INTERNATIONAL MICROCOMPUTER SOFTWARE INC /CA/
Form 10QSB
February 11, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549
FORM 10-QSB

[X] Quarterly Report Pursuant to Section 13 or 15(d) of the securities Exchange Act of 1934

For the quarterly period ended DECEMBER 31, 2003

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

For the transition period from: _____ to _____

Commission File Number 0-15949

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC.
(Exact name of Small business issuer in its charter)

CALIFORNIA	94-2862863
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identificati
100 ROWLAND WAY, SUITE 300, NOVATO, CALIFORNIA	94945
(Address of principal executive offices)	(Zip code)

(415) 878-4000
Issuer's telephone number

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES /X/ NO /_/

As of FEBRUARY 6, 2004, 23,447,368 Shares of Issuer's common stock, no par value, were outstanding.

Transitional Small Business Disclosure Format: YES /_/ NO /X/

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC.
AND SUBSIDIARIES

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PART I - FINANCIAL INFORMATION

ITEM1- CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	(UNAUDITED) DECEMBER 31, 2003	JUNE 30, 2003
ASSETS		
Current assets:		
Cash and cash equivalents	$ 5,249	$ 10,399
Investment in marketable securities	197	--
Receivables, less allowances for doubtful accounts, discounts and returns of $630 and $445	1,123	734
Receivables, other (related to discontinued operations)	1,000	--
Inventories	512	268
Other current assets	484	240
TOTAL CURRENT ASSETS	8,565	11,641
FIXED ASSETS, NET	271	85
Intangible assets		
Capitalized software, net	778	87
Domain names, net	1,419	4
Distribution rights, net	--	36
Capitalized customer lists	128	--

Goodwill	608	179
TOTAL INTANGIBLE ASSETS	2,933	306
Other assets		
Note receivable from related party	350	--
Investment in securities	1,138	998
Assets related to discontinued operations	1,300	1,300
TOTAL OTHER ASSETS	2,788	2,298
TOTAL ASSETS	$ 14,557	$ 14,330
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term debt	786	304
Trade accounts payable	871	564
Income tax payable	--	271
Accrued and other liabilities	610	1,541
Deferred revenue	241	305
TOTAL CURRENT LIABILITIES	2,508	2,985
Liabilities related to discontinued operations	84	84
Long-term debt and other obligations	181	--
TOTAL LIABILITIES	2,773	3,069
Shareholders' equity:		
Common stock, no par value; 300,000,000 authorized; Issued and outstanding 23,347,368 and 22,818,232 shares	36,099	35,546
Accumulated deficit	(24,221)	(24,223)
Accumulated other comprehensive loss	(94)	(62)
TOTAL SHAREHOLDERS' EQUITY	11,784	11,261
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 14,557	$ 14,330

See Notes to Condensed Consolidated Financial Statements

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INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)
(In thousands, except per share amounts)
(Unaudited)

	THREE MONTHS ENDED DECEMBER 31,	
	2003	2002

Net revenues	$ 2,674	$ 2,466
Product costs	793	1,075
GROSS MARGIN	1,881	1,391
Costs and expenses:		
Sales and marketing	1,065	836
General and administrative	991	499
Research and development	531	445
TOTAL OPERATING EXPENSES	2,587	1,780
OPERATING LOSS	(706)	(389)
Other income and (expense):		
Interest and other, net	60	(127)
Unrealized gain on marketable securities	47	--
Gain on liquidation of foreign subsidiaries	--	--
Gain (loss) on extinguishment of debt	(5)	257
LOSS BEFORE INCOME TAX	(604)	(259)
Income tax benefit	6	--
LOSS FROM CONTINUING OPERATIONS	(598)	(259)
Gain from the sale of discontinued operations	1,000	--
Income from discontinued operations, net of income tax	--	208
NET INCOME (LOSS)	$ 402	($ 51)
Other comprehensive income (loss), net of tax:		
Foreign currency translation, net of tax	(28)	(6)
OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX	$ 374	($ 57)
BASIC EARNINGS (LOSS) PER SHARE		
Loss per share from continuing operations	($ 0.02)	($ 0.01)
Gain from the sale of discontinued operations	$ 0.04	--
Income from discontinued operations, net of income tax	--	$ 0.01
Earnings (loss) per share	$ 0.02	$ 0.00
DILUTED EARNINGS (LOSS) PER SHARE		
Loss per share from continuing operations	($ 0.02)	($ 0.01)
Gain from the sale of discontinued operations	$ 0.04	--
Income from discontinued operations, net of income tax	--	$ 0.01
Earnings (loss) per share	$ 0.02	$ 0.00
Shares used in computing basic earnings (loss) per share information	23,268	22,792
Shares used in computing diluted earnings (loss) per share information	23,268	22,792

See Notes to Condensed Consolidated Financial Statements

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
Six Months ended December 31, 2003
(In thousands)
(Unaudited)

	COMMON STOCK		
	SHARES	AMOUNT	ACCUMULATED DEFICIT
BALANCE AT JUNE 30, 2003	22,818	$35,546	($24,223)
Issuance of common stock related to:			
Warrants exercised	305	65	
Stock options exercised	124	71	
Acquisitions	100	92	
Issuance of warrants related to:			
Consulting services rendered		248	
Acquisitions		59	
Issuance of stock options related to:			
Consulting services rendered		7	
Variable accounting adjustment related to stock options previously issued		11	
Net income			2
Comprehensive loss			
BALANCE AT DECEMBER 31, 2003	23,347	$36,099	($24,221)

See Notes to Condensed Consolidated Financial Statements

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INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	SIX MONTHS ENDED DECEMBER 31	
	2003	2002
Cash flows from operating activities:		
NET CASH USED BY OPERATING ACTIVITIES	($ 2,507)	($ 694)
Cash flows from investing activities:		
Acquisition of product lines	(1,525)	--

Acquisition of business	(257)	--
Loan to related party	(350)	--
Investment in marketable securities	(160)	--
Purchase of equipment and furniture	(174)	(11)
Purchase of software	(13)	(14)
Cash used by discontinued operations in investing activities	--	(154)
NET CASH USED BY INVESTING ACTIVITIES	(2,479)	(179)
Cash flows from financing activities:		
Settlement of note payable (Imageline)	(160)	--
Note borrowings	--	321
Note repayments	(109)	(558)
Warrants exercised	65	--
Options exercised	71	--
Proceeds from issuance of common stock	--	1
Repayment of capital lease obligations	--	(76)
Cash used by discontinued operations in financing activities	--	(95)
NET CASH USED BY FINANCING ACTIVITIES	(133)	(407)
Effect of exchange rate change on cash and cash equivalents	(31)	(2)
Net decrease in cash and cash equivalents	(5,150)	(1,282)
Cash and cash equivalents at beginning of period	10,399	2,455
CASH AND CASH EQUIVALENTS AT END OF THE PERIOD	$ 5,249	$ 1,173

See Notes to Condensed Consolidated Financial Statements

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The interim condensed consolidated financial statements have been prepared from the records of International Microcomputer Software, Inc. and Subsidiaries ("IMSI") without audit. All significant inter-company balances and transactions have been eliminated in consolidation. In the opinion of management, all adjustments, which consist of only normal recurring adjustments, to present fairly the financial position at December 31, 2003 and the results of operations and cash flows for the three and six months ended December 31, 2003 and 2002, have been made. The interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in our Annual Report on Form 10-KSB for the fiscal year ended June 30, 2003. The results of operations for the three and six months ended December 31, 2003 are not necessarily indicative of the results to be expected for any other interim period or for the full year.

2. DISCONTINUED OPERATIONS

As previously disclosed in our annual report on Form 10-KSB for the fiscal year ended June 30, 2003, we sold ArtToday, Inc ("ArtToday"), our wholly-owned subsidiary based in Arizona, to Jupitermedia Corporation ("Jupiter") in June 2003. Under Generally Accepted Accounting Principles ("GAAP") in the United

States, ArtToday's operating results for the three and six months ended December 31, 2002, have been accounted for as discontinued operations.

Reclassifications have been made to the amounts reported in fiscal 2003 to conform to the current year presentation. The amounts reported for fiscal 2003 present the results of operations for ArtToday as discontinued operations due to the sale of ArtToday on June 30, 2003.

During the quarter ended December 31, 2003, we recorded a gain of $1.0 Million from the sale of discontinued operations representing the successful achievement of the first earnout from the sale of ArtToday. This earnout was contingent on ArtToday reaching certain revenue milestones. We have received confirmation from Jupiter that the full amount of the $1.0 Million earnout was earned and will be paid per the stock purchase agreement by February 14, 2004.

3. RECLASSIFICATIONS

Effective for the quarter ended December 31, 2003, we revised our accounting treatment with regard to fees paid to our third party E-commerce solution provider, whereby we now record them as sales and marketing expenses as compared to our prior treatment of them as an offset to revenue. The effect of this reclassification, as of December 31, 2003, was to increase revenues and sales and marketing expense by $138,000 and $187,000 for the three and six months ended December 31, 2003. In order to conform our prior year's results to this revised presentation for the three and six months ended December 31, 2002, we have increased revenues and sales and marketing expense by $77,000 and $155,000, respectively.

4. PRODUCT LINE AND OTHER ACQUISITIONS

PLANWORKS

On November 17, 2003, we acquired Planworks L.L.C. ("Planworks"), a leading online provider of house plans. Planworks operates the houseplanguys.com website that contains an extensive library of over 11,000 unique house plans and has more than 25,000 members. We also acquired ten other domain names which will be used to assist individuals and designers looking for house plans and related products, further strengthening the IMSI network of online design and content commerce sites. The total consideration for the acquisition included the following:

- Cash: $275,000 of which $260,000 was paid upon closing with the remaining $15,000 balance to be held in an escrow account for a period of eight months.

- 85,000 restricted shares of IMSI common stock priced as of the acquisition date or $1.16 per share.

CADSYMBOL ACQUISITION

On November 6, 2003, we entered into an asset purchase agreement with Assisto GmbH ("Assisto"), a German company, whereby we acquired title and interest in certain tangible and intangible assets of Assisto. The assets included certain CAD symbol content, custom developed software and all related assets including inventory, web sites and domain names.

The total purchase price of approximately $372,000 will be paid according to the following schedule:

- Approximately $172,000 at closing;
- Approximately $200,000 to be held in escrow and released over the next fifteen months.

In addition, we granted to Ane Gyldholm and Michael Heckmann, principals of Assisto, warrants to each purchase twenty thousand (20,000) shares of IMSI's common stock at any time within the three year period following the closing at an exercise price of $1.21, which was the price of IMSI's common stock on the closing date.

CADSYMBOLS ACQUISITION

On October 27, 2003, we entered into an asset license and purchase agreement with Cardiff Consultants, Limited, a New York corporation ("Cardiff"), whereby we acquired from Cardiff the exclusive, non-transferable right to use the cadsymbols.com and cadsymbols.net domain names and trademarks until December 31, 2006, when Cardiff is to assign the domain names and trademark to us subject to our payment of all amounts due Cardiff. The total consideration for the acquisition ($845,000) is comprised of the following:

- Three Hundred Thirty-Five Thousand Dollars ($335,000) upon the execution of the agreement;
- Two Hundred Fifty-Five Thousand Dollars ($255,000) in two payments to be paid over the next nine months
- Royalty payments to Cardiff equal to two percent (2.0%) of the net revenues, subject to certain minimums for the next three years based on sales generated by the websites.

In addition, we granted to Cardiff a warrant to purchase twenty-five thousand (25,000) shares of IMSI's common stock at any time within the three-year period following the execution of the agreement at $1.14 per share.

Upon the execution of the agreement, Cardiff deposited in an escrow account the assignment agreement of each domain name, and the assignment agreement of the trademark. The escrow agreement calls for release of the assignment documents to us on September 30, 2006 subject to the cumulative payment to Cardiff of all amounts due.

CADKEY ACQUISITION TERMINATION

As previously disclosed, on August 22, 2003, we entered into an agreement with CADKEY Corporation ("CADKEY") a Massachusetts corporation to purchase substantially all of its assets. The proposed purchase price was $2,500,000 and the assumption of CADKEY customer obligations. The acquisition was conditioned upon court approval pursuant to Section 363 of the U.S. Bankruptcy Code after CADKEY filed a voluntary petition under Chapter 11 of the Bankruptcy Code on August 22, 2003 in the U.S. Bankruptcy Court in Worcester, Massachusetts.

On October 27, 2003, we terminated our bid to acquire substantially all of the assets of CADKEY through an auction sale. As a result of the termination, we received a break up fee of $45,000 which was recorded as a reduction of legal expense and were reimbursed for $225,000 of professional fees advanced to CADKEY in addition to the $250,000 that was initially held in escrow. These amounts were initially recorded as short-term assets in the "Other current assets" account.

CADALOG

On September 12, 2003, we acquired from CADalog, Inc, CADalog.com, a network of websites that offers one of the largest mechanical parts symbols libraries on-line and allows members access to over 8 million 2D and 3D hardware component symbols. The acquisition also included the purchase of CADalog, Inc.'s Partsxl.com, Partswork.com and 3DModelsharing.com websites. This acquisition gives us the opportunity to sell additional CAD content and software plug-ins. The total consideration for the acquisition was $295,000. A payment of $250,000 was made on September 19, 2003 and the remaining $45,000 will be held in an escrow account with $15,000 to be released to the seller ninety days after the closing date, and the remaining $30,000 to be released after a period of twelve months. The escrow balance of $45,000 was fully funded on October 8, 2003.

DESIGNCAD

On July 28, 2003, we entered into an agreement to purchase the tangible and intangible assets of Upperspace Corporation ("Upperspace"), an Oklahoma corporation, constituting its DesignCAD line of products, several learning aids, and various smaller design programs.

The purchase price included the following consideration:

- $700,000 cash (of which $100,000 is being held in an escrow account for a period of twelve months)
- $300,000, 5% simple interest, promissory note payable 12 months from the date of closing
- An earn-out based on net revenue that could result in an additional $300,000 during the next three fiscal years
- A license pursuant to which Upperspace shall act for a period as the exclusive distributor of the purchased products to retail outlets, and a non-exclusive reseller of the product through direct sales channels such as the internet, email, telephone and fax.

The table below documents the components of consideration paid for each acquisition completed in the three and six months ended December 31, 2003 detailed above and the allocation of that consideration to the tangible and intangible assets acquired.

	PLANWORKS	CADSYMBOL	CADSYMBOLS
DATE TRANSACTION CLOSED:	NOVEMBER 17, 2003	NOVEMBER 6, 2003	OCTOBER 27, 2003
CONSIDERATION			
Cash	$ 260	$ 171	$ 335
Less: Cash on hand	(16)	-	-

Escrow	-	170	-
Stock	77	-	-
Warrants	-	30	18
Notes payable	14	-	474
Liabilities assumed	23	-	-
Transaction fees	20	1	3
TOTAL CONSIDERATION	$ 378	$ 372	$ 830
ASSET ALLOCATION			
Tangible Assets			
Inventory	-	-	-
Marketing materials	-	-	-
Prepaid expenses	1	-	-
Computer hardware	-	12	-
Computer software	-	-	-
TOTAL TANGIBLE ASSETS	$ 1	$ 12	$ -
Intangible Assets			
Capitalized software / content	-	180	-
Websites and associated domain names	315	180	830
Customer list	33	-	-
Goodwill	29	-	-
TOTAL INTANGIBLE ASSETS	$ 377	$ 360	$ 830
TOTAL ASSETS ALLOCATED	$ 378	$ 372	$ 830

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5. NOTE PAYABLE TO IMAGELINE

On July 7, 2003, we repaid the note payable to Imageline in the amount of $160,000 representing the final payment in connection with our mutual settlement as previously disclosed in our annual report on Form 10-KSB for the fiscal year ended June 30, 2003.

6. NOTE RECEIVABLE FROM RELATED PARTY - DCDC 15% NOTE

On September 18, 2003, we entered into a 15% one-year note with Digital Creative Development Corporation ("DCDC") whereby we extended a loan to DCDC in the amount of $350,000. The note is due, with interest, on September 18, 2004. The note is secured by 400,000 shares of IMSI's stock held by DCDC. The agreement also calls for DCDC not to sell any other IMSI common stock which it holds, with the exception of private sales of IMSI common stock, prior to February 15, 2004.

Concurrent with this note, DCDC repaid the entire principal portion of a $50,000 note, made in favor of IMSI on February 25, 2003. That note, due on February 25, 2004, was unsecured and carried a 4% interest rate. This note had been previously recorded as a fully reserved receivable as it was unsecured. The reversal of the reserve upon the repayment of this note was consequently accounted for as other income during the quarter ended September 30, 2003. The interest payable, amounting to $1,162, is still outstanding as of the filing and is due and payable on February 18, 2004.

7. SEGMENT INFORMATION

We have three reportable operating segments based on the sales market. Two of these are geographic segments and generate revenues and incur expenses related to the sale of our PC productivity software. The third segment comprises the revenues and expenses related to Keynomics, our business applications subsidiary which provides ergonomic and keyboard training for worker-enhanced safety, productivity and ergonomic compliance improvements through its proprietary software system, "The KeySoft Performance System".

The following table details segment information (in thousands). The foreign segment refers to the operations of our German and Australian wholly owned subsidiaries, IMSI GmbH and IMSI Australia PTY Ltd.

QUARTER ENDED DECEMBER 31, 2003	KEYNOMICS	NORTH AMERICA	OTHER FORE
Net Revenues	$319	2,225	13
Operating income (loss)	(58)	(672)	2
Identifiable assets	223	15,575	37
QUARTER ENDED DECEMBER 31, 2002			
Net Revenues	$447	$1, 902	$11
Operating income (loss)	58	(400)	(47
Identifiable assets	627	2,972	30
SIX MONTHS ENDED DECEMBER 31, 2003			
Net Revenues	$478	$3,685	$29
Operating income (loss)	(201)	(1,216)	1
Identifiable assets	223	15,575	37
SIX MONTHS ENDED DECEMBER 31, 2002			
Net Revenues	$624	$3,641	$27
Operating loss	(8)	(870)	(29
Identifiable assets	627	2,972	30

8. EARNINGS (LOSS) PER SHARE

Basic earnings per share are computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share are computed using the weighted average number of common and potentially dilutive securities outstanding during the period. Potentially dilutive securities consist of the incremental common shares issuable upon exercise of stock options and warrants (using the treasury stock method). Potentially dilutive securities are excluded from the computation if their effect is anti-dilutive.

The following table sets forth the computation of basic and diluted earnings (loss) per share:

	THREE MONTHS ENDED	
	DECEMBER 31, 2003	DECEMBER 3 2002
NUMERATOR:		
Net income (loss)	$402	($51
Numerator for basic earnings (loss) per share - income (loss) available to common stockholders	$402	($51
Numerator for diluted earnings (loss) per share - income (loss) available to common stockholders after assumed conversions	$402	($51
DENOMINATOR:		
Denominator for basic earnings (loss) per share - weighted average shares outstanding	23,268,099	22,792,26
Effect of dilutive securities using the treasury stock method as at December 31, 2003:		
7,343,244 Warrants Outstanding	--	-
2,058,644 Stock Options Outstanding	--	-
Effect of dilutive securities using the treasury stock method as at December 31, 2002:		
5,366,577 Warrants Outstanding	--	-
2,204,638 Stock Options Outstanding	--	-
Dilutive potential common shares		-
Denominator for diluted earnings (loss) per share - adjusted weighted average shares and assumed conversion	23,268,099	22,792,26
BASIC EARNINGS (LOSS) PER SHARE	$0.02	($0.00
DILUTED EARNINGS (LOSS) PER SHARE	$0.02	($0.00

9. STOCK-BASED AWARDS

Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure, an Amendment of FASB Statement No. 123," amends the disclosure requirements of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), to require more prominent disclosures in both annual and interim financial statements regarding the method of accounting for stock-based employee compensation and the effect of the method used on reported results.

We account for stock-based compensation plans in accordance with Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," under which no compensation cost is recognized in the financial statements for employee stock warrants and options when grants are made at an exercise price equal to the fair market value of the Company's stock. We have adopted the disclosure only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation".

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Under variable plan accounting, we recognize a charge equal to the per share change in the share value until the underlying options expire or are exercised. During the three and six months ended December 31, 2003 we recognized charges of ($2,069) and $12,735 respectively related to variable awards. This compares to charges of $0 and ($5,947), respectively for the three and six months ended December 31, 2002.

Had compensation cost for the stock-based compensation plans been determined based upon the fair value at grant dates for awards under those plans consistent with the method prescribed by SFAS 123, net income would have been reduced to the pro forma amounts indicated below:

(in thousands, except per share amounts)	THREE MONTHS ENDED DECEMBER 31,	
	2003	2002
NET INCOME (LOSS), AS REPORTED	$402	($51)
Intrinsic compensation charge recorded under APB 25	247	(387)
Pro Forma compensation charge under SAS 123	(614)	(316)
PRO FORMA NET INCOME (LOSS)	35	(754)
Pro Forma net income (loss) per share:		
Basic--as reported	$0.02	($0.00)
Basic--pro forma	$0.00	($0.03)
Diluted--as reported	$0.02	($0.00)
Diluted--pro forma	$0.00	($0.03)

The fair value of each option granted was estimated on the date of the grant using the Black-Scholes option-pricing model using the following weighted average assumptions:

	QUARTER ENDED DECEMBER 31,

	2003	2002
Risk-free interest rates	2.36% - 4.18%	1.21%
Expected dividend yields	--	--
Expected volatility	101.11%	126.08%
Expected option life (in years)	3 - 10	5 - 10

The weighted average fair value per option as of the grant date for grants made for both the three and six months ended December 31, 2003 was $0.85. This compares to $0.56 and $0.70, respectively for the three and six months ended December 31, 2002.

10. NEW ACCOUNTING STANDARDS

ACCOUNTING FOR REVENUE ARRANGEMENTS WITH MULTIPLE DELIVERABLES In November 2002, the EITF reached a consensus on Issue No. 00-21, Revenue Arrangements with Multiple Deliverables. Issue 00-21 provides guidance on how to account for arrangements that involve the delivery or performance of multiple products, services and/or rights to use assets. The provisions of Issue 00-21 will apply to revenue arrangements entered into in fiscal periods beginning after June 15, 2003. The adoption of Issue 00-21 did not have a material effect on our consolidated financial position, results of operations or cash flows.

AMENDMENT OF STATEMENT 133 ON DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES On April 30, 2003, the FASB issued Statement No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities. Statement 149 is intended to result in more consistent reporting of contracts as either freestanding derivative instruments subject to Statement 133 in its entirety, or as hybrid instruments with debt host contracts and embedded derivative features. In addition, Statement 149 clarifies the definition of a derivative by providing guidance on the meaning of initial net investments related to derivatives. Statement 149 is effective for contracts entered into or modified after June 30, 2003. At December 31, 2003, we do not hold any derivative instruments. The adoption of Statement 149 did not have an effect on our consolidated financial position, results of operations or cash flows.

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FINANCIAL INSTRUMENTS WITH CHARACTERISTICS OF BOTH LIABILITIES AND EQUITY On May 15, 2003, the FASB issued Statement No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity. Statement 150 establishes standards for classifying and measuring as liabilities certain financial instruments that embody obligations of the issuer and have characteristics of both liabilities and equity. Statement 150 represents a significant change in practice in the accounting for a number of financial instruments, including mandatory redeemable equity instruments and certain equity derivatives that frequently are used in connection with share repurchase programs. Statement 150 is effective for all financial instruments created or modified after May 31, 2003, and to other instruments as of July 1, 2003. We adopted Statement 150 on July 1, 2003 and the effect of adopting this statement did not have an impact on our financial position, results of operations or cash flows.

11. GOODWILL

Total goodwill at December 31, 2003 related to the acquisitions of Keynomics, DesignCAD and Planworks was $608,000. In accordance with SFAS No. 142, Goodwill and Intangible Assets, we will assess the underlying goodwill for impairment annually or more frequently if circumstances indicate impairment.

12. SUBSEQUENT EVENTS (PROPOSED ACQUISITION OF ALADDIN SYSTEMS, INC.)

On January 21, 2004, we announced that we entered into a definitive agreement with Aladdin Systems Holdings, Inc. to acquire its wholly owned subsidiary, Aladdin Systems, Inc. ("Aladdin"), a developer and publisher of utility software solutions in the areas of information access, removal, recovery, security and distribution of information and data for the Windows(R), Linux(R) and Macintosh(R) platforms.

The proposed consideration, which was based upon an in-depth analysis of Aladdin's current and projected business results, comparable companies and similar transactions, is a combination of cash, stock and a convertible note with a aggregate value of approximately $8 million plus an earn-out that could result in an additional $2 million in payments during the next three years.

We will rely on our available cash balance upon closing to fund the initial cash payment component of this transaction.

The transaction is expected to close in March 2004 and is subject to customary closing conditions.

ITEM 2- MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS

The following information should be read in conjunction with the consolidated financial statements and the notes thereto and in conjunction with Management's Discussion and Analysis or Plan of Operations in our Fiscal 2003 Form 10-KSB. This quarterly report on Form 10-QSB, and in particular this "Management's Discussion and Analysis or Plan of Operations," may contain forward-looking statements regarding future events or our future performance. These future events and future performance involve certain risks and uncertainties including those discussed in the "Other Factors That May Affect Future Operating Results" section of this Form 10-QSB, as well as in our Fiscal 2003 Form 10-KSB, as filed with the Securities and Exchange Commission ("SEC"). Actual events or our actual future results may differ materially from any forward-looking statements due to such risks and uncertainties. We assume no obligation to update these forward-looking statements to reflect actual results or changes in factors or assumptions affecting such forward-looking statements. This analysis is not intended to serve as a basis for projection of future events.

CRITICAL ACCOUNTING POLICIES

In accordance with recent Securities and Exchange Commission guidance, those material accounting policies that we believe are the most critical to an investor's understanding of our financial results and condition have been expanded and are discussed below. Certain of these policies are particularly important to the portrayal of our financial position and results of operations and require the application of significant judgment by our management to determine the appropriate assumptions to be used in the determination of certain estimates.

REVENUE RECOGNITION

Revenue is recognized in accordance with American Institute of Certified Public Accountants Statement of Position ("SOP") 97-2, Software Revenue Recognition, and SOP 98-9, Modification of SOP 97-2, With Respect to Certain Transactions.

Revenue is recognized when persuasive evidence of an arrangement exists (generally a purchase order), product has been delivered, the fee is fixed and determinable, and collection of the resulting account is probable.

- Revenue from packaged product sales to resellers and end users is recorded at the time of the sale net of estimated returns.

- Revenue from sales to distributors is recognized when the product sells through to retailers and end users. Sales to distributors permit limited rights of return according to the terms of the contract.

- For software delivered via the Internet, revenue is recorded when the customer downloads the software.

- Revenue from post contract customer support (PCS) is recognized ratably over the contract period.

- Training fees are recognized when the service is performed.

- Subscription revenue is recognized ratably over the contract period.

- Revenue from hybrid products is allocated to the underlying components based on the ratio of the value of each component to the total price and each portion is recognized accordingly.

- Non-refundable advanced payments received under license agreements with no defined terms are recognized as revenue when the customer accepts the delivered software.

- Revenue from software licensed to developers, including amounts in excess of non-refundable advanced payments, is recorded as the developers ship products containing the licensed software.

- Revenue from minimum guaranteed royalties in republishing agreements is recognized ratably over the term of the agreement. Royalties in excess of the guaranteed minimums are recognized when collected.

- Revenue from Original Equipment Manufacturer (OEM) contracts is recognized upon completion of our contractual obligations.

RESERVE FOR RETURNS, PRICE DISCOUNTS AND REBATES

Reserves for returns, price discounts and rebates are estimated using historical averages, open return requests, channel inventories, recent product sell-through activity and market conditions. Our allowances for returns, price discounts and rebates are based upon management's best judgment and estimates at the time of preparing the financial statements. Reserves are subjective estimates of future activity that are subject to risks and uncertainties, which could cause actual results to differ materially from estimates.

Our return policy generally allows our distributors to return purchased products primarily in exchange for new products or for credit towards future purchases as part of stock balancing programs. These returns are subject to certain limitations that may exist in the contract with an individual distributor, governing, for example, aggregate return amounts, and the age, condition and packaging of returned product. Under certain circumstances, such as terminations or when a product is defective, distributors could receive a cash refund if returns exceed amounts owed.

INVENTORIES

Inventories are valued at the lower of cost or market and are accounted for on the first-in, first-out basis. Management performs periodic assessments to determine the existence of obsolete, slow moving and non-salable inventories, and records necessary provisions to reduce such inventories to net realizable value. As of December 31, 2003, distributors held approximately $61,000 of our inventory under consignment arrangements.

IMPAIRMENT

Property, equipment, intangible and certain other long-lived assets are amortized over their useful lives. Useful lives are based on management's estimates of the period that the assets will generate revenues. Long-lived assets are written down to fair value whenever events or changes indicate that the carrying amount of an asset may not be recoverable. Our policy is to review the recoverability of all long-lived assets at a minimum of once per year and record an impairment loss when the fair value of the assets does not exceed the carrying amount of the asset.

In accordance with SFAS No. 142, Goodwill and Intangible Assets, we will assess the underlying goodwill for impairment annually or more frequently if circumstances indicate impairment.

RECENT EVENTS

PLANWORKS

On November 17, 2003, we acquired Planworks, a leading online provider of house plans. Planworks operates the houseplanguys.com website that contains an extensive library of over 11,000 unique house plans and has more than 25,000 members. We also acquired ten other domain names which will be used to assist individuals and designers looking for house plans and related products, further strengthening the IMSI network of online design and content commerce sites. The total consideration for the acquisition included the following:

- Cash: $275,000 of which $260,000 was paid upon closing with the remaining $15,000 balance to be held into an escrow account for a period of eight moths.

- 85,000 restricted shares of IMSI common stock which were priced as of the acquisition date or $1.16 per share.

CADSYMBOL ACQUISITION

On November 6, 2003, we entered into an asset purchase agreement with Assisto, whereby we acquired title and interest in certain tangible and intangible assets of Assisto. The assets included certain CAD symbol content, custom developed software and all related assets including inventory, web sites and domain names.

The total purchase price of approximately $372,000 will be paid according to the following schedule:

- Approximately $172,000 at closing;

- Approximately $200,000 to be held in escrow and released over the next fifteen months.

In addition, we granted to Ane Gyldholm and Michael Heckmann, principals of Assisto, warrants to each purchase twenty thousand (20,000) shares of IMSI's common stock at any time within the three year period following the closing at an exercise price of $1.21, which was the price of IMSI's common stock on the closing date.

CADSYMBOLS ACQUISITION

On October 27, 2003, we entered into an asset license and purchase agreement with Cardiff, whereby we acquired from Cardiff the exclusive, non-transferable right to use the cadsymbols.com and cadsymbols.net domain names and trademarks until December 31, 2006, when Cardiff is to assign the domain names and trademark to us subject to our payment of all amounts due Cardiff. The total consideration for the acquisition ($845,000) is comprised of the following:

- Three Hundred Thirty-Five Thousand Dollars ($335,000) upon the execution of the agreement;

- Two Hundred Fifty-Five Thousand Dollars ($255,000) in two payments to be paid over the next nine months

- Royalty payments to Cardiff equal to two percent (2.0%) of the net revenues, subject to certain minimums for the next three years based on sales generated by the websites.

In addition, we granted to Cardiff a warrant to purchase twenty-five thousand (25,000) shares of IMSI's common stock at any time within the three year period following the execution of the agreement at $1.14 per share.

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Upon the execution of the agreement, Cardiff deposited in an escrow account the assignment agreement of each domain name, and the assignment agreement of the trademark. The escrow agreement calls for release of the assignment documents to us on September 30, 2006 subject to the cumulative payment to Cardiff of all amounts due.

CADKEY ACQUISITION TERMINATION

As previously disclosed, on August 22, 2003, we entered into an agreement with CADKEY to purchase substantially all of its assets. The proposed purchase price was $2,500,000 and the assumption of CADKEY customer obligations. The acquisition was conditioned upon court approval pursuant to Section 363 of the U.S. Bankruptcy Code after CADKEY filed a voluntary petition under Chapter 11 of the Bankruptcy Code on August 22, 2003 in the U.S. Bankruptcy Court in Worcester, Massachusetts.

On October 27, 2003, we terminated our bid to acquire substantially all of the assets of CADKEY through an auction sale. As a result of the termination, we received a break up fee of $45,000 which was recorded as a reduction of legal expense and were reimbursed for $225,000 of professional fees advanced to CADKEY in addition to the $250,000 that was initially held in escrow. These amounts were initially recorded as short-term assets in the "Other current assets" account.

CADALOG

On September 12, 2003, we acquired from CADalog, Inc, CADalog.com, a network of websites that offers one of the largest mechanical parts symbols libraries on-line and allows members access to over 8 million 2D and 3D hardware component symbols. The acquisition also included the purchase of CADalog, Inc.'s Partsxl.com, Partswork.com and 3DModelsharing.com websites. This acquisition gives us the opportunity to sell additional CAD content and software plug-ins. The total consideration for the acquisition was $295,000. A payment of $250,000 was made on September 19, 2003 and the remaining $45,000 will be held in an escrow account with $15,000 to be released to the seller ninety days after the closing date, and the remaining $30,000 to be released after a period of twelve months. The escrow balance of $45,000 was fully funded on October 8, 2003.

DESIGNCAD

On July 28, 2003, we entered into an agreement to purchase the tangible and intangible assets of Upperspace corporation, constituting its DesignCAD line of products, several learning aids, and various smaller design programs.

The purchase price included the following consideration:

- $700,000 cash (of which $100,000 is being held in an escrow account for a period of twelve months)
- $300,000, 5% simple interest, promissory note payable 12 months from the date of closing
- An earn-out based on net revenue that could result in an additional $300,000 during the next three fiscal years
- A license pursuant to which Upperspace shall act for a period as the exclusive distributor of the purchased products to retail outlets, and a non-exclusive reseller of the product through direct sales channels such as the internet, email, telephone and fax.

The table below documents the components of consideration paid for each acquisition completed in the three and six months ended December 31, 2003 detailed above and the allocation of that consideration to the tangible and intangible assets acquired.

	PLANWORKS	CADSYMBOL	CADSYMBOLS	CADALOG
DATE TRANSACTION CLOSED:	NOVEMBER 17, 2003	NOVEMBER 6, 2003	OCTOBER 27, 2003	SEPTEMBER 12, 2003
CONSIDERATION				
Cash	$ 260	$ 171	$ 335	$ 250
Less: Cash on hand	(16)	--	--	--
Escrow	--	170	--	45
Stock	77	--	--	--
Warrants	--	30	18	--
Notes payable	14	--	474	--

Liabilities assumed	23	--	--	--
Transaction fees	20	1	3	--
TOTAL CONSIDERATION	$ 378	$ 372	$ 830	$ 295
ASSET ALLOCATION				
Tangible Assets				
Inventory	--	--	--	--
Marketing materials	--	--	--	--
Prepaid expenses	1	--	--	--
Computer hardware	--	12	--	7
Computer software	--	--	--	--
TOTAL TANGIBLE ASSETS	$ 1	$ 12	$ --	$ 7
INTANGIBLE ASSETS				
Capitalized software / content	--	180	--	268
Websites and associated domain names	315	180	830	20
Customer list	33	--	--	--
Goodwill	29	--	--	--
TOTAL INTANGIBLE ASSETS	$ 377	$ 360	$ 830	$ 288
TOTAL ASSETS ALLOCATED	$ 378	$ 372	$ 830	$ 295

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RESULTS OF OPERATIONS

The following table sets forth our results of operations for the three months ended December 31, 2003 and 2002 in absolute dollars and as a percentage of net revenues. It also details the changes from the prior fiscal year in absolute dollars and in percentages.

On June 30, 2003, we sold ArtToday, our wholly owned subsidiary based in Arizona to Jupiter. Under Generally Accepted Accounting Principles in the United States, ArtToday's operating results for all periods presented have been accounted for as discontinued operations.

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	THREE MONTHS ENDED DECEMBER 31,			
	2003		2002	
	$	AS % OF SALES	$	AS % OF SALES
Net revenues	$ 2,674	100%	$ 2,466	100%
Product cost	793	30%	1,075	44%
GROSS MARGIN	1,881	70%	1,391	56%
Operating expenses				
Sales & marketing	1,065	40%	836	34%
General & administrative	991	37%	499	20%
Research & development	531	20%	445	18%
TOTAL OPERATING EXPENSES	2,587	97%	1,780	72%
OPERATING LOSS	(706)	-26%	(389)	-16%
Other Income (expenses)				
Interest and other, net	60	2%	(127)	-5%
Unrealized gain on marketable securities	47	2%	--	--
Gain on liquidation of foreign subsidiaries	--	--	--	--
Gain on extinguishment of debt	(5)	--	257	10%
TOTAL OTHER INCOME (EXPENSES)	102	4%	130	5%
LOSS BEFORE INCOME TAX	(604)	-23%	(259)	-11%
Income tax benefit	6	--	--	--
LOSS FROM CONTINUING OPERATIONS	(598)	-22%	(259)	-11%
Gain from the sale of discontinued operations	1,000	37%	--	--
Income from discontinued operations, net of income tax	--	--	208	8%
NET INCOME (LOSS)	$ 402	15%	$ (51)	-2%

	SIX MONTHS ENDED DECEMBER 31,			
	2003		2002	

	$	AS % OF SALES	$	AS % OF SALES	$ (
Net revenues	$ 4,455	100%	$ 4,543	100%	
Product cost	1,371	31%	1,582	35%	
GROSS MARGIN	3,084	69%	2,961	65%	
Operating expenses					
Sales & marketing	1,803	40%	1,604	35%	
General & administrative	1,675	38%	1,442	32%	
Research & development	1,007	23%	822	18%	
TOTAL OPERATING EXPENSES	4,485	101%	3,868	85%	
OPERATING LOSS	(1,401)	-31%	(907)	-20%	
Other Income (expenses)					
Interest and other, net	140	3%	(182)	-4%	
Unrealized gain on marketable securities	177	4%	--	--	
Gain on liquidation of foreign subsidiaries	--	--	42	1%	
Gain on extinguishment of debt	76	2%	435	10%	
TOTAL OTHER INCOME (EXPENSES)	393	9%	295	6%	
LOSS BEFORE INCOME TAX	(1,008)	-23%	(612)	-13%	
Income tax benefit	10	--	--	--	
LOSS FROM CONTINUING OPERATIONS	(998)	-22%	(612)	-13%	
Gain from the sale of discontinued operations	1,000	22%	--	--	
Income from discontinued operations, net of income tax	--	--	425	9%	
NET INCOME (LOSS)	$ 2	--	$ (187)	-4%	

NET REVENUES

Net revenues of each of our principal product categories in dollars and as a percentage of total net revenues for the three and six months ended December 31, 2003 and 2002 are summarized in the following table (in thousands except for percentage amounts):

	THREE MONTHS ENDED DECEMBER 31,					
	2003		2002			
	$	%	$	%	$ CHANGE	% CHANGE

Precision Design	$1,349	50%	$ 745	30%	$ 604	81%
Business Applications and Other	1,325	50%	1,721	70%	(396)	-23%
NET REVENUES	$2,674	100%	$2,466	100%	$ 208	8%

	SIX MONTHS ENDED DECEMBER 31,					
	2003		2002			
	$	%	$	%	$ CHANGE	% CHANG
Precision Design	$2,050	46%	$1,752	39%	$ 298	17%
Business Applications and Other	2,405	54%	2,791	61%	(386)	-14%
NET REVENUES	$4,455	100%	$4,543	100%	$ (88)	-2%

Sales of our flagship product, TurboCAD(R), increased in the three and six months ended December 31, 2003 as compared to the same reporting periods in the previous fiscal year, resulting in an overall increase in revenues in the precision design category. The introduction of the "DesignCAD" line of products during the first quarter of fiscal 2004 and the additional revenues we earned from the acquisition of Planworks in the second quarter of fiscal 2004 accounted for the increase in sales of the precision design products as compared to the same period from the previous fiscal year. Revenues from Planworks amounted to $111,000 during the quarter ended December 31, 2003.

Overall revenues in the "Business Applications and Other" segment decreased during the three and six months ended December 31, 2003 as compared to the same periods of the previous fiscal year. Revenues from Keynomics, our productivity software subsidiary are included in this category and amounted to $318,000 and $478,000 during the three and six months ended December 31, 2003, respectively as compared to $447,000 and $625,000, respectively in the comparable periods from the previous fiscal year. The decline in sales of our historically strong selling products in this category like MasterClips and OrgPlus was the primary reason for the overall decrease in the "Business Applications and Other" segment despite the introduction of new titles during the first half of the fiscal year (PhotoObject) in addition to the release of newer version of our existing products (EasyLanguage and Net Accelerator).

Internationally, we distribute our products through our wholly owned German and Australian subsidiary and republishing partners in Europe and Asia. The increase in international sales during the three and six months ended December 31, 2003 is primarily due to our reentry into the European market by re-activating our German subsidiary during the previous fiscal year which allowed us to sell directly into the European Union. Total net sales from our German subsidiary accounted for $77,000 and $260,000, respectively during the three and six months ended December 31, 2003. The following table details the revenue breakdown between the domestic and international markets for the periods indicated.

	THREE MONTHS ENDED DECEMBER 31,					
	2003		2002			
	$	%	$	%	$ CHANGE	% CHANGE
Domestic sales	$2,296	86%	$2,186	88%	$ 110	5%
International sales	378	14%	280	12%	98	35%
NET REVENUES	$2,674	100%	$2,466	100%	$ 208	8%

	SIX MONTHS ENDED DECEMBER 31,					
	2003		2002			
	$	%	$	%	$ CHANGE	% CHANGE
Domestic sales	$3,669	82%	$3,949	87%	($ 280)	-7%
International sales	786	18%	594	13%	192	32%
NET REVENUES	$4,455	100%	$4,543	100%	$ 88	2%

We are currently serving the domestic and international retail markets using direct sales methods and republishing agreements. Low barriers to entry, intense price competition, and business consolidations continue to characterize the consumer software industry. Each of these factors along with the intermittent unfavorable retail conditions, including erosion of margins from competitive marketing and high rates of product returns, may adversely affect our revenues in the future.

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Our international revenues may be affected by the risks customarily associated with international operations, including fluctuations of the U.S. dollar, increases in duty rates, exchange or price controls, longer collection cycles, government regulations, political instability and changes in international tax laws.

RESERVE FOR RETURNS, PRICE DISCOUNTS AND REBATES

During the second quarter of fiscal 2004 we provided $181,000 for returns and received actual returns of approximately $112,000. The return reserve balance as of December 31, 2003 of $583,000 is consistent with the level of our estimate of excess inventory in the channel.

PRODUCT COSTS

Our product costs include the costs of CD-ROM duplication, printing of manuals, packaging and fulfillment, freight-in, freight out, license fees, royalties that we pay to third parties based on sales of published software and amortization of capitalized software acquisition and development costs. Costs associated with the return of products, such as refurbishment and the write down in value of returned goods are also included in product costs. The decrease in product costs in absolute dollars and as a percentage of net revenues for the three and six months ended December 31, 2003 as compared to the same periods from the previous fiscal year was primarily attributable to decreased amortization expenses and to a change in product mix toward the lower cost / higher margin precision design products.

GROSS MARGIN

Gross margin improved to 70% from 56% and to 69% from 65% during the three and six months ended December 31, 2003, respectively. This increase in gross margin is attributable to;

- A shift in our product mix towards the "precision design" segment from the "business application and other" segment as we increased our direct marketing emphasis. This is demonstrated by the re-launch of our revenue generating websites in September 2003, newly acquired products including DesignCAD, and the launch of new high margin services.

- A reduction in amortization expenses for software products as a result of the products being fully amortized.

Given the uncertain product lifecycle for some of our historically high margin products and depending on the success of newer versions launches, we may see our gross margin decline in future reporting periods.

SALES AND MARKETING

Our sales and marketing expenses consist primarily of salaries and benefits of sales and marketing personnel, commissions, advertising, printing and direct mail expenses. The increase in sales and marketing expenses during the three and six months ended December 31, 2003 was mainly attributable to the following:

- Increased direct mail expenses relative to our growing efforts to focus on direct targeting of our customers via marketing campaigns.

- Increased commissions paid to outside service providers that help us with their sales forces and E-commerce systems.

- The revision of our accounting treatment with regard to fees paid to our third party E-commerce solution provider, whereby we now record the fees as sales and marketing expenses. The effect of this reclassification was to increase sales and marketing expense by $61,000 and $32,000 for the three and six months ended December 31, 2003 as compared to the previous year.

GENERAL AND ADMINISTRATIVE

Our general and administrative expenses consist primarily of salaries and benefits for employees in the legal, finance, accounting, human resources, information systems and operations departments, fees to our professional advisors, rent and other general operating costs.

The increase in general and administrative expenses during the quarter ended December 31, 2003 as compared to the same quarter from the previous year was primarily due to amortization expense of $237,000 from the issuance of warrants to outside consultants mainly providing services in the area of investor relations. The comparable period from the previous fiscal year also included the reversal of the intrinsic value of warrants issued to Mr. Martin Wade III, our CEO, as part of his initial employment agreement. During the second quarter of fiscal 2003, we amended Mr. Wade's employment agreement whereby IMSI and Mr. Wade agreed to the full and complete cancellation of all outstanding warrants granted to Mr. Wade. Consequently, we reversed, during the six months ended December 31, 2003, $432,000 of already incurred amortization expense of the intrinsic value of warrants issued to Mr. Wade but were unvested.

Excluding the effect of the two transactions above, general and administrative expenses would have declined by approximately $195,000 during the quarter ended December 31, 2003 as compared to the same period from the previous fiscal year. We also experienced a substantial decline in legal fees as a result of the settlement of all outstanding legal actions from previous periods which accounted for the majority of the decrease in the general and administrative expenses.

RESEARCH AND DEVELOPMENT

Our research and development expenses consist primarily of salaries and benefits for research and development employees and payments to independent contractors. The increase in research and development expenses in the three months ended December 31, 2003 as compared to the same period from the previous fiscal year resulted mainly from increased personnel costs.

We continue to maintain a consistent investment in existing and new products. The constant ratio of research and development expenses as a percentage of sales reflects our commitment to investing in and developing our core products as well as maintaining strong relationships with our third party development team in Russia.

INTEREST AND OTHER, NET

Interest and other expenses, net, include interest and penalties on debt instruments, foreign currency transaction gains and losses, and other non-recurring items. The following table summarizes the components of interest and other, net for the three-month period ended December 31, 2003 and 2002:

	THREE MONTHS ENDED DECEMBER 31,			
	2003	2002	$ CHANGE FROM PREVIOUS YEAR	
INTEREST & OTHER EXPENSE, NET				
Interest expense	$ 0	$ (129)	$ 129	100%
Interest income	19	2	17	1141%
Foreign exchange gain (loss)	41	-	41	100%
Other income	-	-	-	0%

TOTAL	$ 60	$ (127)	$ 187	147%

	SIX MONTHS ENDED DECEMBER 31,			
	2003	2002	$ CHANGE FROM PREVIOUS YEAR	
INTEREST & OTHER EXPENSE, NET				
Interest expense	$ (3)	$ (176)	$ 173	98%
Interest income	45	8	37	477%
Foreign exchange gain (loss)	48	(14)	62	434%
Other income	50	-	50	100%
TOTAL	$ 140	$ (182)	$ 322	177%

UNREALIZED GAIN ON MARKETABLE SECURITIES

We recorded a $47,000 and a $177,000 gain on marketable securities during the three and six months ended December 31, 2003, respectively as we marked to market value our equity portfolio. The following table summarizes the net gain on marketable securities:

DESCRIPTION	QUARTER ENDED DECEMBER 31, 2003	SIX
Gain (loss) on Jupitermedia common stock	($2,500)	
Gain on professionally managed portfolio	49,050	
TOTAL	$46,550	

GAIN ON EXTINGUISHMENT OF DEBT

During the six months ended December 31, 2003, we recognized a gain of $76,000 from the extinguishment of debt primarily relating to the settlement of liabilities related to assets under a capital lease.

During the six months ended December 31, 2002, we recognized a gain of $435,000 from the extinguishment of debt representing the difference between the carrying balances and the settlement amounts payable to a variety of unsecured creditors, of which $84,000 was attributable to the extinguishment of debt owed to Baystar Capital.

PROVISION FOR INCOME TAXES

In the three months ended December 31, 2003, we recorded a tax benefit of $6,000 related to the refund of our estimated state income tax paid in prior fiscal years.

We have not recorded a tax benefit for domestic tax losses because of the uncertainty of realization. We adhere to Statement of Financial Accounting Standards No. 109 "Accounting for Income Taxes," which requires an asset and liability approach to financial accounting and reporting for income taxes. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

GAIN FROM THE SALE OF DISCONTINUED OPERATIONS

During the quarter ended December 31, 2003, we recorded a gain of $1.0 Million from the sale of discontinued operations representing the successful achievement of the first earnout from the sale of ArtToday. This earnout was contingent on ArtToday reaching certain revenue milestones. We have received confirmation from Jupitermedia that the full amount of the $1.0 Million earnout was earned and will be paid per the stock purchase agreement by February 14, 2004.

INCOME FROM DISCONTINUED OPERATIONS

In June 2003, we sold ArtToday, our wholly owned subsidiary based in Arizona, to Jupitermedia. Under Generally Accepted Accounting Principles ("GAAP") in the United States, ArtToday's operating results for the three and six months ended December 31, 2002, totaling $208,000 and $425,000, respectively, have been accounted for as discontinued operations.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2003, we had $5,249,000 in cash and cash equivalents. This represents a $1,480,000 decline from the $6,729,000 balance at September 30, 2003 and a $5,150,000 decline from the $10,399,000 balance at June 30, 2003. Working capital at December 31, 2003 was $6,057,000. This represents a decline of $994,000 over the working capital at September 30, 2003 and a decline of $2,599,000 over the working capital at June 30, 2003 of $8,656,000.

Our operating activities used net cash of $2,507,000 during the six months ended December 31, 2003. This compares to net cash used from operations of $694,000 during the six months ended December 31, 2002. Our increased operating loss, combined with payments we made relating to accrued taxes and other accrued expenses and the increase in our receivables and inventories contributed to the increased usage of cash in the six months ended December 31, 2003 as compared to the same period from the previous fiscal year. Receivables and inventories increased during the six months ended December 31, 2003 primarily due to a change in the method of distribution for some of our products, including TurboCAD(R), from licensing arrangements to selling directly to resellers and distributors.

Our investing activities consumed net cash of $2,479,000 during the six months ended December 31, 2003, as compared to net cash used of $179,000 during the comparable period from the previous fiscal year. The cash was mainly used to acquire Planworks and several new product lines. The following table details the cash outlays for the acquisitions we made during the six months ended December 31, 2003.

	ACQUIRED IN	C
WEBSITES, CONTENT AND NEW PRODUCT LINES:		
CADsymbols	2nd quarter of Fiscal 2004	
CADsymbol	2nd quarter of Fiscal 2004	
DesignCAD	1st quarter of Fiscal 2004	
Cadalog	1st quarter of Fiscal 2004	
Other	2nd quarter of Fiscal 2004	
BUSINESS		
Planworks	2nd quarter of Fiscal 2004	
TOTAL		

These acquisitions are consistent with our strategy to grow our software business with a focus on products and services that complement our direct marketing and online distribution strengths. We expect to continue to identify and acquire products and launch services that satisfy real customer needs and have the combination of high growth potential and positive EBITDA. These acquisitions, including the proposed Aladdin Systems, Inc. acquisition, will be funded thru a combination of cash on hand, debt and the issuance of our common stock. The divestiture of ArtToday provided us with sufficient liquidity to continue to strengthen our product portfolio and distribution channels.

Our investing activities also included investment in marketable securities in the amount of $160,000 during the quarter ended September 30, 2003.

Also, during the first quarter of fiscal 2004, we entered into a 15% one-year note with DCDC whereby we extended a loan to them in the amount of $350,000. The note is due, with interest, on September 18, 2004. The note is secured by 400,000 shares of IMSI's stock held by DCDC. The agreement also calls for DCDC not to sell any other IMSI common stock that it holds, with the exception of private sales of IMSI common stock, prior to February 15, 2004.

Our financing activities consumed net cash of $133,000 during the six months ended December 31, 2003. This compares to $407,000 of net cash used by financing activities during the comparable periods from the previous fiscal year. As previously disclosed, we paid $160,000 to Imageline on July 7, 2003, which represents the final payment in connection with our mutual settlement of previous infringement claims. This payment accounted for most of the cash used in our financing activities during the six months ended December 31, 2003 and was in part offset by cash received from the exercise of warrants and options in the amounts of $65,000 and $71,000, respectively.

Historically, we have financed our working capital and capital expenditure requirements primarily from retained earnings, short-term and long-term notes and bank borrowings, capitalized leases and sales of common stock. The sale of ArtToday to Jupitermedia in June 2003 provided us with additional sources of funds to support future growth. We may also seek additional equity and/or debt financing to sustain our growth strategy. However, we believe that we have sufficient funds to support our operations at least for the next twelve months, based on our current cash position and equity sources. If we are successful in continuing to improve our financial performance, we believe that we will be able to obtain any additional financing required on competitive terms. In addition, we will continue to seek opportunities and discussions with third parties concerning the sale or license of certain product lines and/or the sale or license of a portion of our assets.

To achieve our growth objectives, we are considering different strategies, including growth through mergers and/or acquisitions. As a result, we are evaluating and we will continue to evaluate other companies and businesses for potential synergies that would add value to our existing operations.

The forecast period of time through which our financial resources will be adequate to support working capital and capital expenditure requirements is a forward-looking statement that involves risks and uncertainties, and actual results could vary. Furthermore, any additional equity financing may be dilutive to shareholders, and debt financing may involve restrictive covenants.

OTHER FACTORS THAT MAY AFFECT FUTURE OPERATING RESULTS

Factors that may affect operating results in the future include, but are not limited to:

- Market acceptance of our products or those of our competitors
- Timing of introductions of new products and new versions of existing products
- Expenses relating to the development and promotion of such new products and new version introductions
- Intense price competition and numerous end-user rebates
- Projected and actual changes in platforms and technologies
- Accuracy of forecasts of, and fluctuations in, consumer demand
- Extent of third party royalty payments
- Rate of growth of the consumer software and Internet markets
- Timing of orders or order cancellation from major customers
- Changes or disruptions in the consumer software distribution channels
- Economic conditions, both generally and within the software or Internet industries
- Achievement of future earn-outs related to the sale of ArtToday, Inc.

ITEM 3- CONTROLS AND PROCEDURES

(a) Under the supervision and with the participation of IMSI's management, including IMSI's principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-14(c) promulgated under the Securities Exchange Act of

1934, as amended (the "Exchange Act"), within 90 days of the filing date of this report. Based on their evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are effective.

(b) We have evaluated our accounting procedures and control processes related to material transactions to ensure they are recorded timely and accurately in the financial statements. There have been no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation referenced in paragraph (a) above.

PART II - OTHER INFORMATION

ITEM 1- LEGAL PROCEEDINGS

Not Applicable

ITEM 2- CHANGES IN SECURITIES

Not Applicable

ITEM 3- DEFAULTS UPON SENIOR SECURITIES

Not Applicable

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

On February 10, 2004, we filed with the Securities and Exchange Commission a Proxy Statement on Schedule 14-A pursuant to section 14(A) of the Securities Exchange Act Of 1934 in connection with the solicitation of proxies by the board of directors of IMSI for use at the annual meeting of shareholders to be held on March 17, 2004.

The annual meeting of the shareholders of IMSI will be held for the following purposes:

- To elect seven directors for a term of one year.
- To approve the 2004 Incentive Stock Option Plan.
- To authorize the issuance of options aggregating up to 49.0% of the outstanding capitalization.
- To ratify the appointment of Grant Thornton LLP as IMSI's independent auditors for the fiscal year ending June 30, 2004.
- To consider and act on such other business as may properly come before the meeting or any adjournment or adjournments thereof.

The Board of Directors has nominated the following persons for election:

NAME	AGE	OCCUPATION

Bruce Galloway	45	Chairman of the Board of Directors	200
Martin Wade, III	54	Chief Executive Officer	200
Evan Binn	64	Director	200
Donald Perlyn	60	Director	200
Robert Mayer	49	Executive Vice President	200
Robert S. Falcone	57	Director	200
Richard J. Berman	61	Director	200

ITEM 5- OTHER INFORMATION

Not Applicable

ITEM 6- EXHIBITS AND REPORTS ON FORM 8-K

EXHIBITS AND FINANCIAL STATEMENTS:

The following documents are filed as a part of this Report:

FINANCIAL STATEMENTS

The following consolidated financial statements of International Microcomputer Software, Inc., and Subsidiaries are incorporated by reference in Part I, Item 1:

Consolidated Balance Sheet at December 31, 2003 and June 30, 2003

Consolidated Statements of Operations for the interim periods ended December 31, 2003 and 2002

Consolidated Statements of Shareholders' Equity for the interim period ended December 31, 2003

Consolidated Statements of Cash Flows for the interim periods ended December 31, 2003 and 2002

Notes to Consolidated Financial Statements

EXHIBITS

The following exhibits are filed as part of, or incorporated by reference into this Report:

31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certification of Chief Financial Officer Pursuant to Section 906 of the

Sarbanes-Oxley Act of 2002

(b) REPORTS ON FORM 8-K

- On November 17, 2003 we filed a Form 8-K to announce our financial results for the fiscal quarter ended September 30, 2003.

SIGNATURES

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

INTERNATIONAL MICROCOMPUTER SOFTWARE, INC.

DATE: FEBRUARY 11, 2003

BY: /S/ MARTIN WADE, III
Martin Wade, III
Director & Chief Executive Officer

BY: /S/ WILLIAM J. BUSH
William J. Bush
Chief Financial Officer (Principal Accounting Officer)

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