

Edgar Filing: Wayside Technology Group, Inc. - Form 10-Q

Wayside Technology Group, Inc.
Form 10-Q
November 08, 2007

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

FORM 10-Q

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

For the quarterly period ended September 30, 2007

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

For the transition period from _____ to _____

Commission File No. 000-26408

Wayside Technology Group, Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

13-3136104
(I.R.S. Employer Identification No.)

1157 Shrewsbury Avenue, Shrewsbury, New Jersey 07702

(Address of principal executive offices)

Registrant's Telephone Number (732) 389-8950

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 and Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and non-accelerated filer" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

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

There were 4,689,396 outstanding shares of common stock, par value \$.01 per share, as of October 30, 2007, not including 595,104 shares classified as treasury stock.

PART I - FINANCIAL INFORMATION
WAYSIDE TECHNOLOGY GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share amounts)

	September 30, <u>2007</u> (Unaudited)	December 31, <u>2006</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 9,270	\$ 13,832
Marketable securities	9,421	7,032
Accounts receivable, net	20,150	28,045
Inventory - finished goods	1,249	1,265
Prepaid expenses and other current assets	848	607
Deferred income taxes	926	1,632
Total current assets	41,864	52,413
Equipment and leasehold improvements, net	620	488
Other assets	2,096	2,927
Deferred income taxes	1,127	1,453
Total assets	\$ 45,707	\$ 57,281
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued expenses	\$ 21,691	\$ 35,304
Dividend payable	-	638
Total current liabilities	21,691	35,942
Other liabilities	20	41
Total liabilities	21,711	35,983
Commitments and contingencies		
Stockholders' equity		
Common stock, \$.01 par value; authorized, 10,000,000 shares; issued 5,284,500 shares	53	53
Additional paid-in capital	29,406	29,252
Treasury stock, at cost, 605,104 shares and 687,879 shares, respectively	(2,376)	(1,905)
Accumulated deficit	(3,530)	(6,302)
Accumulated other comprehensive income	443	200
Total stockholders' equity	23,996	21,298

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Total liabilities and stockholders' equity	\$	45,707	\$	57,281
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The accompanying notes are an integral part of these condensed consolidated financial statements

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WAYSIDE TECHNOLOGY GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(Unaudited)
(In thousands, except per share data)

	Nine months ended September 30,		Three months ended September 30,	
	2007	2006	2007	2006
Net sales	\$ 132,752	\$ 125,479	\$ 41,790	\$ 48,679
Cost of sales	119,834	113,196	37,664	44,299
Gross profit	12,918	12,283	4,126	4,380
Selling, general and administrative expenses	8,998	8,999	2,962	3,109
Income from operations	3,920	3,284	1,164	1,271
Interest income, net	749	501	257	222
Realized foreign exchange gain	1	2	1	1
Income before income tax provision	4,670	3,787	1,422	1,494
Provision for income taxes	1,898	1,556	600	635
Net income	\$ 2,772	\$ 2,231	\$ 822	\$ 859
Net income per common share - Basic	\$ 0.63	\$ 0.54	\$ 0.19	\$ 0.20
Net income per common share - Diluted	\$ 0.59	\$ 0.50	\$ 0.18	\$ 0.19
Weighted average common shares outstanding- Basic	4,395	4,162	4,426	4,213
Weighted average common shares outstanding- Diluted	4,682	4,495	4,674	4,548
Reconciliation to comprehensive income:				
Net income	\$ 2,772	\$ 2,231	\$ 822	\$ 859
Other comprehensive income, net of tax:				
Unrealized gain on marketable securities	4	21	4	6
Foreign currency translation adjustments	239	74	77	16
Total comprehensive income	\$ 3,015	\$ 2,326	\$ 903	\$ 881

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The accompanying notes are an integral part of these condensed consolidated financial statements

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WAYSIDE TECHNOLOGY GROUP, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
 (Unaudited)

(In thousands, except share amounts)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Treasury Stock	Accumulated Deficit	Accumulated other comprehensive Income	Total
Balance at January 1, 2007	5,284,500	\$53	\$29,252	\$(1,905)	\$(6,302)	\$200	\$21,298
Net income					2,772		2,772
Translation adjustment						239	239
Unrealized gain on available- for-sale securities						4	4
Exercise of stock options			542	452			994
Dividends paid			(1,345)				(1,345)
Tax benefit from exercises of non-qualified stock options			501				501
Share-based compensation expense			448				448
Restricted stock grants			8	(8)			-
Treasury shares repurchased			-	(915)			(915)
Balance at September 30, 2007	5,284,500	\$53	\$29,406	\$(2,376)	\$(3,530)	\$443	\$23,996

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

WAYSIDE TECHNOLOGY GROUP, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Unaudited)
 (In thousands)

	Nine months Ended September 30,	
	<u>2007</u>	<u>2006</u>
Net income	\$ 2,772	\$ 2,231
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	234	214
Provision for doubtful accounts	31	147
Deferred income taxes	1,032	688
Loss on sale of fixed assets	-	6
Share-based compensation expense	448	156
Changes in operating assets and liabilities:		
Accounts receivable	8,689	(3,449)
Inventory	16	957
Prepaid expenses and other current assets	(241)	(137)
Accounts payable and accrued expenses	(13,613)	5,083
Net change in other assets and liabilities	(23)	24
Net cash (used in) provided by operating activities	(655)	5,920
Cash flows from investing activities:		
Purchases of available-for-sale securities	(16,473)	(13,056)
Redemptions of available-for-sale securities	14,088	11,950
Capital expenditures	(358)	(297)
Proceeds from sale of fixed assets	-	10
Net cash used in investing activities	(2,743)	(1,393)
Cash flows from financing activities:		
Dividend paid	(1,983)	(2,228)
Proceeds from exercise of stock options	994	722
Treasury stock repurchased	(915)	(7)
Tax benefit from stock option exercises	501	736
Net cash used in financing activities	(1,403)	(777)
Effect of foreign exchange rate on cash	239	74
Net (decrease) increase in cash and cash equivalents	(4,562)	3,824
Cash and cash equivalents at beginning of period	13,832	7,369
Cash and cash equivalents at end of period	\$ 9,270	\$ 11,193
Supplemental Cash Flow Data		
Cash paid during the year for:		
Income taxes	\$ 506	\$ 258

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

WAYSIDE TECHNOLOGY GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS

September 30, 2007

(Unaudited)

The accompanying unaudited condensed consolidated financial statements of Wayside Technology Group, Inc. and its Subsidiaries (collectively, the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. The unaudited condensed consolidated statements of income for the interim periods are not necessarily indicative of results for the full year. For further information, refer to the consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K filed with the Securities Exchange Commission for the year ended December 31, 2006.

The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to product returns, bad debts, inventories, investments, intangible assets, income taxes, contingencies and litigation. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. In the opinion of the Company's management, all adjustments that are of a normal recurring nature, considered necessary for fair presentation, have been included. Actual results may differ from these estimates under different assumptions or conditions.

1. In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 ("SFAS 159"), "The Fair Value Option for Financial Assets and Financial Liabilities. SFAS 159 allows entities the option to measure eligible financial instruments at fair value as of specified dates. Such election, which may be applied on an instrument by instrument basis, is typically irrevocable once elected. Statement 159 is effective for fiscal years beginning after November 15, 2007, and early application is allowed under certain circumstances. We are currently evaluating the impact of SFAS 159, but do not expect the adoption of SFAS 159 to have a material impact on our consolidated financial operations or cash flows.

In June 2006, the FASB issued Financial Interpretation No. 48, "Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109" ("FIN 48"), which is a change in accounting for income taxes. FIN 48 specifies how tax benefits for uncertain tax positions are to be recognized, measured, and derecognized in financial statements; requires certain disclosures of uncertain tax matters; specifies how reserves for uncertain tax positions should be classified on the balance sheet; and provides transition and interim period guidance, among other provisions. The Company has adopted the provisions of FIN 48 as of January 1, 2007, and has analyzed filing positions in all of the federal and state jurisdictions where it is required to file income tax returns, as well as all open tax years in these jurisdictions. The Company has identified its federal consolidated tax return and its state tax return in New Jersey and its Canadian tax return as "major" tax jurisdictions, as defined. The only periods subject to examination for the Company's federal return are the 2005 through 2006 tax years. The audit of the tax year 2004 has been completed, with no adjustments proposed by the Internal Revenue Service. The current periods subject to examination for the Company's state returns in New Jersey are years 2002 through 2006. The current periods subject to examination for the Company's Canadian tax returns are the years 2003 through 2006. The Company did not record a cumulative effect adjustment related to the adoption of FIN 48.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 ("SFAS 157"), "Fair Value Measurements," which defines fair value, establishes guidelines for measuring fair value and expands

disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting

pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. Earlier adoption is permitted, provided the Company has not yet issued financial statements, including for interim periods, for that fiscal year. We are currently evaluating the impact of SFAS 157, but do not expect the adoption of SFAS 157 to have a material impact on our consolidated financial position, results of operations or cash flows.

2. Assets and liabilities of the Company's Canadian subsidiary have been translated at current exchange rates, and related revenues and expenses have been translated at average rates of exchange in effect during the period. The revenue from our Canadian operations in the first nine months of 2007 was \$16.6 million as compared to \$16.2 million for the first nine months of 2006. The revenue from our Canadian operations for the third quarter of 2007 was \$5.1 million as compared to \$5.2 million for the third quarter of 2006.

3. Cumulative translation adjustments and unrealized gains (losses) on available-for-sale securities have been classified within accumulated other comprehensive income, which is a separate component of stockholders' equity.

4. The Company records revenues from sales transactions when title to products sold passes to the customer. Usual sales terms are FOB shipping point, at which time title and risk of loss has passed to the customer and delivery has occurred. The majority of the Company's revenues relate to products recognized on a gross basis with the selling price to the customer recorded as net sales and the acquisition cost of the product to the Company recorded as cost of sales. At the time of sale, the Company also records an estimate for sales returns based on historical experience. Certain software maintenance products, third party services and extended warranties sold by the Company (for which the Company is not the primary obligor) are recognized on a net basis in accordance with Staff Accounting Bulletin (SAB) No. 101 and No. 104, "Revenue Recognition" and Emerging Issues Task Force (EITF) 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent". Accordingly, such revenues are recognized in net sales either at the time of sale or over the contract period, based on the nature of the contract, at the net amount retained by the Company, with no cost of goods sold.

In accordance with EITF 00-10, "Accounting for Shipping and Handling Fees and Costs", the Company records freight billed to its customers as net sales and the related freight costs as a cost of sales. Vendor rebates and price protection are recorded when earned as a reduction to cost of sales or merchandise inventory, as applicable. Cooperative reimbursements from vendors, which are earned and available, are recorded in the period the related advertising expenditure is incurred. Cooperative reimbursements are recorded as net sales in accordance with EITF 02-16, "Accounting for Consideration Received from a Vendor by a Customer (Including a Reseller of the Vendor's Products)".

5. Investments in available-for-sale securities at September 30, 2007 were (in thousands):

	Cost	Market value	Unrealized gain
U.S. Government Securities	\$ 9,417	\$ 9,421	\$ 4

The cost and market value of the Company's investments at September 30, 2007 by contractual maturity were (in thousands):

	Cost	Estimated Fair Value
Due in one year or less	\$ 9,417	\$ 9,421

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Investments in available-for-sale securities at December 31, 2006 were (in thousands):

	Cost	Market Value	Unrealized gain (loss)
U.S. Government Securities	\$ 6,941	\$ 6,941	-
Corporate Bonds	\$ 91	\$ 91	-
Total Marketable Securities	\$ 7,032	\$ 7,032	-

The cost and market value of the Company's investments at December 31, 2006 by contractual maturity were (in thousands):

	Cost	Estimated Fair Value
Due in one year or less	\$ 7,032	\$ 7,032

6. Balance Sheet Detail - (in thousands):

Other assets consisted of the following at September 30, 2007 and December 31, 2006:

	September 30, 2007	December 31, 2006
Accounts Receivable - long-term	\$2,030	\$2,855
Security Deposits	56	56
Trademarks	10	16
Total	\$2,096	\$2,927

Accounts receivable-long-term result from product sales with extended payment terms that are discounted to their present values at the prevailing market rates. In subsequent periods, the accounts receivable are increased to the amounts due and payable from the customers through the accretion of interest income on the unpaid accounts receivable due in future years.

Accounts payable and accrued expenses consist of the following as of September 30, 2007 and December 31, 2006:

	September 30, 2007	December 31, 2006
Trade accounts payable	\$20,440	\$33,955
Other accrued expenses	1,251	1,349
	\$21,691	\$35,304

7. Basic EPS is computed by dividing net income by the weighted average number of shares outstanding during the period. Diluted EPS is computed considering the potentially dilutive effect of outstanding stock options and nonvested shares of restricted stock. A reconciliation of the numerators and denominators of the basic and diluted per share computations follows (in thousands, except per share data):

	Nine months ended		Three months ended	
	September 30, <u>2007</u>	September 30, <u>2006</u>	September 30, <u>2007</u>	September 30, <u>2006</u>
Numerator:				
Net income	\$2,772	\$2,231	\$822	\$859
Denominator:				
Weighted average shares (Basic)	4,395	4,162	4,426	4,213
Dilutive effect of outstanding options and nonvested shares of restricted stock	287	333	248	335
Weighted average shares including assumed conversions (Diluted)	4,682	4,495	4,674	4,548
Basic net income per share	\$0.63	\$0.54	\$0.19	\$0.20
Diluted net income per share	\$0.59	\$0.50	\$0.18	\$0.19

9. On July 25, 2007, the Board of Directors declared a quarterly dividend of \$.15 per share of its common stock paid on August 20, 2007 to shareholders of record on August 6, 2007. Our Board intends to periodically review the amount and frequency of future payments of dividends, if any, in light of the Company's operations and need for capital. The dividend is reflected as a reduction of Additional Paid in Capital.

10. The Company had two major vendors that accounted for 37.8% and 8.6% of total purchases during the nine months ended September 30, 2007 and 31.9% and 10.6%, respectively, for the three months then ended. The Company had two major vendors that accounted for 48.6% and 12.8% of total purchases during the nine months ended September 30, 2006 and 56.4% and 13.3%, respectively, for the three months then ended. The Company had two major customers that accounted for 12.0% and 9.3% of total net sales during the nine months ended September 30, 2007 and 8.6% and 12.2% respectively during the three months ended September 30, 2007. These customers accounted for 12.4% and 5.2% and 15.7% and 4.7% of total net sales, respectively, during the nine and three months ended September 30, 2006. These customers accounted for 3.8% and 6.1%, respectively, of total net accounts receivable as of September 30, 2007.

11. The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction, and in various state and foreign jurisdictions. The Company believes that it has appropriate support for the income tax positions taken and to be taken on its tax returns and that its accruals for tax liabilities are adequate for all open years based on an assessment of many factors including past experience and interpretations of tax law applied to the facts of each matter. The Company's policy is to include any income tax related interest expense or penalties as a component of income tax expense.

The provision consists of the following:

	Nine months ended September 30,		Three months ended September 30,	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Current:	\$638	\$625	\$328	\$102
Federal	75	110	21	18
State	153	87	38	10
Canada	866	822	387	130
Deferred tax expense				
Federal	\$833	\$577	\$152	\$413
State	199	157	61	92
	1,032	734	213	505
Total	\$1,898	\$1,556	\$600	\$635
Effective Tax rate	40.6%	41.1%	42.2%	42.5%

As of September 30, 2007, the Company had U.S. deferred tax assets of approximately \$2.1 million reflecting, in part, a benefit of \$0.1 million in U.S. federal and state tax loss carry forwards, which will expire in varying amounts between 2007 and 2025. The full realization of the tax benefit associated with the carry forwards depends predominantly upon the Company's ability to generate taxable income during the carry forward period.

12. Effective January 1, 2006, we adopted SFAS No. 123(R), "Share-Based Payment," using the modified prospective transition method. Under the modified prospective transition method, recognized compensation cost for the nine and three months ended September 30, 2007 and 2006 includes 1) compensation cost for all share-based payments granted prior to, but not yet vested as of, January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of Statement 123; and 2) compensation cost for all share-based payments granted on or after January 1, 2006, based on the grant date fair value estimated in accordance with Statement 123(R). In accordance with the modified prospective method, we have not restated prior period results.

The Company's 2006 Stock-Based Compensation Plan (the "2006 Plan") authorizes the grant of Stock Options, Stock Units, Stock Appreciation Rights, Restricted Stock, Deferred Stock, Stock Bonuses, and other equity-based awards. The number of shares of common stock initially available under the 2006 Plan is 800,000. During 2006 315,000 shares of restricted stock were granted. In the first nine months of 2007, the Company granted 10,000 shares of restricted common stock that vest over 60 months; and there were forfeitures of 12,500 shares of restricted common stock. The number of shares of common stock available for future award grants to employees and directors under this plan is 487,500.

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Changes during 2007 in options outstanding for the combined plans were as follows:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value (\$M)(1)
Outstanding at January 1, 2007	602,335	\$7.56		
Granted in 2007	-	-		
Canceled in 2007	-	-		
Exercised in 2007	(149,445)	6.66		
Outstanding at September 30, 2007	452,890	7.86	6.0	2.6
Exercisable at September 30, 2007	452,890	7.86	6.0	2.6

(1) The intrinsic value is calculated as the difference between the market value at September 30, 2007 and the exercise price of the shares.

A summary of nonvested shares of restricted stock awards outstanding under the Company's 2006 Plan as of September 30, 2007, and changes during the nine months then ended is as follows:

	Shares	Weighted Average Grant Date Fair Value
Nonvested shares at January 1, 2007	293,500	\$13.68
Granted in 2007	10,000	15.19
Vested in 2007	(32,250)	13.81
Forfeited in 2007	(12,500)	14.57
Nonvested shares at September 30, 2007	258,750	13.65

As of September 30, 2007, there is approximately \$3.5 million of total unrecognized compensation costs related to nonvested restricted stock share-based compensation arrangements. The unrecognized compensation cost is expected to be recognized over a weighted-average period of 7.03 years.

For the nine months ended September 30, 2007 and 2006, the Company recognized share-based compensation cost of approximately \$448,000 and \$156,000, respectively, which is included in general and administrative expense. For the three months ended September 30, 2007 and 2006 the Company recognized share-based compensation cost of approximately \$146,000 and \$149,000, respectively. The Company does not capitalize any share-based compensation cost.

13. SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," requires that public companies report profits and losses and certain other information on their "reportable operating segments" in their annual and interim financial statements. The internal organization used by the Company's Chief Operating Decision Maker (CODM) to assess performance and allocate resources determines the basis for reportable operating segments. The Company's CODM is the Chief Executive Officer.

As of January 1, 2006 the Company is organized into two reportable operating segments -- the "Programmer's Paradise" segment, which sells technical software, hardware and services directly to end-users (such as individual programmers, corporations, government agencies, and educational institutions) and the "Lifeboat" segment, which distributes technical software to corporate resellers, VARs, consultants and systems integrators.

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As permitted by SFAS No. 131, the Company has utilized the aggregation criteria in combining its operations in Canada with the domestic segments as they provide the same products and services to similar clients and are considered together when the CODM decides how to allocate resources.

Segment income is based on segment revenue less the respective segments cost of revenues as well as segment direct costs (including such items as payroll costs and payroll related costs, such as profit sharing, incentive awards and insurance) and excluding corporate general and administrative expenses not attributed to a business unit. The Company only identifies accounts receivable and inventory by segment as shown below as "Selected Assets"; it does not allocate its other assets, including capital expenditures by segment.

The following segment reporting information of the Company is provided (in thousands):

	Nine months ended		Three months ended	
	September 30,		September 30,	
	2007	2006	2007	2006
Revenue:				
Programmer's Paradise	\$32,217	\$41,963	\$11,021	\$17,225
Lifeboat	100,535	83,516	30,769	31,454
	132,752	125,479	41,790	48,679
Gross Profit:				
Programmer's Paradise	\$4,302	\$5,667	\$1,421	\$2,100
Lifeboat	8,616	6,616	2,705	2,280
	12,918	12,283	4,126	4,380
Direct Costs:				
Programmer's Paradise	\$2,197	\$2,602	\$739	\$803
Lifeboat	2,133	1,597	733	576
	4,330	4,199	1,472	1,379
Segment Income:				
Programmer's Paradise	2,104	3,065	682	1,297
Lifeboat	6,484	5,019	1,972	1,704
Segment Income	8,588	8,084	2,654	3,001
Corporate general and administrative expenses	4,668	4,800	1,490	1,730
Interest income	749	501	257	222
Foreign currency translation gain	1	2	1	1
Income before taxes	\$4,670	\$3,787	\$1,422	\$1,494
Selected Assets By Segment:				
Programmer's Paradise	7,694	9,251		
Lifeboat	13,705	14,093		
Corporate assets	24,308	27,767		
Segment Select Assets	\$45,707	\$51,111		

14. In the second quarter of 2007 the Vice President of Marketing and Business Development resigned from his position with Wayside Technology Group, Inc. (the "Company").

In connection with resignation, the Company issued a letter (the "Resignation Letter"). Pursuant to the Resignation Letter, the Company will pay the former executive his current salary of \$150,000 (plus payments for unused vacation time) in 24 equal semimonthly installments. The Company is expensing the \$150,000 ratably over the term of the consulting agreement which is one year following the Resignation Letter.

15. During the second quarter of 2006, the Company made the decision to close down and sublease its sales office in Hauppauge, New York. Based on forecasted sublease income compared to estimated expenses, the Company recorded a liability and took a charge of approximately \$97,000 during the second quarter of 2006.

The balance of the lease liability at January 1, 2007 was \$41,000 and during the first nine months of 2007 the Company incurred \$31,000 in charges net of sublease income and accrued \$10,000 in interest expense so that the remaining lease liability is \$20,000 at September 30, 2007.

16. Certain reclassifications have been made to the prior year financial statements in order to conform to current year presentation.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under the heading "Certain Factors Affecting Operating Results" and elsewhere in this report. The following discussion should be read in conjunction with the consolidated financial statements and related notes included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission for the year ended December 31, 2006.

Overview

As of January 1, 2006 the Company is organized into two reportable operating segments -- the "Programmer's Paradise" segment, which sells technical software, hardware and services directly to end-users (such as individual programmers, corporations, government agencies, and educational institutions) and the "Lifeboat" segment, which distributes technical software to corporate resellers, VARs, consultants and systems integrators.

The Company's sales and results of operations have fluctuated and are expected to continue to fluctuate on a quarterly basis as a result of a number of factors, including: the loss of any major vendor, condition of the software industry in general; shifts in demand for software products; industry shipments of new software products or upgrades; the timing of new merchandise and catalog offerings; fluctuations in response rates; fluctuations in postage, paper, shipping and printing costs and in merchandise returns; adverse weather conditions that affect response, distribution or shipping; shifts in the timing of holidays; and changes in the Company's product offerings. The Company's operating expenditures are based on sales forecasts. If revenues do not meet expectations in any given quarter, operating results may be materially adversely affected.

Results of Operations

The following table sets forth for the periods indicated certain financial information derived from the Company's consolidated statements of income expressed as a percentage of net sales. This comparison of financial results is not necessarily indicative of future results:

	Nine months ended		Three months ended	
	<u>September 30,</u>		<u>September 30,</u>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	90.3	90.2	90.1	91.0
Gross profit	9.7	9.8	9.9	9.0
Selling, general and administrative expenses	6.7	7.2	7.1	6.4
Income from operations	3.0	2.6	2.8	2.6
Interest income, net	0.5	0.4	0.6	0.5
Realized foreign currency exchange gain(loss)	-	-	-	-
Income before income taxes	3.5	3.0	3.4	3.1
Provision for income taxes	1.4	1.2	1.4	1.3
Net income	2.1%	1.8%	2.0%	1.8%
Net Sales				

Net sales for the third quarter of 2007 decreased 14% or \$6.9 million to \$41.8 million compared to \$48.7 million for the same period in 2006.

Total sales for the third quarter of 2007 for our Lifeboat segment were \$30.8 million compared to \$31.5 million in the third quarter of 2006, representing a 2% decrease. Total sales for the third quarter of 2007 for our Programmer's Paradise segment were \$11.0 million compared to \$17.2 million in the third quarter of 2006, representing a 36% decrease.

For the nine months ended September 30, 2007, net sales increased 6% or \$7.3 million to \$132.8 million compared to \$125.5 million for the same period in 2006. Sales for the nine months ended September 30, 2007 for our Programmer's Paradise division were \$32.2 million compared to \$42.0 million for the same period last year. Sales for the nine months ended September 30, 2007 for our Lifeboat division were \$100.5 million compared to \$83.5 million for the same period last year.

In the Lifeboat Distribution segment, sales for the third quarter of 2007 decreased by 2%, compared to the year-earlier period, primarily due to price competition for VMware products, offset, in part, by strong sales growth for our remaining distribution lines. VMware, our largest vendor, opened up distribution for a number of competitors in 2007. The majority of these distributors decided to adopt an ultra low price strategy. Gross margins went down to as much as zero percent for large deals in the third quarter of 2007. VMware labeled sales for our Lifeboat Distribution segment decreased \$6.4 million as compared to the third quarter of 2006. Our remaining distribution sales showed excellent growth. Excluding VMware, sales increased by \$5.7 million or 41%.

In the Programmer's Paradise segment, sales for the third quarter of 2007 decreased by \$6.2 million, compared with the year-earlier period, primarily due to declining VMware sales as well as increased competition in the "direct to end user" segment of our business. The decline in VMware sales are mainly due to a change in the government's GSA program by VMware. VMware has selected an exclusive reseller/distributor for GSA government sales. Instead of invoicing the government and recognizing the revenue, Programmer's Paradise now receives a referral fee for VMware GSA sales. While this has a positive impact on gross margins, sales are impacted negatively. VMware's sales for our Programmers Paradise segment decreased \$3.1 million.

Gross Profit

The increase in sales of software licenses for which we receive only an agency fee, as well as sales of software maintenance contracts for which only the gross profit is recorded as net sales, makes period-to-period comparability of net sales and costs of goods sold more difficult. We believe that gross profit is a more reliable measure of business performance and is more useful in comparing period-to-period trends than net sales. Gross Profit for the quarter ended September 30, 2007 was \$4.1 million compared to \$4.4 million in the third quarter of 2006, a 6% decrease. Total gross profit for our Programmer's Paradise segment for the quarter ended September 30, 2007 was \$1.4 million compared to \$2.1 million in the third quarter of 2006, representing a 32% decrease. Total gross profit for our Lifeboat segment for the quarter ended September 30, 2007 was \$2.7 million compared to \$2.3 million in the third quarter of 2006, representing a 19% increase.

For the nine months ended September 30, 2007 gross profit increased by \$0.6 million to \$12.9 million compared to \$12.3 million in the same period in 2006. Programmer's Paradise gross profit for the nine months ended September 30, 2007 was \$4.3 million compared to \$5.7 million for the first nine months of 2006. Lifeboat's gross profit for the nine months ended September 30, 2007 was \$8.6 million compared to \$6.6 million for the first nine months of 2006. Gross profit margin as a percentage of net sales, for the nine months ended September 30, 2007 was 9.7% compared to 9.8% in the same period last year. Gross profit margin, as a percentage of net sales, for the quarter ending September 30, 2007 was 9.9% compared to 9.0% in the third quarter of 2006.

Gross profit margin for our Programmer's Paradise segment for the third quarter of 2007 was 12.9% compared to 12.2% in the third quarter of 2006. This was primarily due to increases in agency fees, vendor rebates and increases in the sales of services. These increases were offset by decreases in product margins, which includes vendor funding for advertising.

Gross profit margin for our Lifeboat segment for the third quarter of 2007 was 8.8% compared to 7.3% in the third quarter of 2006. This was primarily due to the strong growth in our higher margin specialty distribution lines and the decline of the lower margin, high volume VMware sales.

On a forward-looking basis, gross profit margin in future periods may be less than that achieved in the third quarter of 2007. We continuously assess the impact of large transactions and the continued shift in customer mix to the Lifeboat distribution segment with lower gross margins on the overall profitability of our Company. We foresee possible pressure on gross profit margins as a result of various factors, including the continued shift in customer mix to our Lifeboat segment, participation by vendors in inventory price protection and rebate programs, product mix, including software maintenance and third party services, pricing strategies, market conditions and other factors, any of which could result in a reduction of gross profit margins below those realized in the third quarter of 2007.

Selling, General and Administrative Expenses

Total selling, general, and administrative ("SG&A") expenses for the third quarter of 2007 were \$3.0 million compared to \$3.1 million in the third quarter of 2006. As a percentage of net sales, SG&A expenses for the third quarter of 2007 were 7.1% compared to 6.4% in the third quarter of 2006. For the nine months ended September 30, 2007 SG&A expenses were \$9.0 million compared to \$9.0 million in the same period last year. As a percentage of net sales, SG&A expenses were 6.7% compared to 7.2% in the same period last year.

The Company expects that its SG&A expenses, as a percentage of net sales, may vary by quarter depending on changes in sales volume, as well as the levels of continuing investments in key growth initiatives.

Direct selling costs for the third quarter of 2007 were \$1.5 million compared to \$1.4 million in 2006.

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Total direct selling costs for our Programmer's Paradise division for the third quarter of 2007 were \$0.7 million compared to \$0.8 million in 2006, representing an 8% decrease.

Total direct selling costs for our Lifeboat division for the third quarter of 2007 were \$0.7 million compared to \$0.5 million in 2006, representing a 27% increase, which was mainly a result of the Company hiring additional sales staff to support the growth of our Lifeboat division.

Income Taxes

The provision consists of the following: The provision consists of the following:

	Nine months ended		Three months ended	
	September 30,		September 30,	
	2007	2006	2007	2006
Current:				
Federal	\$638	\$625	\$328	\$102
State	75	110	21	18
Canada	153	87	38	10
	866	822	387	130
Deferred tax expense				
Federal	\$833	\$577	\$152	\$413
State	199	157	61	92
	1,032	734	213	505
Total	\$1,898	\$1,556	\$600	\$635
Effective Tax rate	40.6%	41.1%	42.2%	42.5%

As of September 30, 2007, the Company had U.S. deferred tax assets of approximately \$2.1 million reflecting, in part, a benefit of \$0.1 million in U.S. federal and state tax loss carry forwards, which will expire in varying amounts between 2007 and 2025. The full realization of the tax benefit associated with the carry forwards depends predominantly upon the Company's ability to generate taxable income during the carry forward period.

Liquidity and Capital Resources

During the first nine months of 2007 our cash and cash equivalents decreased by \$4.6 million to \$9.2 million at September 30, 2007, from \$13.8 million at December 31, 2006. During the first nine months of 2007, net cash used in operating activities was \$0.7 million, net cash used in investing activities amounted to \$2.7 million and net cash used in financing activities amounted to \$1.4 million offset by the effect of foreign exchange gains on cash of \$0.2 million.

Net cash used in operating activities for the first nine months of 2007 was \$0.7 million. Cash was used primarily in connection with a decrease in accounts payable and accrued expenses of \$13.6 million offset by a decrease in accounts receivable of \$8.7 million caused primarily by the decline in sales and income from operations net of non-cash charges of \$4.5 million.

Net cash used in investing activities in the first nine months of 2007 amounted to \$2.7 million. In light of the current low interest rates on our short-term savings accounts we decided to invest an additional net \$2.4 million

in U.S. government securities. These securities are highly rated and highly liquid. These securities are classified as available-for-sale securities in accordance with SFAS 115 "Accounting for Certain Investments in Debt and Equity Securities", and as a result, unrealized gains and losses are reported as part of accumulated other comprehensive income (loss). The remaining \$0.4 million of cash used in investing activities consisted of capital expenditures.

Net cash used in financing activities for the nine months ended September 30, 2007 was \$1.4 million which consisted of dividend payments of \$2.0 million and share buybacks of \$0.9 million offset by the proceeds and the resulting tax benefits from the exercise of options of \$1.5 million.

The Company's current and anticipated use of its cash and cash equivalents is, and will continue to be, to fund working capital, operational expenditures, the stock buyback program and dividends if declared by the board of directors. Our business plan furthermore contemplates to continue to use our cash to pay vendors promptly in order to obtain more favorable conditions.

We believe that the funds held in cash and cash equivalents will be sufficient to fund our working capital and cash requirements for at least the next 12 months. We currently do not have any credit facility and, in the foreseeable future, we do not plan to enter into an agreement providing for a line of credit.

Contractual Obligations as of September 30, 2007 were summarized as follows:

(Dollars in thousands)

	Total	Payment due by Period			
		Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-term debt	-	-	-	-	-
Capital Lease Obligations	-	-	-	-	-
Operating Leases	\$1,764	\$283	\$1,018	\$463	-
Purchase Obligations	-	-	-	-	-
Other Long term Obligations	-	-	-	-	-
Total Contractual Obligations	\$1,764	\$283	\$1,018	\$463	\$-

Operating leases primarily relates to the leases of the space used for our operations in Shrewsbury, New Jersey, and Mississauga, Canada. In the third quarter of 2006, the Company extended the lease on our Shrewsbury location for an additional fifty months extending the lease until December 2012. During the second quarter of 2006, the Company made the decision to close down and sublease it sales office in Hauppauge, New York. The table above includes minimum rent payments for the Hauppauge office net of sublease income. The commitments for operating leases include the minimum rent payments and a proportionate share of operating expenses and property taxes.

The Company is not committed by lines of credit or standby letters of credit, and has no standby repurchase obligations or other commercial debt commitments. The Company is not engaged in any transactions with related parties.

As of September 30, 2007, we did not have any off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of Regulation S-K.

Critical Accounting Policies and Estimates

The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements that have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. The Company recognizes revenue from the sale of software and hardware for microcomputers, servers and networks upon shipment or upon electronic delivery of the product. The Company expenses the advertising costs associated with producing its catalogs. The costs of these catalogs are expensed in the same month the catalogs are mailed.

On an on-going basis, the Company evaluates its estimates, including those related to product returns, bad debts, inventories, investments, intangible assets, income taxes, contingencies and litigation.

The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The Company records revenues from sales transactions when title to products sold passes to the customer. Usual sales terms are FOB shipping point, at which time title and risk of loss has passed to the customer and delivery has occurred. The majority of the Company's revenues relate to products recognized on a gross basis with the selling price to the customer recorded as net sales and the acquisition cost of the product to the Company recorded as cost of sales. At the time of sale, the Company also records an estimate for sales returns based on historical experience. Certain software maintenance products, third party services and extended warranties sold by the Company (for which the Company is not the primary obligor) are recognized on a net basis in accordance with Staff Accounting Bulletin (SAB) No. 101 and No. 104, "Revenue Recognition" and Emerging Issues Task Force (EITF) 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent". Accordingly, such revenues are recognized in net sales either at the time of sale or over the contract period, based on the nature of the contract, at the net amount retained by the Company, with no cost of goods sold.

In accordance with EITF 00-10, "Accounting for Shipping and Handling Fees and Costs", the Company records freight billed to its customers as net sales and the related freight costs as a cost of sales. Vendor rebates and price protection are recorded when earned as a reduction to cost of sales or merchandise inventory, as applicable. Cooperative reimbursements from vendors, which are earned and available, are recorded in the period the related advertising expenditure is incurred. Cooperative reimbursements are recorded as net sales in accordance with EITF 02-16, "Accounting for Consideration Received from a Vendor by a Customer (Including a Reseller of the Vendor's Products)".

The Company believes the following critical accounting policies used in the preparation of its consolidated financial statements affect its more significant judgments and estimates. The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. The Company writes down its inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-offs may be required.

Recent Accounting Pronouncements

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 ("SFAS 159"), "The Fair Value Option for Financial Assets and Financial Liabilities. SFAS 159 allows entities the option to measure eligible financial instruments at fair value as of specified dates. Such election, which may be applied on an instrument by instrument basis, is typically irrevocable once elected. SFAS 159 is effective for fiscal years beginning after November 15, 2007, and early application is allowed under certain circumstances. We are currently evaluating the impact of SFAS 159, but do not expect the adoption of SFAS 159 to have a material impact on our consolidated financial operations or cash flows.

In June 2006, the FASB issued Financial Interpretation No. 48, "Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109" ("FIN 48"), which is a change in accounting for income taxes. FIN 48 specifies how tax benefits for uncertain tax positions are to be recognized, measured, and derecognized in financial statements; requires certain disclosures of uncertain tax matters; specifies how reserves for uncertain tax positions should be classified on the balance sheet; and provides transition and interim period guidance, among other provisions. The Company has adopted the provisions of FIN 48 as of January 1, 2007, and has analyzed filing positions in all of the federal and state jurisdictions where it is required to file income tax returns, as well as all open tax years in these jurisdictions. The Company has identified its federal consolidated tax return and its state tax return in New Jersey and its Canadian tax return as "major" tax jurisdictions, as defined in FIN 48. The only periods subject to examination for the Company's federal return are the 2005 through 2006 tax years. The audit of the tax year 2004 has been completed with no adjustments proposed by the Internal Revenue Service. The periods subject to examination for the Company's state returns in New Jersey are years 2002 through 2006. The period subject to examination for the Company's Canadian tax returns are the years 2003 through 2006. The Company did not record a cumulative effect adjustment related to the adoption of FIN 48.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 ("SFAS 157"), "Fair Value Measurements," which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. Earlier adoption is permitted, provided the company has not yet issued financial statements, including for interim periods, for that fiscal year. We are currently evaluating the impact of SFAS 157, but do not expect the adoption of SFAS 157 to have a material impact on our consolidated financial position, results of operations or cash flows.

Certain Factors Affecting Operating Results

This report includes "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Statements in this report regarding future events or conditions, including statements regarding industry prospects and the Company's expected financial position, business and financing plans, are forward-looking statements. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. We strongly urge current and prospective investors to carefully consider the cautionary statements and risks contained in this report. Such risks include, but are not limited to, the continued acceptance of the Company's distribution channel by vendors and customers, the timely availability and acceptance of new products, contribution of key vendor relationships and support programs, as well as factors that affect the software industry in general.

The Company operates in a rapidly changing business, and new risk factors emerge from time to time. Management cannot predict every risk factor, nor can it assess the impact, if any, of all such risk factors on the Company's business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those projected in any forward-looking statements.

Accordingly, forward-looking statements should not be relied upon as a prediction of actual results and readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their dates. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

The statement concerning future sales and future gross profit margin are forward looking statements involving certain risks and uncertainties such as availability of products, product mix, market conditions and other factors, which could result in a fluctuation of sales below recent experience.

Stock Volatility.

The technology sector of the United States stock markets has experienced substantial volatility in recent periods. Numerous conditions, which impact the technology sector or the stock market in general or the Company in particular, whether or not such events relate to or reflect upon the Company's operating performance, could adversely affect the market price of the Company's Common Stock.

Furthermore, fluctuations in the Company's operating results, announcements regarding litigation, the loss of a significant vendor, increased competition, reduced vendor incentives and trade credit, higher postage and operating expenses, and other developments, could have a significant impact on the market price of the Company's common stock.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

In addition to its activities in the United States, the Company also conducts business in Canada. We are subject to general risks attendant to the conduct of business in Canada, including economic uncertainties and foreign government regulations. In addition, the Company's Canadian business is subject to changes in demand or pricing resulting from fluctuations in currency exchange rates or other factors.

The Company's \$9.4 million investments in marketable securities are only in highly liquid U.S. government securities. The remaining cash balance is invested in short-term savings accounts with our primary bank, JPMorgan Chase Bank. As such, the risk of significant changes in the value of our cash invested is minimal.

Item 4T. Controls and Procedures

Evaluation of Disclosure Controls and Procedures.

As required by Rule 13a-15(b) under the Exchange Act, our management carried out an evaluation of the effectiveness of the design and operation of the Company's "disclosure controls and procedures" as of September 30, 2007. This evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer (principal executive officer) and Chief Accounting Officer (principal financial officer). As defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, disclosure controls and procedures are controls and other procedures of the Company that are designed to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including our Chief Executive Officer and Chief Accounting Officer, as appropriate, to allow timely decisions regarding required disclosure.

Based upon that evaluation, our Chief Executive Officer and Chief Accounting Officer concluded that our disclosure controls and procedures were effective as of September 30, 2007. It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

Changes in Internal Control Over Financial Reporting. As required by Rule 13a-15(d) under the Exchange Act, our management, including our Chief Executive Officer and Chief Accounting Officer, also conducted an evaluation of our internal control over financial reporting to determine whether any change occurred during the quarter ended September 30, 2007, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. Based on that evaluation during the quarter ended September 30, 2007 there has been no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1A - Risk Factors

There have been no material changes in the Company's risk factors as disclosed in the Company's annual report on Form 10-K for t