IMAGING TECHNOLOGIES CORP/CA
Form 10QSB
November 25, 2003

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

FORM 10-QSB

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2003

or

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

Commission file No. 0-12641

[GRAPHIC OMITED]

IMAGING TECHNOLOGIES CORPORATION
(Exact name of registrant as specified in its charter)

DELAWARE 33-0021693
(State or other jurisdiction of incorporation or organization) (IRS Employer ID No.)

17075 VIA DEL CAMPO
SAN DIEGO, CA 92127
(Address of principal executive offices)

Registrant's Telephone Number, Including Area Code: (858) 451-6120

Check whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the 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

The number of shares outstanding of the registrant's common stock as of November 14 2003 was 289,293,819

Transitional Small Business Disclosure Format (check one): Yes [ ] No [X]

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PART I. - FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

IMAGING TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET
(in thousands, except share data)
(unaudited)

	SEPT.
ASSETS	
Current assets	
Cash.	$
Accounts receivable, net of allowance of $86	
Inventories, net.	
Prepaid expenses and other current assets	
Total current assets	
Goodwill	
Patent, net of accumulated amortization of $90	
PEO contracts, net of accumulated amortization of $108	
Property and equipment, net of accumulated depreciation.	
Workers' compensation deposit and other assets	
Total assets.	$
LIABILITIES AND SHAREHOLDERS' DEFICIENCY	
Current liabilities	
Borrowings under bank notes payable	$
Notes payable, current portion (including related party note of $1,500)	
Convertible debentures, net of discounts of $342.	
Accounts payable.	
Obligations under capital lease	
PEO payroll taxes and other payroll deductions.	
PEO accrued worksite employee	

Advances from related party	
Other accrued expenses.	
Total current liabilities.	
Long-term liabilities:	
Long-term capital lease	
Long-term convertible debentures, less discounts of $139.	
Long-term notes payable (including related party note of $250).	
Total liabilities.	
Preferred stock - minority interest in subsidiary.	
Shareholders' deficiency	
Series A convertible, redeemable preferred stock, $1,000 par value, 7,500 shares authorized, 20.5 shares issued and outstanding.	
Common stock, $0.005 par value, 500,000,000 shares authorized; 265,384,510 shares issued and outstanding	
Common stock warrants and options	
Paid-in capital	
Accumulated deficit	
Total shareholders' deficiency	
Total liabilities and shareholders' deficiency.	$

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

IMAGING TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
THREE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002
(in thousands, except share data)
(unaudited)

(In thousands, except per share amounts)

Revenues	
Sales of products	$
Software sales, licenses and royalties.	
Temporary staffing services	
PEO services (gross billings of $13,060 and $2,822 respectively; less worksite employee payroll costs of $13,060 and $2,430, respectively)	
Total revenue	
Costs of revenues	
Cost of products sold	
Cost of software sales, licenses and royalties.	
Cost of temporary staffing.	
Cost of PEO services.	

Total cost of revenues	
Operating expenses	
Selling, general, and administrative	
Research and development	
Loss from operations	
Other income (expense):	
Interest and finance costs, net	
Gain on extinguishment of debt	
Other	
Loss before provision for income taxes	
Provision for income taxes	
Net loss	
Preferred stock dividends	
Net loss attributed to common shareholders	$
Loss per common shares	
Basic and diluted	$
Weighted average common shares - basic and diluted	

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

IMAGING TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
THREE MONTH ENDED SEPTEMBER 30, 2003 AND 2002
(in thousands, except share data)
(unaudited)

Cash flows from operating activities	
Net loss	$
Adjustments to reconcile net loss to net cash from operating activities	
Depreciation and amortization	
Stock issued for services	
Amortization of debt discount	
Value of service for exercise of warrants	
Value of warrants issued for services	

Changes in operating assets and liabilities:	
Accounts receivable	
Inventories	
Prepaid expenses and other	
Accounts payable and accrued expenses	
PEO liabilities	
Other assets	
Net cash used in operating activities	
Cash flows from investing activities	
Cash expenditures	
Net cash used in investing activities	
Cash flows from financing activities	
Change in cash overdraft, net	
Net borrowings under bank notes payable	
Issuance of notes payable	
Repayment of notes payable	
Repayment of capital lease obligation	
Net proceeds from issuance of common stock	
Net cash provided by (used in) financing activities	
Net decrease in cash and cash equivalents	
Cash and cash equivalents, beginning of period	
Cash and cash equivalents, end of period	$

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

IMAGING TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINTUED)
THREE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002
(in thousands, except share data)
(unaudited)

NON-CASH INVESTING AND FINANCING ACTIVITIES

During the three months ended September 30, 2003, the Company issued: 1) 5,220,000 shares of its common stock for services valued at $129,400; 2) 10,272,110 shares of its common stock for compensation valued at $140,332; 3) 20,260,000 shares of its common stock for debt of $405,200; and 4) 48,400,337 shares of its common stock for the conversion of convertible debentures in the amount of $345,562.

During the three months ended September 30, 2002, the Company rescinded the $70,000 conversion of convertible notes payable into common stock.

IMAGING TECHNOLOGIES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except share data)
(unaudited)

NOTE 1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Imaging Technologies Corporation and Subsidiaries (the "Company" or "ITEC") have been prepared pursuant to the rules of the Securities and Exchange Commission (the "SEC") for quarterly reports on Form 10-QSB and do not include all of the information and note disclosures required by accounting principles generally accepted in the United States of America. These financial statements and notes herein are unaudited, but in the opinion of management, include all the adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the Company's financial position, results of operations, and cash flows for the periods presented. These financial statements should be read in conjunction with the Company's audited financial statements and notes thereto for the years ended June 30, 2003, 2002, and 2001 included in the Company's annual report on Form 10-K filed with the SEC. Interim operating results are not necessarily indicative of operating results for any future interim period or for the full year.

Jackson Staffing

Effective September 1, 2003, the Company acquired, through hiring two key persons, the operations and results thereof of the temporary staffing service then owned by Jackson Staffing, LLC.

There is no specific acquisition agreement, except for the hiring of the two owners as employees of SourceOne Group, Inc., a wholly-owned subsidiary of the Company. The Company did not acquire Jackson Staffing, but only assumed its business and employees. Accordingly, only the results of Jackson Staffing for the month ended September 30, 2003 are included in the Company's financial statements.

NOTE 2. GOING CONCERN CONSIDERATIONS

The accompanying unaudited consolidated financial statements have been prepared assuming that the Company will continue as a going concern. For the three months ended September 30, 2003, the Company had a net loss of $2,353,000. As of September 30, 2003, the Company had a negative working capital deficiency of $30,139,000 and had a shareholders' deficiency of $110,132,000. In addition, the Company is in default on certain note payable obligations and is being sued by numerous trade creditors for nonpayment of amounts due. The Company is also deficient in its payments relating to payroll tax liabilities. These conditions raise substantial doubt about the Company's ability to continue as a going concern.

On August 20, 1999, at the request of Imperial Bank, the Company's primary lender, the Superior Court of San Diego appointed an operational receiver who took control of the Company's day-to-day operations on August 23, 1999. On June 21, 2000, in connection with a settlement agreement reached with Imperial Bank, the Superior Court of San Diego issued an order dismissing the operational receiver.

On October 21, 1999, Nasdaq notified the Company that it no longer complied with the bid price and net tangible assets/market capitalization/net income requirements for continued listing on The Nasdaq SmallCap Market. At a hearing on December 2, 1999, a Nasdaq Listing Qualifications Panel also raised public interest concerns relating to the Company's financial viability. The Company's common stock was delisted from The Nasdaq Stock Market effective with the close of business on March 1, 2000. As a result of being delisted from The Nasdaq

SmallCap Market, shareholders may find it more difficult to sell common stock. This lack of liquidity also may make it more difficult to raise capital in the future. Trading of the Company's common stock is now being conducted over-the-counter through the NASD Electronic Bulletin Board and covered by Rule 15g-9 under the Securities Exchange Act of 1934. Under this rule, broker/dealers who recommend these securities to persons other than established customers and accredited investors must make a special written suitability determination for the purchaser and receive the purchaser's written agreement to a transaction prior to sale. Securities are exempt from this rule if the market price is at least $5.00 per share.

The Securities and Exchange Commission adopted regulations that generally define a "penny stock" as any equity security that has a market price of less than $5.00 per share. Additionally, if the equity security is not registered or authorized on a national securities exchange or the Nasdaq and the issuer has net tangible assets under $2,000,000, the equity security also would constitute a "penny stock." Our common stock does constitute a penny stock because our common stock has a market price less than $5.00 per share, our common stock is no longer quoted on Nasdaq and our net tangible assets do not exceed $2,000,000. As our common stock falls within the definition of penny stock, these regulations require the delivery, prior to any transaction involving our common stock, of a disclosure schedule explaining the penny stock market and the risks associated with it. Furthermore, the ability of broker/dealers to sell our common stock and the ability of shareholders to sell our common stock in the secondary market would be limited. As a result, the market liquidity for our common stock would be severely and adversely affected. We can provide no assurance that trading in our common stock will not be subject to these or other regulations in the future, which would negatively affect the market for our common stock.

The Company must obtain additional funds to provide adequate working capital and finance operations. However, there can be no assurance that the Company will be able to complete any additional debt or equity financings on favorable terms or at all, or that any such financings, if completed, will be adequate to meet the Company's capital requirements including compliance with the Imperial Bank settlement agreement. Any additional equity or convertible debt financings could result in substantial dilution to the Company's shareholders. If adequate funds are not available, the Company may be required to delay, reduce or eliminate some or all of its planned activities, including any potential mergers or acquisitions. The Company's inability to fund its capital requirements would have a material adverse effect on the Company. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

NOTE 3. STOCK BASED COMPENSATION

The Company accounts for employee stock options in accordance with Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees". Under APB 25, the Company does not recognize compensation expense related to options issued under the Company's employee stock option plans, unless the option is granted at a price below market price on the date of grant. In 1996, SFAS No. 123 "Accounting for Stock-Based Compensation", became effective for the Company. SFAS No. 123, which prescribes the recognition of compensation expense based on the fair value of options on the grant date, allows companies to continue applying APB 25 if certain pro forma disclosures are made assuming hypothetical fair value method, for which the Company uses the Black-Scholes option-pricing model.

For non-employee stock based compensation, the Company recognizes an expense in accordance with SFAS No. 123 and values the equity securities based on the fair value of the security on the date of grant. For stock-based awards, the value is based on the market value for the stock on the date of grant and if the stock has restrictions as to transferability, a discount is provided for lack of tradability. Stock option awards are valued using the Black-Scholes option-pricing model.

The Company applies Accounting Principles Board Opinion No. 25 and related Interpretations in accounting for its stock option plans. The Company has opted under SFAS No. 123 to disclose its stock-based compensation with no financial effect. The pro forma effects of applying SFAS No. 123 in this initial phase-in period are not necessarily representative of the effects on reported net income or loss for future years. Had compensation expense for the Company's stock option plans been determined based upon the fair value at the grant date for awards under these plans consistent with the methodology prescribed under SFAS No. 123, the Company's pro forma net loss and net loss per share would have been as follows for the three months ended September 30:

(In thousands, except share amounts). . . .	2003	2002
Net loss		
As reported	$ (2,446)	$ (2,052)
Compensation recognized under APB No. 25. .	-	-
Compensation recognized under SFAS No. 123.	-	-
Pro forma	$ (2,446)	$ (2,052)
Basic earnings (loss) per share		
As reported	$ (0.01)	$ (0.08)
Pro forma	$ (0.01)	$ (0.08)

This option valuation model requires input of highly subjective assumptions. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing model does not necessarily provide a reliable single measure of fair value of its employee stock options.

The weighted average fair value of the options granted during fiscal years 2003 and 2002 is estimated on the date of grant using the Black-Scholes option-pricing model. All options granted in fiscal years 2003 and 2002 vested immediately. The weighted average fair values and weighted average assumptions used in calculating the fair values were as follows for the years ended June 30:

	2003	2002
Fair Value of options granted.	$0.015	$0.56
Risk free interest rate. . . .	3.5%	3.5%
Expected life (years).	3	1
Expected volatility.	421%	179%
Expected dividends	-	-

NOTE 4. LOSS PER COMMON SHARE

The Company reports earnings (loss) per share in accordance with SFAS No. 128, "Earnings per Share." Basic earnings (loss) per share are computed by dividing income (loss) available to common shareholders by the weighted average number of common shares available. Diluted earnings (loss) per share is computed similar to basic earnings (loss) per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. Diluted earnings (loss) per share have not been presented since the effect of the assumed conversion of options and warrants to purchase common shares would have an anti-dilutive effect. The following potential common shares have been excluded from the computation of diluted net loss per share for the three months ended September 30, 2003: warrants - 6,002,356 and stock options - 34,158,100.

NOTE 5. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

During April 2003, the FASB issued SFAS 149 - "Amendment of Statement 133 on Derivative Instruments and Hedging Activities", effective for contracts entered into or modified after June 30, 2003, except as stated below and for hedging relationships designated after June 30, 2003. In addition, except as stated below, all provisions of this Statement should be applied prospectively. The provisions of this Statement that relate to Statement 133 Implementation Issues that have been effective for fiscal quarters that began prior to June 15, 2003, should continue to be applied in accordance with their respective effective dates. In addition, paragraphs 7(a) and 23(a), which relate to forward purchases or sales of when-issued securities or other securities that do not yet exist, should be applied to both existing contracts and new contracts entered into after June 30, 2003. The Company does not participate in such transactions, however, is evaluating the effect of this new pronouncement, if any, and will adopt FASB 149 within the prescribed time.

During May 2003, the FASB issued SFAS 150 - "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity", effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a freestanding financial instrument that is within its scope as a liability (or an asset in some circumstances). Many of those instruments were previously classified as equity. Some of the provisions of this Statement are consistent with the current definition of liabilities in FASB Concepts Statement No. 6, Elements of Financial Statements. The adoption of this new pronouncement did not have a material impact to the Company's financial position or results of operations.

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities." Interpretation 46 changes the criteria by which one company includes another entity in its consolidated financial statements. Previously, the criteria were based on control through voting interest. Interpretation 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. A company that consolidates a variable interest entity is called the primary beneficiary of that entity. The consolidation requirements of Interpretation 46 apply immediately to variable interest entities created after January 31, 2003. The consolidation requirements apply to other entities in the first fiscal year or interim period beginning after December 15, 2003. Certain of the disclosure requirements apply in all financial statements issued after January 31, 2003, regardless of when the variable interest entity was established. The Company does not expect the adoption to have a material impact on the Company's financial position or results of operations.

NOTE 6. REVENUE RECOGNITION RELATED TO PEO SEGMENT

The Company recognizes its revenues associated with its PEO business pursuant to EITF 99-19 "Reporting Revenue Gross as a Principal versus Net as an Agent." Previously, the Company reported its worksite employees as a component of direct costs, The Company's revenues are now reported net of worksite employee payroll cost (net method). To conform to the net method, the Company reclassified worksite employee payroll costs for each of its quarters in the fiscal year ended June 30, 2003 and its Form 10K for the year ended June 30, 2002. These reclassifications had no effect on gross profit, operating loss, or net loss.

NOTE 7. CONVERTIBLE NOTES PAYABLE

Listed below is a roll-forward schedule of the convertible debentures:

(In Thousands)		
Balance at June 30, 2003	$	1,857
Issuance of convertible debentures during the quarter.		-
Converted into common stock.		(346)
Amortization of value of warrants and preferential conversion feature		237
Balance at September 30, 2003.	$	1,748

NOTE 8. SHAREHOLDERS' DEFICIENCY

Amendment To The Certificate Of Incorporation.

On September 28, 2001, the Company's shareholders authorized an amendment to the Certificate of Incorporation to: (i) effect a stock combination (reverse split) of the Company's common stock in an exchange ratio to be approved by the Board, ranging from one (1) newly issued share for each ten (10) outstanding shares of common stock to one (1) newly issued share for each twenty (20) outstanding shares of common stock (the "Reverse Split"); and (ii) provide that no fractional shares or scrip representing fractions of a share shall be issued, but in lieu thereof, each fraction of a share that any shareholder would otherwise be entitled to receive shall be rounded up to the nearest whole share. There will be no change in the number of the Company's authorized shares of common stock and no change in the par value of a share of Common Stock.

On August 9, 2002, the Company's board of directors approved and effected a 1 for 20 reverse stock split. All share and per share data have been retroactively restated to reflect this stock split.

Stock Issuances

During the three months ended September 30, 2003, ITEC issued the following:

- 5,220,000 shares of its common stock for legal and consulting services valued at $129,400. The value of the services was determined using the market value of ITEC's common stock on the date of issuance;

- 10,272,110 shares of its common stock for compensation valued at $140,332. The value of the services was determined using the market value of ITEC's common stock on the date of issuance;

- 20,260,000 shares of its common stock for debt of $405,200; and

- 48,400,337 shares of its common stock for the conversion of convertible debentures in the amount of $345,562.

NOTE 9. SEGMENT INFORMATION

The Company managed and internally reported the Company's business as three reportable segments, principally, (1) products and accessories, (2) software, (3) temporary staffing, and (4) PEO services.

Segment information for the period ended March 31, 2003 is as follows:

(in thousands)

	PRODUCTS	SOFTWARE	TEMPORARY STAFFING	PEO SERVICES	TOTAL
3-months ended 9/30/03					
Revenues.	$ 131	$ 36	$ 767	$ 3,952	$ 4,886
Operating income (loss)	(368)	(935)	40	(786)	(2,049)
3-months ended 9/30/02					
Revenues.	$ 486	$ 138	$ -	$ 392	$ 1,016
Operating income (loss)	(890)	(207)	-	(338)	(1,435)

NOTE 10. SUBSEQUENT EVENTS

From October 1, 2003 to November 14, 2003, the Company issued 23,909,309 shares of its common stock to consultants, for warrant exercises, for conversion of convertible debt, and for the reduction of debt.

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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this Quarterly Report on Form 10-QSB. The statements contained in this Report on Form 10-QSB that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including statements regarding our expectations, hopes, intentions or strategies regarding the future. Forward-looking statements include statements regarding: future product or product development; future research and development spending and our product development strategies, and are generally identifiable by the use of the words "may", "should", "expect", "anticipate", "estimates", "believe", "intend", or "project" or the negative thereof or other variations thereon or comparable terminology. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements (or industry results, performance or achievements) expressed or implied by these forward-looking statements to be materially different from those predicted. The factors that could affect our actual results include, but are not limited to, the following: general economic and business conditions, both nationally and in the regions in which we operate; competition; changes in business strategy or development plans; our inability to retain key employees; our inability to obtain sufficient financing to continue to expand operations; and changes in demand for products by our customers.

OVERVIEW

Imaging Technologies Corporation (ITEC) develops and distributes imaging software and distributes digital imaging products. ITEC sells a range of imaging products for use in graphics and publishing, digital photography, and other niche business and technical markets. Our core technologies are related to the design and development of software products that improve the accuracy of color reproduction.

In November 2001, we embarked on an expansion program to provide more services to help with tasks that have negatively impacted the business operations of its existing and potential customers. To this end, ITEC, through strategic acquisitions, became a professional employer organization ("PEO").

ITEC now provides comprehensive personnel management services through its wholly-owned SourceOne Group and EnStructure subsidiaries. Each of these subsidiaries provides a broad range of services, including benefits and payroll administration, health and workers' compensation insurance programs, personnel records management, and employer liability management to small and medium-sized businesses.

In May 2002, we entered into an agreement to acquire Dream Canvas, Inc., a Japanese corporation that has developed machines currently used for the automated printing of custom stickers, popular in the Japanese consumer market. We completed the acquisition of Dream Canvas Technology, Inc. (DCT) in October 2002 and paid the sum of $40,000 with the issuance of 100,000 shares of its common stock. In December 2002, ITEC sold DCT to Baseline Worldwide Limited for $75,000 in cash.

In July 2002, we entered into an agreement to acquire controlling interest in Quik Pix, Inc. ("QPI"). QPI shares are traded on the National Quotation Bureau Pink Sheets under the symbol QPIX. On January 14, 2003, we completed the acquisition of shares, representing controlling interest, of Quik Pix, Inc.

In August 2002, we entered into an agreement to acquire controlling interest in Greenland Corporation. Greenland shares are traded on the Electronic Bulletin Board under the symbol GRLC. On January 14, 2003, we completed the acquisition of shares, representing controlling interest, of Greenland.

From July 1, 2003 to November 6, 2003, we issued 109,963,339 shares of our common stock to consultants, for warrant exercises, for conversion of convertible debt, and for the reduction of debt.

Effective September 1, 2003, we acquired, through hiring two key persons, the operations and results thereof of the temporary staffing service then owned by Jackson Staffing, LLC.

There is no specific acquisition agreement, except the hiring of the two owners as employees of SourceOne Group, Inc., a wholly-owned subsidiary of ITEC. We did not acquire Jackson Staffing, but only assumed its business and employees. Accordingly, only the results of operations for the month ended September 30, 2003 are included in our financial statements.

Our business continues to experience operational and liquidity challenges. Accordingly, year-to-year financial comparisons may be of limited usefulness now and for the next several periods due to anticipated changes in our business as these changes relate to potential acquisitions of new businesses, changes in product lines, and the potential for suspending or discontinuing certain components of the business.

Our current strategy is: to expand our PEO business and to commercialize our own technology, which is embodied in our ColorBlind Color Management software and other products obtained through strategic acquisitions.

To successfully execute our current strategy, we will need to improve our working capital position. The report of our independent auditors accompanying our June 30, 2003 financial statements includes an explanatory paragraph indicating there is a substantial doubt about ITEC's ability to continue as a going concern, due primarily to the decreases in our working capital and net worth. We plan to overcome the circumstances that impact our ability to remain a going concern through a combination of achieving profitability, raising additional debt and equity financing, and renegotiating existing obligations.

Since the removal of the court appointed operational receiver in June 2000, we have been able to reestablish relationships with some past customers and distributors and to establish relationships with new customers. Additionally, we have been working to reduce costs through the reduction in staff, the suspension of certain research and development programs, such as the design and manufacture of controller boards and printers, and the suspension of product sales and marketing programs related to office equipment and services in favor of a greater concentration on its PEO and imaging software businesses. We began a program to reduce our debt through debt to equity conversions. We continue to pursue the acquisition of businesses that will grow our business.

There can be no assurance, however, that we will be able to complete any additional debt or equity financings on favorable terms or at all, or that any such financings, if completed, will be adequate to meet our capital requirements. Any additional equity or convertible debt financings could result in substantial dilution to our shareholders. If adequate funds are not available, we may be required to delay, reduce or eliminate some or all of our planned activities, including any potential mergers or acquisitions. Our inability to fund our capital requirements would have a material adverse effect on the Company. Also see "Liquidity and Capital Resources." and "Risks and Uncertainties - Future Capital Needs."

RESTRUCTURING AND NEW BUSINESS UNITS

From August 20, 1999 until June 21, 2000, we were under the control of an operational receiver, appointed by the Court pursuant to litigation between ITEC and Imperial Bank. The litigation has been dismissed and management has reassumed control. However, management did not have operational control for nearly all of fiscal 2000.

In July 2001, we suspended our printer controller development and manufacturing operations in favor of selling products from other companies to its customers.

In October 2002, we suspended our sales and marketing activities associated with the distribution of office products, including printers, scanners, plotters, and computer networking devices.

ACQUISITION AND SALE OF BUSINESS UNITS

In December 2000, we acquired all of the shares of EduAdvantage.com, Inc., an internet sales organization that sells computer hardware and software products to educational institutions and other customers via its websites: www.eduadvantage.com and www.soft4u.com. During fiscal 2001, we began integrating EduAdvantage operations. However, these operations have not been profitable and we are evaluating the future of this business unit.

In October 2001, we acquired certain assets, for stock, related to our office products and services business activities, representing $250,000 of inventories, fixed assets, and accounts receivable. We have since suspended these operations in favor of concentrating on its software and PEO businesses and the products and services offered by its recent acquisitions.

In November 2001, we acquired SourceOne Group, Inc. (SOG) and operate it as a wholly-owned subsidiary. SOG provides PEO services, including benefits and payroll administration, health and workers' compensation insurance programs, personnel records management, and employer liability management to small and medium-sized businesses.

In March 2002, we acquired all of the outstanding shares of EnStructure, Inc. ("EnStructure), a PEO company, for restricted ITEC common stock. The purchase price may be increased or decreased based upon EnStructure's representations of projected revenues and profits, which are defined in the acquisition agreement.

In May 2002, we entered into an agreement to acquire Dream Canvas, Inc., a Japanese corporation that has developed machines currently used for the automated printing of custom stickers, popular in the Japanese consumer market. We completed the acquisition of Dream Canvas Technology, Inc. (DCT) in October 2002 and paid the sum of $40,000 with the issuance of 100,000 shares of our common stock. In December 2002, we sold DCT to Baseline Worldwide Limited for $75,000 in cash.

In July 2002, we entered into an agreement to acquire controlling interest in Quik Pix, Inc. ("QPI"). QPI shares are traded on the National Quotation Bureau Pink Sheets under the symbol QPIX. On January 14, 2003, we completed the acquisition of shares, representing controlling interest, of QPI.

In August 2002, we entered into an agreement to acquire controlling interest in Greenland Corporation. Greenland shares are traded on the Electronic Bulletin Board under the symbol GRLC. On January 14, 2003, we completed the acquisition of shares, representing controlling interest, of Greenland.

SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES

Management's Discussion and Analysis of Financial Condition and Results of Operations discusses our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. On an on-going basis, we evaluate our estimates and judgments, including those related to allowance for doubtful accounts, value of intangible assets and valuation of non-cash compensation. We base our estimates and judgments on historical experiences and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The most significant accounting estimates inherent in the preparation of our consolidated financial statements include estimates as to the appropriate carrying value of certain assets and liabilities which are not readily apparent from other sources, primarily allowance for doubtful accounts and estimated fair value of equity instruments used for compensation. These accounting policies are described at relevant sections in this discussion and analysis and in the notes to the consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2002.

REVENUE RECOGNITION RELATED TO PEO SEGMENT

We recognizes its revenues associated with its PEO business pursuant to EITF 99-19 "Reporting Revenue Gross as a Principal versus Net as an Agent." Previously, we reported our worksite employees as a component of direct costs, our revenues are now reported net of worksite employee payroll cost (net method). To conform to the net method, we reclassified worksite employee payroll costs for each of its quarters within the fiscal year ended June 30, 2003 and the annual report on Form 10K for the year ended June 30, 2002. These reclassifications had no effect on gross profit, operating loss, or net loss.

RESULTS OF OPERATIONS

Revenues

Revenues were $4,886,000 and $1,016,000 for the three-month period ended September 30, 2003 and 2002, respectively, an increase of $3,870,000 or 381%. The increase in revenues was due primarily to the increase in our PEO customer base and the addition of temporary staffing operations that began on September 1, 2003. Since the acquisition of SOG, we have lost several customers, primarily due to changes in rates for services, especially workers' compensation insurance. Additionally, we elected to terminate certain customers due to profitability concerns. New customers, particularly related to ExpertHR, a wholly-owned subsidiary of Greenland, have been acquired, and more are anticipated pursuant to signed agreements, which we expect will contribute to increased revenues in the current fiscal year.

PEO Services

PEO revenues for the three-month period ended September 30, 2003 and 2002 were $3,952,000 and $392,000, respectively, an increase of $3,560,000 or 908%. The increase in revenues was due primarily to the increase in our PEO customer base and the acquisition of Greenland Corporation in January 2003.

Temporary Staffing

On September 1, 2003, we hired certain employees who had previously worked in the temporary staffing business. As a result, these new employees were able to bring to us their books of business, which resulted in revenues of $767,000 since the date of their hire.

Imaging Products

Sales of imaging products were $131,000 and $486,000 for the three month period ended September 30, 2003 and 2002, respectively, a decrease of $355,000 or 73%. The decrease in product sales was due to the suspension of sales and marketing activities associated with the resale of office products, including copiers, printers, and network solutions. We plan to further evaluate our position related to product sales and marketing.

Revenue from software sales, licensing fees and royalties were $36,000 and $138,000 for the three-month period ended September 30, 2003 and 2002 respectively, a decrease of $102,000 or 74%. The reduction in software revenues was due to our lack of sufficient working capital to support sales and marketing activities. Royalties from the licensing of ColorBlind source code are insignificant and are reported as part of software sales.

Royalties and licensing fees vary from quarter to quarter and are dependent on the sales of products sold by OEM customers using ITEC technologies. These revenues, however, continue to decline, and are expected to decline in the future due to our focus on imaging product sales and our PEO operations as opposed to technology licensing activities.

COST OF PRODUCTS SOLD

Cost of PEO services were $3,151,000 (80% of PEO revenues) and $142,000 (36% of PEO revenues) for the three-month period ended September 30, 2003 and 2002, respectively. The decrease in gross profit is due primarily to increased costs of workers' compensation insurance premiums, which could not be passed on to our clients.

Cost of temporary staffing was $693,000 (90% of temporary staffing revenue). There were no such revenues in the prior-year period.

Cost of products sold were $83,000 (63% of product sales) and $235,000 (48% of product sales) for the three-month period ended September 30, 2003 and 2002, respectively. The decrease in margins is due primarily to the substantial reduction in product sales for the reported periods as a result of the suspension of sales and marketing activities associated with the resale of office products, including copiers, printers, and network solutions.

Cost of software, licenses and royalties were $3,000 (15% of associated revenues) and $21,000 (15% of associated revenues) for the three-month period ended September 30, 2003 and 2002, respectively.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses have consisted primarily of salaries and commissions of sales and marketing personnel, salaries and related costs for general corporate functions, including finance, accounting, facilities and legal, advertising and other marketing related expenses, and fees for professional services.

Selling, general and administrative expenses for the three-month period ended September 30, 2003 and 2002, respectively, were $3,005,000 and $2,053,000 an increase of $952,000 or 46%. The increase is due to the acquisition of Greenland and QPI, and the increased overhead associated with operating a larger company.

COSTS OF RESEARCH AND DEVELOPMENT

There were no costs incurred for research and development in the three months ended September 30, 2003 and 2002.

We have been reducing our research and development costs during the past several quarters. We have suspended most of our engineering and licensing activities associated with OEM printer products and have re-directed our research and development costs toward the support of our ColorBlind software products.

OTHER INCOME AND EXPENSE

Interest and financing costs were $235,000 and $621,000 for the three months ended September 30, 2003 and 2002, respectively. The decrease is a reduction in beneficial conversions of our convertible debt compared to the year-earlier period.

LIQUIDITY AND CAPITAL RESOURCES

Historically, the Company has financed its operations primarily through cash generated from operations, debt financing, and from the sale of equity securities. Additionally, in order to facilitate its growth and future liquidity, the Company has made some strategic acquisitions.

As a result of some of the Company's financing activities, there has been a significant increase in the number of issued and outstanding shares. During the three-month period ended September 30, 2003, the Company issued an additional 84,152,447 shares. These shares of common stock were issued primarily for corporate expenses in lieu of cash, and for the exercise of warrants.

As of September 30, 2003, the Company had negative working capital of $30,232,000, a decrease in working capital of approximately $1,786,000 as compared to June 30, 2003, due primarily to our net loss in the quarterly period ended September 30, 2003.

Net cash used in operating activities was $465,000 for the three month period ended September 30, 2003 as compared to $121,000 for the three months ended September 30, 2002, a increase of $344,000 or 284%, due primarily to the suspension of our business and the additional cash requirements.

Cash used in investing activities was $124,000 for the three month period ended September 30, 2003, an increase of $124,000 (100%) from the year-earlier period.

We have no material commitments for capital expenditures. Our 5% convertible preferred stock (which ranks prior to ITEC's common stock), carries cumulative dividends, when and as declared, at an annual rate of $50.00 per share. The aggregate amount of such dividends in arrears at September 30, 2003, was approximately $387,000.

Our capital requirements depend on numerous factors, including market acceptance of our products and services, the resources we devote to marketing and selling our products and services, and other factors. The report of our independent auditors accompanying our June 30, 2003 financial statements includes an explanatory paragraph indicating there is a substantial doubt about our ability to continue as a going concern, due primarily to the decreases in our working capital and net worth. (Also see Note 2 to the Consolidated Financial Statements.)

RISKS AND UNCERTAINTIES

IF WE ARE UNABLE TO SECURE FUTURE CAPITAL, WE WILL BE UNABLE TO CONTINUE OUR OPERATIONS.

Our business has not been profitable in the past and it may not be profitable in the future. We may incur losses on a quarterly or annual basis for a number of reasons, some within and others outside our control. See "Potential Fluctuation in Our Quarterly Performance." The growth of our business will require the commitment of substantial capital resources. If funds are not available from operations, we will need additional funds. We may seek such additional funding through public and private financing, including debt or equity financing. Adequate funds for these purposes, whether through financial markets or from other sources, may not be available when we need them. Even if funds are available, the terms under which the funds are available to us may not be acceptable to us. Insufficient funds may require us to delay, reduce or eliminate some or all of our planned activities.

To successfully execute our current strategy, we will need to improve our working capital position. The report of our independent auditors accompanying the Company's June 30, 2003 financial statements includes an explanatory paragraph indicating there is a substantial doubt about the Company's ability to continue as a going concern, due primarily to the decreases in our working capital and net worth. The Company plans to overcome the circumstances that impact our ability to remain a going concern through a combination of increased revenues and decreased costs, with interim cash flow deficiencies being addressed through additional equity financing.

IF OUR QUARTERLY PERFORMANCE CONTINUES TO FLUCTUATE, IT MAY HAVE A NEGATIVE IMPACT ON OUR BUSINESS.

Our quarterly operating results can fluctuate significantly depending on a number of factors, any one of which could have a negative impact on our results of operations. The factors include: the timing of product announcements and subsequent introductions of new or enhanced products by us and by our competitors, the availability and cost of products and/or components, the timing and mix of shipments of our products, the market acceptance of our new products and services, seasonality, changes in our prices and in our competitors' prices, the timing of expenditures for staffing and related support costs, the extent and success of advertising, research and development expenditures, and changes in general economic conditions.

We may experience significant quarterly fluctuations in revenues and operating expenses as we introduce new products and services. Accordingly, any inaccuracy in our forecasts could adversely affect our financial condition and results of operations. Demand for our products and services could be adversely affected by a slowdown in the overall demand for imaging products and/or PEO services. Our failure to complete shipments during a quarter could have a material adverse effect on our results of operations for that quarter. Quarterly results are not necessarily indicative of future performance for any particular period.

THE MARKET PRICE OF OUR COMMON STOCK HISTORICALLY HAS FLUCTUATED SIGNIFICANTLY.

Our stock price could fluctuate significantly in the future based upon any number of factors such as: general stock market trends, announcements of developments related to our business, fluctuations in our operating results, a shortfall in our revenues or earnings compared to the estimates of securities analysts, announcements of technological innovations, new products or enhancements by us or our competitors, general conditions in the markets we serve, general conditions in the worldwide economy, developments in patents or other intellectual property rights, and developments in our relationships with our customers and suppliers.

In addition, in recent years the stock market in general, and the market for shares of technology and other stocks have experienced extreme price fluctuations, which have often been unrelated to the operating performance of affected companies. Similarly, the market price of our common stock may fluctuate significantly based upon factors unrelated to our operating performance.

SINCE OUR COMPETITORS HAVE GREATER FINANCIAL AND MARKETING RESOURCES THAN WE DO, WE MAY EXPERIENCE A REDUCTION IN MARKET SHARE AND REVENUES.

The markets for our products and services are highly competitive and rapidly changing. Some of our current and prospective competitors have significantly greater financial, technical, manufacturing and marketing resources than we do. Our ability to compete in our markets depends on a number of factors, some within and others outside our control. These factors include: the frequency and success of product and services introductions by us and by our competitors, the selling prices of our products and services and of our competitors' products and services, the performance of our products and of our competitors' products, product distribution by us and by our competitors, our marketing ability and the marketing ability of our competitors, and the quality of customer support offered by us and by our competitors.

A key element of our strategy is to provide competitively priced, quality products and services. We cannot be certain that our products and services will continue to be competitively priced. We have reduced prices on certain of our products in the past and will likely continue to do so in the future. Price reductions, if not offset by similar reductions in product costs, will reduce our gross margins and may adversely affect our financial condition and results of operations.

The PEO industry is highly fragmented. While many of our competitors have limited operations, there are several PEO companies equal or substantially greater in size than ours. We also encounter competition from "fee-for-service" companies such as payroll processing firms, insurance companies, and human resources consultants. The large PEO companies have substantially more resources than us and provide a broader range of resources than we do.

IF WE ACQUIRE COMPLEMENTARY BUSINESSES, WE MAY NOT BE ABLE TO EFFECTIVELY INTEGRATE THEM INTO OUR CURRENT OPERATIONS, WHICH WOULD ADVERSELY AFFECT OUR OVERALL FINANCIAL PERFORMANCE.

In order to grow our business, we may acquire businesses that we believe are complementary. To successfully implement this strategy, we must identify suitable acquisition candidates, acquire these candidates on acceptable terms, integrate their operations and technology successfully with ours, retain existing customers and maintain the goodwill of the acquired business. We may fail in our efforts to implement one or more of these tasks. Moreover, in pursuing acquisition opportunities, we may compete for acquisition targets with other companies with similar growth strategies. Some of these competitors may be larger and have greater financial and other resources than we do. Competition for these acquisition targets likely could also result in increased prices of acquisition targets and a diminished pool of companies available for acquisition. Our overall financial performance will be materially and adversely affected if we are unable to manage internal or acquisition-based growth effectively. Acquisitions involve a number of risks, including: integrating acquired products and technologies in a timely manner, integrating businesses and employees with our business, managing geographically-dispersed operations, reductions in our reported operating results from acquisition-related charges and amortization of goodwill, potential increases in stock compensation expense and increased compensation expense resulting from newly-hired employees, the diversion of management attention, the assumption of unknown liabilities, potential disputes with the sellers of one or more acquired entities, our inability to maintain customers or goodwill of an acquired business, the need to divest unwanted assets or products, and the possible failure to retain key acquired personnel.

Client satisfaction or performance problems with an acquired business could also have a material adverse effect on our reputation, and any acquired business could significantly under perform relative to our expectations. We cannot be certain that we will be able to integrate acquired businesses, products or technologies successfully or in a timely manner in accordance with our strategic objectives, which could have a material adverse effect on our overall financial performance.

In addition, if we issue equity securities as consideration for any future acquisitions, existing stockholders will experience ownership dilution and these equity securities may have rights, preferences or privileges superior to those of our common stock.

IF WE ARE UNABLE TO DEVELOP AND/OR ACQUIRE NEW PRODUCTS IN A TIMELY MANNER, WE MAY EXPERIENCE A SIGNIFICANT DECLINE IN SALES AND REVENUES, WHICH MAY HURT OUR ABILITY TO CONTINUE OPERATIONS.

The markets for our products are characterized by rapidly evolving technology, frequent new product introductions and significant price competition. Consequently, short product life cycles and reductions in product selling prices due to competitive pressures over the life of a product are common. Our future success will depend on our ability to continue to develop new versions of our ColorBlind software, and to acquire competitive products from other manufacturers. We monitor new technology developments and coordinate with suppliers, distributors and dealers to enhance our products and to lower costs. If we are unable to develop and acquire new, competitive products in a timely manner, our financial condition and results of operations will be adversely affected.

IF THE MARKET'S ACCEPTANCE OF OUR PRODUCTS CEASES TO GROW, WE MAY NOT GENERATE SUFFICIENT REVENUES TO CONTINUE OUR OPERATIONS.

The markets for our products are relatively new and are still developing. We believe that there has been growing market acceptance for color printers, color management software and supplies. We cannot be certain, however, that these markets will continue to grow. Other technologies are constantly evolving and improving. We cannot be certain that products based on these other technologies will not have a material adverse effect on the demand for our products. If our products are not accepted by the market, we will not generate sufficient revenues to continue our operations.

IF WE ARE FOUND TO BE INFRINGING ON A COMPETITOR'S INTELLECTUAL PROPERTY RIGHTS OR IF WE ARE REQUIRED TO DEFEND AGAINST A CLAIM OF INFRINGEMENT, WE MAY BE REQUIRED TO REDESIGN OUR PRODUCTS OR DEFEND A LEGAL ACTION AT SUBSTANTIAL COSTS TO US.

We currently hold no patents. Our software products, hardware designs, and circuit layouts are copyrighted. However, copyright protection does not prevent other companies from emulating the features and benefits provided by our software, hardware designs or the integration of the two. We protect our software source code as trade secrets and make our proprietary source code available to OEM customers only under limited circumstances and specific security and confidentiality constraints.

Competitors may assert that we infringe their patent rights. If we fail to establish that we have not violated the asserted rights, we could be prohibited from marketing the products that incorporate the technology and we could be liable for damages. We could also incur substantial costs to redesign our products or to defend any legal action taken against us. We have obtained U.S. registration for several of our trade names or trademarks, including: PCPI, NewGen, ColorBlind, LaserImage, ColorImage, ImageScript and ImageFont. These trade names are used to distinguish our products in the marketplace.

IF OUR DISTRIBUTORS REDUCE OR DISCONTINUE SALES OF OUR PRODUCTS, OUR BUSINESS MAY BE MATERIALLY AND ADVERSELY AFFECTED.

Our products are marketed and sold through a distribution channel of value added resellers, manufacturers' representatives, retail vendors, and systems integrators. We have a network of dealers and distributors in the United States and Canada, in the European Community and on the European Continent, as well as a growing number of resellers in Africa, Asia, the Middle East, Latin America, and Australia. We support our worldwide distribution network and end-user customers through operations headquartered in San Diego. As of February 7, 2002, we directly employed 6 individuals involved in marketing and sales activities.

A portion of our sales are made through distributors, which may carry competing product lines. These distributors could reduce or discontinue sales of our products, which could adversely affect us. These independent distributors may not devote the resources necessary to provide effective sales and marketing support of our products. In addition, we are dependent upon the continued viability and financial stability of these distributors, many of which are small organizations with limited capital. These distributors, in turn, are substantially dependent on general economic conditions and other unique factors affecting our markets.

INCREASES IN HEALTH INSURANCE PREMIUMS, UNEMPLOYMENT TAXES, AND WORKERS' COMPENSATION RATES WILL HAVE A SIGNIFICANT EFFECT ON OUR FUTURE FINANCIAL PERFORMANCE.

Health insurance premiums, state unemployment taxes, and workers' compensation rates are, in part, determined by our SourceOne subsidiary's claims experience, and comprise a significant portion of SourceOne's direct costs. We employ risk management procedures in an attempt to control claims incidence and structure our benefits contracts to provide as much cost stability as possible. However, should we experience a large increase in claims activity, the unemployment taxes, health insurance premiums, or workers' compensation insurance rates we pay could increase. Our ability to incorporate such increases into service fees to clients is generally constrained by contractual agreements with our clients. Consequently, we could experience a delay before such increases could be reflected in the service fees we charge. As a result, such increases could have a material adverse effect on our financial condition or results of operations.

WE CARRY SUBSTANTIAL LIABILITY FOR WORKSITE EMPLOYEE PAYROLL AND BENEFITS COSTS.

Under our client service agreements, we become a co-employer of worksite employees and we assume the obligations to pay the salaries, wages, and related benefits costs and payroll taxes of such worksite employees. We assume such obligations as a principal, not merely as an agent of the client company. Our obligations include responsibility for (a) payment of the salaries and wages for work performed by worksite employees, regardless of whether the client company makes timely payment to SourceOne of the associated service fee; and (2) providing benefits to worksite employees even if the costs incurred by the SourceOne to provide such benefits exceed the fees paid by the client company. If a client company does not pay us, or if the costs of benefits provided to worksite employees exceed the fees paid by a client company, our ultimate liability for worksite employee payroll and benefits costs could have a material adverse effect on the Company's financial condition or results of operations.

AS A MAJOR EMPLOYER, OUR OPERATIONS ARE AFFECTED BY NUMEROUS FEDERAL, STATE, AND LOCAL LAWS RELATED TO LABOR, TAX, AND EMPLOYMENT MATTERS.

By entering into a co-employer relationship with employees assigned to work at client company locations, we assume certain obligations and responsibilities or an employer under these laws. However, many of these laws (such as the Employee Retirement Income Security Act ("ERISA") and federal and state employment tax laws) do not specifically address the obligations and responsibilities of non-traditional employers such as PEOs; and the definition of "employer" under these laws is not uniform. Additionally, some of the states in which we operate have not addressed the PEO relationship for purposes of compliance with applicable state laws governing the employer/employee relationship. If these other federal or state laws are ultimately applied to our PEO relationship with our worksite employees in a manner adverse to the Company, such an application could have a material adverse effect on the Company's financial condition or results of operations.

While many states do not explicitly regulate PEOs, 21 states have passed laws that have licensing or registration requirements for PEOs, and several other states are considering such regulation. Such laws vary from state to state, but generally provide for monitoring the fiscal responsibility of PEOs and, in some cases, codify and clarify the co-employment relationship for unemployment, workers' compensation, and other purposes under state law. There can be no assurance that we will be able to satisfy licensing requirements of other applicable relations for all states. Additionally, there can be no assurance that we will be able to renew our licenses in all states.

THE MAINTENANCE OF HEALTH AND WORKERS' COMPENSATION INSURANCE PLANS THAT COVER WORKSITE EMPLOYEES IS A SIGNIFICANT PART OF OUR BUSINESS.

The current health and workers' compensation contracts are provided by vendors with whom we have an established relationship, and on terms that we believe to be favorable. While we believe that replacement contracts could be secured on competitive terms without causing significant disruption to our business, there can be no assurance in this regard.

OUR STANDARD AGREEMENTS WITH PEO CLIENTS ARE SUBJECT TO CANCELLATION ON 60-DAYS WRITTEN NOTICE BY EITHER THE COMPANY OR THE CLIENT.

Accordingly, the short-term nature of these agreements make us vulnerable to potential cancellations by existing clients, which could materially and adversely affect our financial condition and results of operations. Additionally, our results of operations are dependent, in part, upon our ability to retain or replace client companies upon the termination or cancellation of our agreements.

A NUMBER OF LEGAL ISSUES REMAIN UNRESOLVED WITH RESPECT TO THE CO-EMPLOYMENT AGREEMENT BETWEEN A PEO AND ITS WORKSITE EMPLOYEES, INCLUDING QUESTIONS CONCERNING THE ULTIMATE LIABILITY FOR VIOLATIONS OF EMPLOYMENT AND DISCRIMINATION LAWS.

Our client service agreement establishes a contractual division of responsibilities between the Company and our clients for various personnel management matters, including compliance with and liability under various government regulations. However, because we act as a co-employer, we may be subject to liability for violations of these or other laws despite these contractual provisions, even if we do not participate in such violations. Although our agreement provides that the client is to indemnify the Company for any liability attributable to the conduct of the client, we may not be able to collect on such a contractual indemnification claim, and thus may be responsible for satisfying such liabilities. Additionally, worksite employees may be deemed to be agents of the Company, subjecting us to liability for the actions of such worksite employees.

IF ALL OF THE LAWSUITS CURRENTLY FILED WERE DECIDED AGAINST US AND/OR ALL THE JUDGMENTS CURRENTLY OBTAINED AGAINST US WERE TO BE IMMEDIATELY COLLECTED, WE WOULD HAVE TO CEASE OUR OPERATIONS.

On or about October 7, 1999, the law firms of Weiss & Yourman and Stull, Stull & Brody made a public announcement that they had filed a lawsuit against us and certain current and past officers and/or directors, alleging violation of federal securities laws during the period of April 21, 1998 through October 9, 1998. On or about November 17, 1999, the lawsuit, filed in the name of Nahid Nazarian Behfarin, on her own behalf and others purported to be similarly situated, was served on us. On January 31, 2003, we executed a Stipulation of Settlement, and the matter was approved by the Superior Court in May 2003. Our insurance company made the required cash settlement payment and the Company issued 5,000,000 shares to fulfill its part of the settlement agreement.

Throughout fiscal 2000, 2001, 2002 and 2003, and through the date of this filing, approximately fifty trade creditors have made claims and/or filed actions alleging the failure of us to pay our obligations to them in a total amount exceeding $1.8 million. These actions are in various stages of litigation, with many resulting in judgments being entered against us. Several of those who have obtained judgments have filed judgment liens on our assets. These claims range in value from less than one thousand dollars to just over one million dollars, with the great majority being less than twenty thousand dollars. Should we be required to pay the full amount demanded in each of these claims and lawsuits, we may have to cease our operations. However, to date, the superior security interest held by Imperial Bank has prevented nearly all of these trade creditors from collecting on their judgments.

IF OUR OPERATIONS CONTINUE TO RESULT IN A NET LOSS, NEGATIVE WORKING CAPITAL AND A DECLINE IN NET WORTH, AND WE ARE UNABLE TO OBTAIN NEEDED FUNDING, WE MAY BE FORCED TO DISCONTINUE OPERATIONS.

For several recent periods, up through the present, we had a net loss, negative working capital and a decline in net worth, which raises substantial doubt about our ability to continue as a going concern. Our losses have resulted primarily from an inability to achieve revenue targets due to insufficient working capital. Our ability to continue operations will depend on positive cash flow, if any, from future operations and on our ability to raise additional funds through equity or debt financing. Although we have reduced our work force and suspended some of our operations, if we are unable to achieve the necessary product sales or raise or obtain needed funding, we may be forced to discontinue operations.

IF AN OPERATIONAL RECEIVER IS REINSTATED TO CONTROL OUR OPERATIONS, WE MAY NOT BE ABLE TO CARRY OUT OUR BUSINESS PLAN.

On August 20, 1999, at the request of Imperial Bank, our primary lender, the Superior Court, San Diego appointed an operational receiver to us. On August 23, 1999, the operational 65receiver took control of our day-to-day operations. On June 21, 2000, the Superior Court, San Diego issued an order dismissing the operational receiver as a part of a settlement of litigation with Imperial Bank pursuant to the Settlement Agreement effective as of June 20, 2000. The Settlement Agreement requires that we make monthly payments of $150,000 to Imperial Bank until the indebtedness is paid in full. However, in the future, without additional funding sufficient to satisfy Imperial Bank and our other creditors, as well as providing for our working capital, there can be no assurances that an operational receiver may not be reinstated. If an operational receiver is reinstated, we will not be able to expand our products nor will we have complete control over sales policies or the allocation of funds.

The penalty for noncompliance of the Settlement Agreement is a stipulated judgment that allows Imperial Bank to immediately reinstate the operational receiver and begin liquidation proceedings against us. We are currently meeting the monthly amount of $150,000 as stipulated by the Settlement Agreement with Imperial Bank. However, the monthly payments have been reduced to $100,000 through January of 2002 and further reduced to $50,000 in 2003.

THE DELISTING OF OUR COMMON STOCK FROM THE NASDAQ SMALLCAP MARKET HAS MADE IT MORE DIFFICULT TO RAISE FINANCING, AND THERE IS LESS LIQUIDITY FOR OUR COMMON STOCK AS A RESULT.

The Nasdaq SmallCap Market and Nasdaq Marketplace Rules require an issuer to evidence a minimum of $2,000,000 in net tangible assets, a $35,000,000 market capitalization or $500,000 in net income in the latest fiscal year or in two of the last three fiscal years, and a $1.00 per share bid price, respectively. On October 21, 1999, Nasdaq notified us that we no longer complied with the bid price and net tangible assets/market capitalization/net income requirements for continued listing on The Nasdaq SmallCap Market. At a hearing on December 2, 1999, a Nasdaq Listing Qualifications Panel also raised public interest concerns relating to our financial viability. While the Panel acknowledged that we were in technical compliance with the bid price and market capitalization requirements, the Panel was of the opinion that the continued listing of our common stock on The Nasdaq Stock Market was no longer appropriate. This conclusion was based on the Panel's concerns regarding our future viability. Our common stock was delisted from The Nasdaq Stock Market effective with the close of business on March 1, 2000. As a result of being delisted from The Nasdaq SmallCap Market, stockholders may find it more difficult to sell our common stock. This lack of liquidity also may make it more difficult for us to raise capital in the future.

Trading of our common stock is now being conducted over-the-counter through the NASD Electronic Bulletin Board and covered by Rule 15g-9 under the Securities Exchange Act of 1934. Under this rule, broker/dealers who recommend these securities to persons other than established customers and accredited investors must make a special written suitability determination for the purchaser and receive the purchaser's written agreement to a transaction prior to sale. Securities are exempt from this rule if the market price is at least $5.00 per share.

The Securities and Exchange Commission adopted regulations that generally define a "penny stock" as any equity security that has a market price of less than $5.00 per share. Additionally, if the equity security is not registered or authorized on a national securities exchange or the Nasdaq and the issuer has net tangible assets under $2,000,000, the equity security also would constitute a "penny stock." Our common stock does constitute a penny stock because our common stock has a market price less than $5.00 per share, our common stock is no longer quoted on Nasdaq and our net tangible assets do not exceed $2,000,000. As our common stock falls within the definition of penny stock, these regulations require the delivery, prior to any transaction involving our common stock, of a disclosure schedule explaining the penny stock market and the risks associated with it. Furthermore, the ability of broker/dealers to sell our common stock and the ability of stockholders to sell our common stock in the secondary market would be limited. As a result, the market liquidity for our common stock would be severely and adversely affected. We can provide no assurance that trading in our common stock will not be subject to these or other regulations in the future, which would negatively affect the market for our common stock.

ITEM 3. CONTROLS AND PROCEDURES

As required by SEC rules, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures at the end of the period covered by this report. This evaluation was carried out under the supervision and with the participation of our management, including our principal executive officer and principal financial officer. Based on this evaluation, these officers have concluded that the design and operation of our disclosure controls and procedures are effective. There were no changes in our internal control over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Disclosure controls and procedures are our controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In October 1999, the law firms of Weiss & Yourman and Stull, Stull & Brody made a public announcement that they had filed a lawsuit against us and certain current and past officers and/or directors, alleging violation of federal securities laws and, in November 1999, the lawsuit, filed in the name of Nahid Nazarian Behfarin, on her own behalf and others purported to be similarly situated, was served on us. In January 2003, we entered into a Stipulation of Settlement with the plaintiffs. We agreed to pay the plaintiffs 5,000,000 shares of common stock and $200,000 in cash. The Parties have accepted the settlement. We have issued the shares, and our insurance carrier has paid the $200,000 cash payment. Pursuant to a hearing in May 2003 the Court provided approval to the settlement.

On August 22, 2002, we were sued by our former landlord, Carmel Mountain #8 Associates, L.P. or past due rent on its former facilities at 15175 Innovation Drive, San Diego, CA 92127. The amount related to this obligation was included as an expense in the year ended June 30, 2003.

ITEC was a party to a lawsuit filed by Symphony Partners, L.P. related to its acquisition of SourceOne Group, LLC. As reported on Form 8-K, dated July 22, 2003, the plaintiffs sought payment of $702 thousand. In June 2003, we entered into a settlement with the plaintiffs for a cash payment of $274 thousand, which has been paid.

ITEC is one of dozens of companies sued by The Massachusetts Institute of Technology, et.al, `related to a patent held by the plaintiffs that may be related to part of the Company's ColorBlind software. Subsequent to the period reported in this filing, in June 2003, we entered into a settlement with the plaintiffs who have agreed to dismiss their claims against us with prejudice in exchange for a settlement fee payment of $10,000, which has been paid.

We have been sued in Illinois state court along with AIA/Merriman, our insurance brokers, by the Arena Football League-2 ("AF2"). Damages payable to AF2, should they win the suit, could exceed $700,000. We expect to defend our position and rely on representations of our insurance brokers.

Throughout fiscal 2000, 2001, and 2002, and through the date of this filing, approximately fifty trade creditors have made claims and/or filed actions alleging the failure of us to pay our obligations to them in a total amount exceeding $3.0 million, which has been reduced to $1.8 million during the 2003. These actions are in various stages of litigation, with many resulting in judgments being entered against us. Several of those who have obtained judgments have filed judgment liens on our assets. These claims range in value from less than one thousand dollars to just over one million dollars, with the great majority being less than twenty thousand dollars.

In connection with ITEC's acquisition of controlling interest of Greenland Corporation, the following are the outstanding legal matters for Greenland Corporation:

Greenland, along with Seren Systems ("Seren"), its then current and primary software developer and supplier for its own ABM terminals, was in the process of completing development of the check cashing service interface to the Mosaic Software host system being implemented to support a large network of V.com terminals. In September 2000, Seren unilaterally halted testing and effectively shut-down any further check cashing development for the V.com project. The parties participating in this project may have been financially damaged, related to the delay in performance by Greenland and Seren. None of the parties have brought suit against Greenland and/or Seren at this time. There is no assurance, however, that such suit(s) will not be brought in the future.

On May 23, 2001 Greenland filed a Complaint in San Diego County naming Michael Armani as the defendant. The Complaint alleges breach of contract by Michael Armani in connection with two separate stock purchase agreements. Greenland seeks damages in the amount of $474,595. On August 7, 2001 Greenland filed a request for Entry of Default against Mr. Armani in the amount of $474,595 and the court granted entry of default. Subsequently Mr. Armani filed a motion to set aside the entry of default and on October 26, 2001 the court granted said motion and the entry of default was set aside. Greenland and Mr. Armani participated in mediation and as a result entered into a settlement agreement whereby Mr. Armani agreed to make certain cash payments to Greenland and the parties entered into mutual release of all claims. Mr. Armani defaulted in his obligation to make the first cash payment and consequently, Greenland obtained a judgment against Mr. Armani for $100,000. Greenland is continuing its efforts to collect on the judgment.

On May 23, 2001 Arthur Kazarian, Trustee for the General Wood Investment Trust (the "Landlord") filed a Complaint in San Diego County naming Greenland as a defendant. The Complaint alleges breach of contract pursuant to the terms of the lease agreement between the Company and the Landlord for the real property located at 1935 Avenida Del Oro, Oceanside, California and previously occupied by Greenland. The Complaint seeks damages in the amount of approximately $500,000. Although Greenland remains liable for the payments remaining for the term of the lease, the Landlord has a duty to mitigate said damages. Greenland recorded a lease termination liability of $275,000 during the year ended December 31, 2001. Greenland entered into a settlement agreement with Arthur Kazarian, Trustee for the General Wood Investment Trust (the "Landlord") where by Greenland agreed to pay the sum of $220,000 to the Landlord in installments payments of $20,000 in May 2002, $50,000 in October 2002 and the remaining balance in December 2002. In the event Greenland defaults in any or all scheduled payments, the Landlord is entitled to a stipulated judgment of approximately $275,000. Greenland was unable to make the scheduled payments and as a result, on July 8, 2002, the Landlord has entered a judgment lien against Greenland in the amount of $279,654.

Greenland entered into an agreement with Intellicorp, Inc. ("Intellicorp") whereby Intellicorp agreed to invest $3,000,000 in exchange for seats on the board of directors and restricted shares of common stock of Greenland. After making the initial payment of $500,000, Intellicorp defaulted on the balance. Greenland sued for recovery of the unpaid $2,500,000. Greenland had issued 46,153,848 shares of common stock for the investment, which were returned to Greenland and cancelled. A default judgment was entered against defendant IntelliCorp, IntelliGroup, and Isaac Chang. In June 2003, a judgment was entered in the Superior Court of the State of California, County of San Diego, against the defendants in favor of Greenland. The amount of the judgment was $3,950,640.02 and was comprised of an award of $2,950,640.02 for compensatory damages and an award of $1,000,000.00 for punitive damages. The Court found, by clear and convincing evidence, that the Defendants acted maliciously and with the intent to defraud Greenland when they entered into a private placement transaction to fund Greenland. The defendant's ability to pay is unknown. The appeal period has expired and we are beginning the collection process.

Max Farrow, a formal officer of Greenland, filed a Complaint in San Diego County naming Greenland, Thomas J. Beener, Intelli-Group, Inc., Intelli-Group LLC and Intelli-Corp, Inc. as defendants. The Complaint alleges breach of contract in connection with Mr. Farrow's resignation as an officer and director of the Company in January 2001. Greenland and Mr. Thomas Beener, entered into a settlement agreement with Max Farrow whereby Mr. Farrow agreed to release Mr. Beener from all claims, obligations etc., in exchange for the issuance of 8 million restricted shares of Greenland common stock. The good faith settlement was approved by the court and the agreed upon consideration was delivered to Mr. Farrow. Greenland entered into a settlement with Farrow whereby Greenland agreed to a judgment of $125,000. However, the judgment will not be enforced until such time as efforts to collect against IntelliCorp et al, have been exhausted. In the event funds are collected from IntelliCorp. Mr. Farrow will receive the first $125,000 plus 50% of the next $200,000 collected. Greenland will retain all amounts collected thereafter.

Fund Recovery, a temporary staffing service filed a complaint against Greenland alleging breach of contract. A summary judgment motion is pending. Greenland recorded the liability amount of $14,000 in the consolidated financial statements.

John Ellis has filed a demand for arbitration in San Diego County against Greenland seeking damages of approximately $70,000 for an alleged breach of contract action. Greenland believes it has valid defenses to the allegations. Mr. Ellis appears to have abandoned this action in arbitration and has elected to pursue a civil suit. However, arbitration action is proceeding .In addition, the parties are attempting mediation to avoid the cost and time of an arbitration proceeding.

John Ellis has filed an action in San Diego County against Greenland seeking damages of approximately $60,000 for an alleged breach of contract action. Greenland believes it has valid defenses to the allegations. This amount was recorded as a liability in the consolidated financial statements. Greenland has filed a motion to quash service of the civil action and to compel arbitration. The court has stayed the proceedings pending the progress and/or outcome of arbitration.

NKS Enterprises, Inc. commenced a legal action against Greenland in San Diego Superior Court in Vista California seeking damages in connection with the purchase and operation of a MaxCash ABM. The case was settled in December 2002. The maximum amount to be paid under the settlement is $100,000. In exchange, Greenland will receive the MaxCash ABM sold to NKS Enterprises. This amount was recorded as a liability in the consolidated financial statements.

In connection with the Company's acquisition of controlling interest of Quik Pix, Inc., we are unaware of any pending litigation.

From time to time, Greenland and QPI may be involved in litigation relating to claims arising out of their operations in the normal course of business.

ITEM 2. CHANGES IN SECURITIES

Common Stock

During the three months ended September 30, 2003, ITEC issued the following unregistered securities:

- 5,220,000 shares of its common stock for legal and consulting services valued at $129,400;

- 10,272,110 shares of its common stock for compensation valued at $140,332;

- 20,260,000 shares of its common stock for debt of $405,200; and

- 48,400,337 shares of its common stock for the conversion of convertible debentures in the amount of $345,562.

Stock Split

On August 9, 2002, the Company's board of directors approved and effected a 1 for 20 reverse stock split. All share and per share data have been retroactively restated to reflect this stock split.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

The Company is currently in default on certain bank loans that have an aggregate outstanding balance at September 30, 2003 of $3,145,000.

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

None

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

10(a) Agreement and Assignment of Rights, dated October 24, 2003, between SourceOne Group, Inc. and ePEO Link.

31.1 Rule 13a-14(a) Certification

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

(b) Reports on Form 8-K

On September 10, 2003, the Registrant filed a Current Report on Form 8-K announcing that on September 3, 2003, the Registrant appointed Pohl, McNabola, Berg & Company, LLP ("PMBC") as the Registrant independent auditors upon the recommendation of its Audit Committee.

On July 22, 2003, Registrant filed a Current Report on Form 8-K announcing that:

- In October 1999, the law firms of Weiss & Yourman and Stull, Stull & Brody made a public announcement that they had filed a lawsuit against the Registrant and certain current and past officers and/or directors, alleging violation of federal securities laws and, in November 1999, the lawsuit, filed in the name of Nahid Nazarian Behfarin, on her own behalf and others purported to be similarly situated, was served on the Registrant. In January 2003, the Registrant entered into a Stipulation of Settlement with the plaintiffs. The Registrant agreed to pay the plaintiffs 5,000,000 shares of common stock and $200,000 in cash. The Parties have accepted the settlement.

- In June 2003, the Registrant entered into a settlement with The Massachusetts Institute of Technology and Electronics For Imaging, related to a patent held by the plaintiffs that was alleged to be related to the Registrant's ColorBlind software products. The plaintiffs have agreed to dismiss its claims against the Registrant with prejudice in exchange for a settlement fee payment of $10,000, which is being paid over a three-month period.

- The Registrant was a party to a lawsuit filed by Symphony Partners, L.P. related to our acquisition of SourceOne Group, LLC. The plaintiffs sought payment of $702,000. In June 2003, the Registrant entered into a settlement with the plaintiffs for a cash payment of $274,000, which has been paid.

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.

Dated: November 24, 2003

IMAGING TECHNOLOGIES CORPORATION (Registrant)

By: /S/ Brian Bonar
____
Brian Bonar
Chairman and Chief Executive Officer

By: /S/ James R. Downey, Jr.
____
James R. Downey, Jr.
Chief Accounting Officer