

**QUARTERLY REPORT FOR
THREE MONTHS ENDED
MARCH 31, 2014**

LIVEWORLD, INC.

(Exact Name of issuer as specified in its charter)

Delaware
(State of Incorporation)

77-0426524
(IRS Employer Identification No.)

**4340 Stevens Creek Blvd. Suite 101
San Jose, California 95129**
(Address of principal executive offices)

(408) 871-5200
(Company's telephone number)

ISSUER'S EQUITY SECURITIES

COMMON STOCK

\$0.001 Par Value
100,000,000 Common Shares Authorized
33,321,634 Shares Issued and Outstanding as of June 25, 2014

INDEPENDENT ACCOUNTANTS' REVIEW REPORT

To the Board of Directors of
Liveworld, Inc.

We have reviewed the accompanying condensed balance sheet of Liveworld, Inc. (the "Company") as of March 31, 2014 and the related condensed statements of operations and cash flows for the three month periods ended March 31, 2014 and 2013. These interim condensed financial statements are the responsibility of the Company's management.

We conducted our review in accordance with standards established by the American Institute of Certified Public Accountants. A review of interim financial statements consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the United States, the objective of which is the expression of an opinion regarding the financial statement taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

/s/ Marcum LLP

Marcum LLP
San Francisco, CA
June 26, 2014

LIVEWORLD, INC.
CONDENSED BALANCE SHEETS
(In thousands, except share data)

	<u>March 31,</u> <u>2014</u>	<u>December 31,</u> <u>2013</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 4,317	\$ 4,413
Accounts receivable	365	488
Prepaid expenses	336	336
Total current assets	<u>5,018</u>	<u>5,237</u>
Property and equipment, net	239	257
Other assets	17	18
Total assets	<u>\$ 5,274</u>	<u>\$ 5,512</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 372	\$ 159
Accrued employee expenses	596	576
Other accrued liabilities	59	6
Deferred revenue	386	665
Total current liabilities	<u>1,413</u>	<u>1,406</u>
Stockholders' equity		
Common stock: \$0.001 par value, 100,000,000 shares authorized 33,321,634 issued and outstanding as of March 31, 2014 and December 31, 2013	33	33
Additional paid-in capital	141,510	141,448
Accumulated deficit	(137,682)	(137,375)
Total stockholders' equity	<u>3,861</u>	<u>4,106</u>
Total liabilities and stockholders' equity	<u>\$ 5,274</u>	<u>\$ 5,512</u>

See accompanying notes to the financial statements

LIVEWORLD, INC.
CONDENSED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Three Months Ended March 31,	
	2014	2013
Total revenues	\$ 3,311	\$ 3,874
Cost of revenues	1,411	1,362
Gross Margin	1,900	2,512
Operating Expense		
Product development	900	1,021
Sales and marketing	548	498
General and administrative	748	702
Total operating expense	2,196	2,221
Income / (loss) from operations	(296)	291
Income before tax	(296)	291
Provision for income taxes	11	6
Net income/ (loss)	(307)	285
Basic income/(loss) per share	\$ (0.01)	\$ 0.01
Shares used in computing basic income/(loss) per share	33,321,634	33,257,634
Diluted income/ (loss) per share	\$ (0.01)	\$ 0.01
Shares used in computing diluted income/ (loss) per share	33,321,634	41,707,087
Departmental allocation of stock-based compensation:		
Cost of revenues	\$ 11	\$ 8
Product development	19	12
Sales and marketing	12	5
General and administrative	20	8
Total stock-based compensation	\$ 62	\$ 33

See accompanying notes to the financial statements

LIVEWORLD, INC.
CONDENSED STATEMENTS OF CASH FLOWS
(In thousands)

	Three Months Ended	
	March 31,	
	2014	2013
	<u> </u>	<u> </u>
Cash flows from operating activities:		
Net income (loss)	\$ (307)	\$ 285
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation	39	29
Stock-based compensation	62	33
Changes in operating assets and liabilities:		
Accounts receivable	123	(1,030)
Other assets	1	33
Accounts payable	213	140
Accrued employee expenses and other liabilities	73	154
Deferred revenue	(279)	(502)
Net cash used in operating activities	<u>(75)</u>	<u>(858)</u>
Cash flows from investing activities:		
Purchase of property and equipment	(21)	(21)
Net cash used in investing activities	<u>(21)</u>	<u>(21)</u>
Change in cash and cash equivalents	(96)	(879)
Cash and cash equivalents, beginning of period	4,413	3,382
Cash and cash equivalents, end of period	<u>\$ 4,317</u>	<u>\$ 2,503</u>
Income taxes paid	<u>\$ 12</u>	<u>\$ 6</u>

See accompanying notes to the financial statements

1. ORGANIZATION

LiveWorld Incorporated (the “Company”) was incorporated in California on April 10, 1996 and reincorporated in Delaware in July 1999. In April 1999 the Company changed its name from LiveWorld Productions to Talk City, Inc. On May 8, 2001, the Company changed its name from Talk City, Inc. to LiveWorld, Inc. The Company’s principal business is social content marketing providing global brands with social media moderation, insight and engagement through combination of technology and human services. Our services and products include: Social Content Management System (SCMS) technology applications, moderation to protect brands, actionable insight to reveal what customers are thinking and what to do about it, and social engagement for marketing, service and support

2. INTERIM FINANCIAL STATEMENTS

The unaudited condensed interim financial information furnished herein reflects all adjustments, consisting only of normal recurring items, which in the opinion of management are necessary to fairly state our financial position, results from operations and cash flows for the dates and periods presented and to make such information presented not misleading. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted; nevertheless, the Company believes that the disclosures herein are adequate to make the information presented not misleading. These unaudited financial statements and related notes should be read in conjunction with our audited annual financial statements for the year ended December 31, 2013. Operating results for the three months ended March 31, 2014 are not necessarily indicative of the results that may be expected for future periods.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Use of Estimates – The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP). The preparation of the accompanying financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

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.

Fair Value Measurements – Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value should maximize the use of observable inputs and minimize the use of unobservable inputs. The accounting guidance for fair value establishes a three-level hierarchy for disclosure of fair value measurements, as follows:

Level 1 – Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date.

Level 2 – Inputs (other than quoted market prices included in Level 1) that are either directly or indirectly observable, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the instrument’s anticipated life.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The carrying values of certain financial instruments of the Company, such as cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate fair value due to their relatively short maturities.

Concentrations of Credit Risk – Financial instruments that potentially subject the Company to a concentration of credit risk consist primarily of cash and cash equivalents. Bank deposits are held with two financial institutions having strong credit ratings and these deposits may at times be in excess of insured limits. The Company is exposed to credit risk in the event of a default by the financial institutions holding its cash and cash equivalents.

The Company’s accounts receivable are derived primarily from customers who have signed contracts with the Company, for the Company to provide services to the customer. The Company performs ongoing credit evaluations of its customers, does not require collateral and maintains allowances for potential credit losses when deemed necessary.

Allowances for Doubtful Accounts – The Company did not record an allowance for doubtful accounts as of March 31, 2014 and December 31, 2013. The Company maintains an allowance for doubtful accounts for estimated losses that may arise if any of its customers are unlikely to make required payments. Management specifically analyzes the age of customer balances, historical bad debt experience, customer credit-worthiness, and changes in customer payment terms when making estimates of the uncollectibility of the Company's accounts receivable balances. If the Company determines that the financial condition of any of its customers deteriorated, whether due to customer specific or general economic issues, an increase in the allowance will be made. Accounts receivable are written off when all collection attempts have failed.

Property and Equipment – Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is calculated using the straight-line method over the estimated useful lives of the respective assets of three years for computer equipment, software, and for furniture and office equipment. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful lives of the respective assets.

Revenues – The Company recognizes revenues when the following criteria have been met: persuasive evidence of an arrangement exists, the fees are fixed or determinable, no obligations remain, and collection of the related receivable is reasonably assured.

Revenues from service development and community set-up activities are deferred and are recognized ratably over the related development and service portions of the contract. Revenues from on-line community hosting, on-line community management, moderation services, and consulting are recognized as the services are provided.

Cost of Revenues – Cost of revenues is comprised of direct costs associated with the sales of our Strategy, Engagement, Moderation and Insight software and services to clients; the expenses associated with the development, set-up and operation of our services, including expenses associated with server costs for managing the software tools, license fees for our platform; and the cost of providing moderators and any strategic consulting services the client may request from us. These expenses consist primarily of salaries, payroll taxes, benefits and related expenditures for moderation and consulting services, as well as, software license fees, hardware costs.

Deferred Revenues – Deferred revenues are the amounts associated with the initial service development and set-up of a community for our clients and/or prepayments by customers. These service development and set-up revenues are paid upfront but recognized ratably as the development and operational service contract is recognized.

Product Development – Product development expenses consist primarily of salaries, payroll taxes, benefits and related expenditures for technology, software development, project management and support personnel. Costs related to the development of new products and enhancements to existing products are charged to operations as incurred. Software development costs are required to be capitalized when a product's technological feasibility has been established by completion of a working model of the product. To date, completion of a working model of the Company's products and general release have substantially coincided. As a result, the Company has not capitalized any software development costs because such costs have not been significant.

Sales and Marketing – Sales and marketing expenses consist primarily of salaries, payroll taxes, benefits and related expenditures for sales and marketing.

General and Administrative – General and administrative expenses are the combined expenses of the operations, facilities, finance, human resources, legal and other administrative functions. The expenses associated with these functions consist primarily of salaries, payroll taxes, benefits, professional fees, and related expenditures for our overall management and administration.

Stock-Based Compensation – The Company accounts for its stock-based compensation expense based on the fair value of the stock-based awards that are ultimately expected to vest. The fair value of an employee stock option grant is estimated on the date of grant using the Black-Scholes option pricing model, and is recognized as expense on a straight-line basis over the employee's requisite service period (generally the vesting period), net of estimated forfeitures. Forfeitures are estimated at the time of grant and revised in subsequent periods if actual forfeitures differ from the prior estimates.

The Company records the expense attributed to non-employee services paid with stock-based awards based on the estimated fair value of the awards determined using the Black-Scholes option pricing model. The measurement of stock-based compensation for non-employees is subject to re-measurement as the options vest, and the expense is recognized over the period during which services are received.

Income Taxes – The Company uses the liability method to account for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between the financial statement carrying amounts of existing assets and liabilities and their tax bases. Deferred tax assets and liabilities are measured using enacted tax rates applied to taxable income in the years in which those temporary differences are expected to be recovered or settled. A valuation allowance is established when necessary to reduce deferred tax assets to the amount expected to be realized. Financial statement effects of uncertain tax positions are recognized when it is more-likely-than-not, based

on the technical merits of the position, that it will be sustained upon examination. Interest and penalties related to unrecognized tax benefits are included within the provision for income tax.

Comprehensive Income (Loss) – Comprehensive income (loss) is defined as a change in equity of a business enterprise during a period, resulting from transactions from non-owner sources. There have been no items qualifying as comprehensive income (loss) and, therefore, for all periods presented, the Company's comprehensive income (loss) was the same as its reported net income (loss).

Earnings Per Share — Basic income (loss) per share is computed using the net income (loss) and the weighted average number of common shares outstanding during the period. Diluted income (loss) per share is computed using the net income and the weighted average number of common shares and dilutive potential common shares outstanding during the period. Potential dilutive common shares include outstanding stock options and warrants. The dilutive effect of outstanding stock options and warrants is computed using the treasury stock method. For the three month period ended March 31, 2014, diluted net loss per common share was the same as basic net loss per common share since the effect of inclusion of potentially dilutive common stock equivalents would have an antidilutive impact due to the loss reported. For the three month periods ended March 31, 2014 and 2013, options and warrants aggregating 21,423,691 and 16,267,678 common share equivalents, respectively, prior to the application of the treasury stock method are not included in the calculation of diluted net income (loss) per share as they are anti-dilutive.

The following table sets forth the computation of basic and diluted net income or loss attributable to common stockholders:

In thousands, except per share amounts	Three Months Ended March 31,	
	2014	2013
Numerator:		
Net income/(loss) attributable to common Stockholders	\$ (307)	\$ 285
Denominator:		
Weighted-average shares used to compute basic EPS	33,322	33,258
Effect of dilutive securities:		
Diluted common shares	----	8,449
Weighted-average shares used to compute diluted EPS	33,322	41,707
Net earnings per share:		
Basic	\$ (0.01)	\$ 0.01
Diluted	\$ (0.01)	\$ 0.01

4. STOCK-BASED COMPENSATION

The 1996 Stock Option Plan (“1996 Plan”) provides for stock options to be granted to employees, independent contractors, officers, and directors. Prior to 2004, options were generally granted at an exercise price which approximated eighty-five percent (85%) to one hundred percent (100%) of the estimated fair value per share at the date of grant, as determined by our Board of Directors. Since 2004, options have generally been granted at one hundred percent (100%) of their estimated fair market value per share at the date of grant, as determined by our Board of Directors. All options issued under the 1996 Plan and the 2007 Stock Option Plan (“2007 Plan”) have a term of ten (10) years, and generally have a vesting schedule such that they vest ratably over four (4) years, twenty-five percent (25%) one (1) year after the grant date and the remainder at a rate of 1/36 per month thereafter. The 1996 Plan expired in October of 2006 and was replaced by our 2007 Plan.

Determining Fair Value

Valuation Method — The Company estimates the fair value of stock options granted using the Black-Scholes option-pricing model and a single option award approach.

Expected Term — The expected term of our stock options has been determined utilizing the “simplified” method for awards that qualify as “plain vanilla” options. The expected term of stock options granted to non-employees is equal to the contractual term of the option award.

Expected Volatility — A volatility rate was used as an estimate of the expected future volatility of the Company’s common stock. The Company estimated the expected stock volatility based on the historical volatility of publicly traded peer companies for periods that are commensurate with the expected term (in years).

Risk-Free Interest Rate — The risk-free interest rate used in the Black-Scholes valuation method is based on the implied yield currently available on U.S. Treasury securities with an equivalent remaining term.

Expected Dividend — No dividends are expected to be paid.

Estimated Forfeitures — When estimating forfeitures, the Company considers voluntary termination behavior as well as analysis of actual option forfeitures.

The Company estimated the fair value of its stock options using the Black-Scholes option-pricing model, by using the following assumptions for the options granted during the three months ended March 31, 2014:

	Stock Options
Dividend yield	0%
Expected volatility	79%
Risk-free interest rate	0.23%
Estimated term	7 Years

A summary of the stock option activity is as follows:

	Shares Available for Grant	Options Outstanding	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Balance as of December 31, 2013	12,058,657	17,395,412	\$ 0.17		
Granted	(620,000)	620,000	\$ 0.25		
Forfeited	435,903	(435,903)	\$ 0.24		
Exercised	----	----	----		
Balance as of March 31, 2014	<u>11,874,560</u>	<u>17,579,509</u>	<u>\$ 0.17</u>	<u>6.3</u>	<u>\$1,924</u>

The aggregate intrinsic value in the table above represents the difference between the exercise price of the underlying awards and the quoted price of our common stock for the options that were in-the-money as of March 31, 2014. As of March 31, 2014, total unrecognized compensation cost related to unvested stock options was approximately \$704,000. The cost is expected to be recognized over a weighted average period of 2.16 years.

5. PROPERTY AND EQUIPMENT

Property, furniture and equipment consisted of the following items:

(\$ in thousands)	March 31, 2014	December 31, 2013
Computer equipment	\$ 1,819	\$ 1,798
Software	1,211	1,211
Furniture and fixtures	31	31
Leasehold improvements	23	23
	<u>3,084</u>	<u>3,063</u>
Accumulated depreciation	(2,845)	(2,806)
Property, furniture and equipment, net	<u>\$ 239</u>	<u>\$ 257</u>

Depreciation expense was approximately \$39,000 and \$29,000 for the three months ended March 31, 2014 and 2013, respectively.

Management's Discussion and Analysis of Financial Condition and Results of Operation (unaudited)

Special Note Regarding Forward-Looking Statements

This report contains forward-looking statements. All statements other than statements of historical fact contained in this document are forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as "may", "will", "should", "expects", "plans", "anticipates", "believes", "estimates", "predicts", "potential" or "continue" or the negative of these terms or other comparable terminology. These statements are only current predictions and are subject to known and unknown risks, uncertainties, and other factors that may cause our or our industry's actual results, levels of activity, performance, or achievements to be materially different from those anticipated by the forward-looking statements.

The following discussion and analysis should be read in conjunction with our financial statements and the notes to those statements included elsewhere in this quarterly report. This discussion contains forward-looking statements reflecting our current expectations that involve risks and uncertainties. Actual results may differ materially from those discussed in these forward-looking statements due to a number of factors, including those set forth in the section entitled "Risk Factors" contained in our 2007 Form 10-K.

Backlog

We maintain a positive outlook for 2014, and our backlog is approximately \$9.0 million for the remainder of the year.

Overview

We provide our global brand clients with social content marketing solutions including strategy, engagement, moderation, and insight through a combination of software and human services. We bring a human touch scaled by technology that creates value out of user content and provides big cost savings. By providing software and services, LiveWorld delivers a full range of social media solutions. 1) Strategy to connect business goals to social media and deploy effective programs 2) Engagement for marketing, service & support. 3) Moderation to protect brands, and 4) Actionable insights to tell brands what their customers think and what to do about it. Our clients use these solutions to improve their relationship marketing, customer support and market learning.

Social Strategy Solution: LiveWorld strategic work enables brands to connect business goals to social media programs including providing social audits and market analysis, defining a social brand identity, and developing effective implementation programs. Our team of strategists range in experience from 10 to 30 years in the online community-social media space and have developed hundreds of programs for global brands.

Social Engagement Solution: The LiveWorld social engagement solutions stimulate the attention of a brand's customers, guides their emotional experiences to care about the brand, remember it, come back for more, and bring their friends with them. The solution consists of conversation content programming plans, social media crisis plans, online events, creative concepts, content, community management, and day to day online engagement. Our Social Content Marketing Software (SCMS) enables human social specialists to respond to customers with an organic feel across social channels, while supporting brand content guidelines.

Social Content Moderation Solution: The LiveWorld content moderation solution protects the brand and creates a positive environment for customers. Our Social Content Marketing Software (SCMS) supports a trained team of human moderators to accept, reject, and escalate content in context, at an affordable cost. The LiveWorld moderation team creates an integrated workflow to cover thousands of pages simultaneously and at rates that are usually 2x to 10x faster than moderation without our tools. Under optimal conditions we are able to moderate up to 2,000 actions/ hour/moderator (800-1,200 typical) and provide our clients with a scalable, flexible service which gives them meaningful insight to their customers. We also provide moderation services on 3rd party applications and platforms with any existing tools that come with those platforms.

Social Insight Solution: The LiveWorld social insight solution enables brands to understand what their customers think and what to do about it. Our Active Listening solutions, monitor the social web and provide actionable insights based on conversational and metrics analysis. These services are available with popular 3rd party listening and analytics tools and/or with LiveWorld software. Our insight agents review and tag content at high speed, maintaining quality by considering the content in context. Using our culture-tone-engagement framework, social strategists evaluate content and conversational dynamics to produce deep insights and actionable recommendations. Our Social Content Marketing Software (SCMS), is designed to engage and scale human review and analysis at every level — helping brands to define what social media content to target to affect which business decisions.

Total Revenues

The Company recognizes revenues when the following criteria have been met: persuasive evidence of an arrangement exists, the fees are fixed or determinable, no obligations remain, and collection of the related receivable is reasonably assured.

Revenues from service development and community set-up activities are deferred and are recognized ratably over the related development and service portions of the contract. Revenues from on-line community hosting, on-line community management, moderation services, and consulting are recognized as the services are provided.

Cost of Revenues

Cost of revenues is comprised of direct costs associated with the sales of our Strategy, Engagement, Moderation and Insight software and services to clients; the expenses associated with the development, set-up and operation of our services, including expenses associated with server costs for managing the software tools, license fees for our platform; and the cost of providing moderators and any strategic consulting services the client may request from us. These expenses consist primarily of salaries, payroll taxes, benefits and related expenditures for moderation and consulting services, as well as, software license fees, hardware costs.

Operating Expenses

Product Development. Product development expenses consist primarily of salaries, payroll taxes, benefits and related expenditures for technology, software development, project management and support personnel. Costs related to the development of new products and enhancements to existing products are charged to operations as incurred.

Sales and Marketing. Sales and marketing expenses consist primarily of salaries, payroll taxes, benefits and related expenditures for sales and marketing.

General and Administrative. General and administrative expenses are the consolidated expenses of the operations, facilities, finance, human resources, legal and other administrative functions. The expenses associated with these functions consist primarily of salaries, payroll taxes, benefits, professional fees, and related expenditures for our overall management and administration.

Stock-Based Compensation. Stock-based compensation expenses include amounts related to the grant of options and warrants to employees and non-employee service providers.

Results From Operations

The following table sets forth our historical operating results as a percentage of total revenues for the periods indicated:

LIVEWORLD, INC. STATEMENT OF OPERATIONS

	Three Months Ended March 31,	
	2014	2013
Total revenues	100%	100%
Cost of revenues	43	35
Gross Margin	57	65
Operating Expense		
Product development	27	26
Sales and marketing	17	13
General and administrative	23	18
Total operating expense	67	57
Income (loss) from operations	(9%)	8%

Three Months Ended March 31, 2014 and 2013

Total Revenues

Our revenues for the three months ended March 31, 2014 were approximately \$3.3 million, as compared to approximately \$3.9 million for the three months ended March 31, 2013. This was a decrease of approximately \$563,000 or 15% period-over-period.

For the three months ended March 31, 2014, revenues from Walmart and Procter and Gamble comprised approximately 66% of our total revenues while all other clients represented approximately 34% of our total revenues. This compares to the three months ended March 31, 2013 where revenues from eBay and Walmart comprised approximately 62% of our total revenues and all other clients represented approximately 38% of total revenues.

Cost of Revenues

Cost of revenues were approximately \$1.4 million, or 43% of total revenues for the three months ended March 31, 2014, and approximately \$1.4 million or 35% of total revenues for the three months ended March 31, 2013. This represented an increase of approximately \$49,000 or 4% period-over-period. This increase was due primarily to a boost in demand for our moderation services.

Operating Expenses

Product Development. Expenditures for product development were approximately \$900,000, or 27% of total revenues for the three months ended March 31, 2014, and approximately \$1.0 million, or 26% of total revenues for the three months ended March 31, 2013. This represented a decrease in absolute dollars of approximately \$121,000, or 12% period-over-period.

The majority of product development costs are personnel related. We believe product development expenditures will increase in absolute dollars in 2014. We are committed to our product development efforts and will continue to invest in product development programs. Such efforts may not result in additional new services and any new services may not generate sufficient revenues, if any, to offset expenses.

Sales and Marketing. Sales and marketing costs were approximately \$548,000, or 17% of total revenues for the three months ended March 31, 2014, and approximately \$498,000, or 13% for the three months ended March 31, 2013 representing an increase in absolute dollars of approximately \$50,000 or 10% period-over-period.

We expect sales and marketing costs to increase as we expand our sales and marketing efforts to new clients. In addition, if our product development efforts are successful and new products or services are created, we will incur increased sales and marketing expense to promote these products or services to new and existing clients.

General and Administrative. General and administrative expenses were approximately \$748,000, or 23% of total revenues for the three months ended March 31, 2014, and approximately \$702,000, or 18% of total revenues for the three months ended March 31, 2013.

Financial Condition, Liquidity and Capital Resources

For the three months ended March 31, 2014 we had negative total cash flows of approximately \$96,000 while for the three months ended March 31, 2013 we had negative total cash flows of approximately \$879,000. The primary reason for the negative cash flows in the first quarter of 2014 were delays in obtaining purchase orders for 2014 renewals.

We ended the three months ended March 31, 2014 with approximately \$4.3 million in cash, as compared to the approximately \$4.4 million in cash at the end of 2013.

We believe that the combination of cash balances, cash flow from operations, and available credit facilities will be sufficient to satisfy cash needs for the current level of operations and planned operations for the foreseeable future.

Our total assets were approximately \$5.3 million as of March 31, 2014, and approximately \$5.5 million as of December 31, 2013. This represented a decrease of approximately \$238,000 of total assets, or 4%, when compared to the total assets as of December 31, 2013.

Accounts receivable was approximately \$365,000 as of March 31, 2014 which was a decrease of approximately \$123,000 or 25% from the accounts receivable balance of approximately \$488,000 as of December 31, 2013. Accounts receivable balances are expected to fluctuate with the levels of new client acquisition and enhancement activity and the timing of billings and collections.

Property and equipment decreased approximately \$18,000 to approximately \$239,000 as of March 31, 2014 from approximately \$257,000 as of December 31, 2013.

As of March 31, 2014, our current assets, which are made up of cash and cash equivalents, accounts receivable, and prepaid expenses were approximately \$5.0 million while our current liabilities, which are made up of our accounts payable and accrued liabilities were approximately \$1.4 million. This represented a positive working capital position of approximately \$3.6 million, which was a decrease of approximately \$226,000 from the period ended December 31, 2013.

In the future, we may strategically seek to take advantage of opportunities in the equity and capital markets to raise additional funds in order to take advantage of opportunities that may become available to us, including expansion of operating activities and acquisition of businesses, products or technologies, or otherwise to respond to competitive pressures. Capital scenarios may include but are not limited to public stock issuance, private investment rounds, merger or acquisition and/or privatization. There can be no assurance that we will be able to raise additional capital on favorable terms or at all.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, investments in special purpose entities or undisclosed borrowings or debt. Additionally, we are not a party to any derivative contracts or synthetic leases.