  | 29       | 22       |
| Other accruals  | 61       | 70       |
| Depreciation  | (4)      | (3)      |
| Differences in book and tax basis of assets<br>of acquired businesses | 3,212    | 3,365    |
|   | -----    | -----    |
| Deferred tax assets   | 10,818   | 10,431   |
| Less: valuation allowance   | (10,818) | (10,431) |
|   | -----    | -----    |
| Net deferred tax assets recognized                                    | \$ 0     | \$ 0     |
|   | =====    | =====    |

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Due to the uncertainties regarding the realization of certain favorable tax attributes in future tax returns, the Company has established a valuation reserve against the otherwise recognizable net deferred tax assets. Changes in the valuation reserve impacted deferred tax expense as follows: fiscal 2007 (\$387,000) and fiscal 2006 \$134,000.

E. EMPLOYEE RETIREMENT PLANS:

The Company has one Internal Revenue Code Section 401(k) plan covering substantially all U.S. based employees and offers an employer match of a portion of an employee's voluntary contributions. The aggregate expense related to this employer match for fiscal 2007 and 2006 was \$74,000 and \$91,000, respectively.

F. 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 ("PDM") computer solutions. The Company's operations are organized geographically with foreign offices in England, 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 (in thousands):

|               | 2007     | 2006     |
|---------------|----------|----------|
|               | -----    | -----    |
| Revenue:      |          |          |
| North America | \$ 8,088 | \$ 9,755 |
| Asia          | 1,136    | 1,197    |

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|                    |           |           |
|--------------------|-----------|-----------|
| Europe             | 2,109     | 2,360     |
| Eliminations       | (284)     | (834)     |
|                    | -----     | -----     |
| Consolidated Total | \$ 11,049 | \$ 12,478 |
|                    | =====     | =====     |

|                    |         |  |
|--------------------|---------|--|
|                    | 2007    |  |
|                    | -----   |  |
| Long-Lived Assets: |         |  |
| North America      | \$6,645 |  |
| Europe             | 179     |  |
|                    | -----   |  |
| Consolidated Total | \$6,824 |  |
|                    | =====   |  |

Foreign revenue is based on the country in which the sale originates. Revenue from Germany was 10% and 11% of total consolidated revenue in fiscal years 2007 and 2006. No other customer or foreign country accounted for 10% or more of total revenue in fiscal 2007 or 2006.

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G. DEBT OBLIGATION WITH RELATED PARTY:

Debt obligations of the Company consist of the following obligations at May 31, 2007 (in thousands):

|                                  |           |
|----------------------------------|-----------|
| \$15,000 Promissory Note         | \$ 11,267 |
| \$3,000 Revolving Line of Credit | 2,421     |
|                                  | -----     |
|                                  | 13,688    |
| Less current portion             | (610)     |
|                                  | -----     |
|                                  | \$ 13,078 |
|                                  | =====     |

During fiscal 2000, the Company entered into a \$11 million borrowing arrangement ("Promissory Note") with Greenleaf Capital ("Greenleaf"). On November 8, 2002, the Company amended the Promissory Note. Under the amended agreement the Company increased its borrowing from \$11.0 million to \$15.0 million. In addition, the interest rate was reduced from 9.75% to Prime Rate plus 3.0%. During fiscal 2006 the rate has increased following changes in the prime rate. Effective April 12, 2006, the interest rate was adjusted to 10.0% to reflect the increase in the prime rate. In September 2006, the most recent change, the interest rate was adjusted to 10.5%. Principal and interest is payable monthly and the Promissory Note has a 15-year loan amortization with the remaining principal of approximately \$11,267,000 due in a single payment in June 2008. The Promissory Note expires on June 12, 2008.

In addition, the Company has a \$3.0 million Revolving Line of Credit with Greenleaf. This facility is used to supplement cash flows from operations to meet the Companies short term capital needs. The interest rate on the Revolving Line of Credit is Prime Rate plus 3.0%. Amounts borrowed under this facility are due annually in June unless otherwise extended. As discussed further below, the due date of the revolving line of credit was extended subsequent to year end.

During fiscal year 2000, the Company entered into a debt conversion agreement

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with Greenleaf. Under the terms of this agreement the Company has the right to repurchase up to 4,054,424 shares at the average price of \$1.233 per share. There is no expiration to this repurchase right.

On June 1, 2007, the Company and Greenleaf agreed to extend the due date on the revolving line of credit to June 2008. Annual maturities of debt obligations for fiscal years ended May 31, as amended, are as follows: 2008 - \$610,000 and 2009- \$13,078,000.

### H. RELATED PARTY TRANSACTIONS:

The Company is dependent upon Greenleaf for all of its funding needs. The Company currently funds its operations through a \$3.0 million Line of Credit facility as described in Note G above that expires annually in June. In addition, the Company has a senior credit facility with Greenleaf as described in Note G above. Greenleaf's President serves as the Chairman of the Board for the Company. In addition, Greenleaf provides advisory services and its President and its Chief Accounting Officer serve as Board members to the Company. Greenleaf is the Company's largest shareholder owning approximately 45% of its outstanding shares. The Company paid Greenleaf a management fee of approximately \$519,000 in fiscal 2007 and \$443,000 in fiscal 2006 in exchange for these services. The Greenleaf management and advisory fee has been included in SG&A expense.

William D. Johnston, a director of SofTech since September 1996, is the sole principal and the President of Greenleaf. Management recommended and the Board of Directors, other than Mr. Johnston who abstained from such vote, unanimously approved all transactions with Greenleaf.

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### I. LEASE COMMITMENTS:

#### OPERATING LEASES

The Company conducts its operations in office facilities leased through October 2008. Rental expense for fiscal years 2007 and 2006 was approximately \$450,000 and \$469,000, respectively.

At May 31, 2007, minimum annual rental commitments under noncancellable leases were as follows:

| Fiscal Year | Gross<br>Commitment |
|-------------|---------------------|
| -----       | -----               |
| 2008        | 282,000             |
| 2009        | 26,000              |

In December 2002 the Company extended its lease for office space at its headquarters in Massachusetts through 2008. As part of that extension, the Company provided the lessor with a letter of credit for \$390,000 from a commercial bank. In addition, the lessor assumed the Company's financial obligations for an abandoned office lease in Massachusetts that had previously been utilized by WTC prior to the Company's acquisition of that company. The benefits derived from the lessor's assumption of this obligation have been treated as a marketing concession and will reduce rent expense over the life of the lease extension.

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### CAPITAL LEASES

In February 2007, the company entered into a capital lease agreement with CitiCapital for a term of 48 months with a \$1 purchase option. The lease incurs interest using the straight line method. The assets are amortized over the life of the lease and amortization of the assets is included in depreciation expense for fiscal year 2007.

|                    |          |
|--------------------|----------|
| Computer equipment | 123,005  |
| Less amortization  | (10,250) |
|                    | -----    |
|                    | 112,755  |

Minimum future lease payments under the capital lease as of May 31, 2007.

|  |          |
|--|----------|
| 2008                                       | 36,411   |
| 2009                                       | 36,411   |
| 2010                                       | 36,411   |
| 2011                                       | 24,273   |
| Minimum lease payment                      | 133,506  |
| Amount representing Interest               | (20,751) |
| Present Value of Minimum<br>lease payments | 112,755  |

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### J. NOTE RECEIVABLE:

Joseph Mullaney, the Company's former Chief Executive Officer, has been extended a non-interest bearing note in the amount of \$134,000 related to a stock transaction in May 1998. The note is partially secured by all Company shares and stock options held by that officer. The Company has accounted for the note as a fixed arrangement.

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### SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

By /S/ Amy E. McGuire  
-----  
Amy E. McGuire, CFO

Date: August 29, 2007

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Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signature  | Title                   | Date    |
|--|-------------------------|---------|
| -----<br>/S/ Jean J. Croteau<br>-----<br>Jean J. Croteau       | President               | 8/29/07 |
| -----<br>/S/ Amy E. McGuire<br>-----<br>Amy E. McGuire         | Chief Financial Officer | 8/29/07 |
| -----<br>/S/ Ronald A. Elenbaas<br>-----<br>Ronald A. Elenbaas | Director                | 8/29/07 |
| -----<br>/S/ William Johnston<br>-----<br>William Johnston     | Director                | 8/29/07 |
| -----<br>/S/ Timothy Tyler<br>-----<br>Timothy Tyler           | Director                | 8/29/07 |
| -----<br>/S/ Michael D. Elliston<br>-----<br>Barry Bedford     | Director                | 8/29/07 |
| -----<br>/S/ Frederick A. Lake<br>-----<br>Frederick A. Lake   | Director                | 8/29/07 |