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IGAMES ENTERTAINMENT INC
Form 10QSB
August 16, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-QSB

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

For the Fiscal Quarter ended June 30, 2004

OR

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

For the transition period from _____ to _____

Commission File No. 000-49723

IGAMES ENTERTAINMENT, INC.

(Exact Name of Small Business Issuer as Specified in its Charter)

Nevada

(State of Other Jurisdiction of
Incorporation or Organization)

88-0501468

(I.R.S. Employer
Identification No.)

700 SOUTH HENDERSON ROAD, SUITE 325, KING OF PRUSSIA, PA 19406

(Address of Principal Executive Offices)

(610) 354-8888

(Issuer's Telephone Number, Including Area Code)

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 August 12, 2004, the issuer had issued and outstanding 5,524,394 shares of its common stock, par value \$0.004 per share.

IGAMES ENTERTAINMENT, INC.
QUARTERLY PERIOD ENDED JUNE 30, 2004

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IGAMES ENTERTAINMENT, INC.

CONSOLIDATED BALANCE SHEET

JUNE 30, 2004
(UNAUDITED)

ASSETS

Current assets:

Cash	\$	395,033
Restricted cash		2,002,376
Accounts receivable		1,185,208
Loans receivable		63,000
Prepaid expenses and other current assets		264,978

Total current assets		3,910,595
Property and equipment, net		395,917
Intangible assets, net		5,506,639
Deferred financing costs		119,586

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\$ 9,932,737
 =====

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Accounts payable	\$ 1,530,923
Accrued expenses	154,390
Current portion of capital lease	17,794
Loans payable	2,000,000
Notes payable	160,000
Lines of credit	5,260,710
Due to officer	335,785
Commissions payable	332,564
Dividends payable	23,875

Total current liabilities	9,816,041

Long-term liabilities:

Capital lease	37,140
---------------------	--------

Stockholders' Equity:

Preferred stock; \$.001 par value, 5,000,000 shares authorized 1,351,640 shares issued and outstanding	1,351
Common stock; \$.004 par value, 50,000,000 shares authorized 5,524,394 shares issued and outstanding	22,097
Additional paid-in capital	10,904,344
Accumulated deficit	(10,848,236)

Total stockholders' equity	79,556

	\$ 9,932,737
	=====

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

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IGAMES ENTERTAINMENT, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS
 (UNAUDITED)

	THREE MONTHS ENDED JUNE 30,	
	2004	2003
	-----	-----
Revenues	\$ 4,614,557	\$ 1,327,088
Operating expenses	3,455,553	963,159
	-----	-----
Gross Profit	1,159,004	363,929
Selling, general and administrative expenses	806,232	266,957

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	-----	-----
Operating profit	352,772	96,972
Other income (expenses):		
Depreciation and amortization	(324,433)	(35,726)
Interest expense, net	(652,351)	(23,548)
Other income	170	-
	-----	-----
	(976,614)	(59,274)
	-----	-----
Net income (loss)	\$ (623,842)	\$ 37,698
	=====	=====
Net income (loss) per common share basic and diluted	\$ (0.12)	\$ 0.01
	=====	=====
Weighted Average Common Shares Outstanding		
-Basic and Diluted	5,156,746	4,042,850
	=====	=====

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

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IGAMES ENTERTAINMENT, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

		Three Months Ended June 30,	
		-----	-----
		2004	2003
		-----	-----
Cash flows from operating activities:			
Net income (loss)	\$ (623,842)	\$	37,698
Adjustments used to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	324,433		35,726
(Increase) decrease in:			
Prepaid expenses and other current assets ..	(73,102)		(5,426)
Accounts receivable	(290,990)		(17,715)
Increase (decrease) in:			
Accounts payable	874,623		100,386
Accrued expenses	41,340		9,631
Commissions payable	294		214,806
	-----		-----
Net cash provided by operating activities	252,756		375,106
	-----		-----
Cash flows from investing activities:			
Purchases of property and equipment	(9,962)		(183,612)
Purchase of intangible assets	-		(9,803)
Purchase of deferred financing	-		(52,162)

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Net cash used in investing activities	(9,962)	(245,577)
Cash flows from financing activities:		
Increase in restricted cash	(1,059,135)	(1,699,899)
Net change in line of credit	2,822,674	1,445,001
Capital lease obligation	-	148,437
Payments on capital lease obligations	(5,446)	(74,218)
Distributions payable to owners	23,875	-
Advances from officer	(3,247)	100,000
Decrease in notes payable	(1,858,500)	-
Dividends	-	(22,500)
Net cash used by financing activities	(79,779)	(103,179)
NET INCREASE IN CASH	163,015	26,350
CASH, beginning of period	232,018	1,363,450
CASH, end of period	\$ 395,033	\$ 1,389,800
Supplemental disclosures:		
Cash paid during the period for interest	\$ 652,351	\$ 23,548
Taxes	\$ -	\$ -

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

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iGAMES ENTERTAINMENT, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION

iGames Entertainment, Inc. (the "Company" or "iGames") was originally incorporated in the State of Florida on May 9, 2001 under the name Alladin Software, Inc. On June 25, 2001, the Company changed its name to iGames Entertainment, Inc. On July 10, 2001, iGames Entertainment, Inc. was incorporated in Nevada, and iGames Entertainment, Inc., a Florida corporation, became a wholly-owned subsidiary.

On January 2, 2004, pursuant to an Amended and Restated Agreement and Plan of Merger (the "Merger Agreement") by and among Money Centers of America, Inc. (Money Centers), Christopher M. Wolfington, iGames, Michele Friedman, Jeremy Stein and Money Centers Acquisition, Inc., a wholly-owned subsidiary of iGames, Money Centers Acquisition, Inc. was merged with and into Money Centers and Money Centers, as the surviving corporation, became a wholly-owned subsidiary of iGames (the "Merger"). For accounting purposes, the transaction was treated as a recapitalization and accounted for as a reverse acquisition. Therefore, the

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financial statements reported herein and accompanying notes thereto reflect the assets, liabilities and operations of Money Centers as if it had been the reporting entity since inception. In connection with the Merger, all of the issued and outstanding shares of capital stock of Money Centers were tendered to iGames and iGames issued to the Money Centers stockholders an aggregate of 1,351,640 shares of iGames Series A Convertible Preferred Stock, \$.001 par value per share, and warrants to purchase an aggregate of 2,500,000 shares of iGames common stock, par value \$.004 per share, at an exercise price of \$.01 per share. Each share of Series A Convertible Preferred Stock is entitled to ten votes in all matters submitted to a vote of iGames shareholders and is convertible at the option of the holders into ten shares of common stock at any time after the date on which iGames amends its articles of incorporation to increase the number of authorized shares of its common stock to at least 125,000,000.

The holders of our Series A Preferred Stock have redemption rights that, if exercised, would require us to redeem our issued and outstanding shares of Series A Preferred Stock and 2,500,000 issued and outstanding stock purchase warrants in exchange for the issued and outstanding common stock of Money Centers of America, Inc.

Money Centers is a single source provider of cash access services to the gaming industry. Money Centers has combined state-of-the-art technology with personalized customer services to deliver the best in ATM, Credit Card Advance, POS Debit, Check Cashing Services, CreditPlus outsourced marker services, and merchant card processing. The Company believes that the acquisition of Money Centers will meet the growing trend towards single source providers of products and services to casinos and other gaming facilities worldwide. This trend supports our business plan to identify fragmented segments of the market to capitalize on merger and acquisition targets of synergistic companies that support our business model. The combined companies will gain wider exposure within the casino and gaming industry.

Pursuant to the terms of a Stock Purchase Agreement between iGames, Helene Regen and Samuel Freshman dated January 6, 2004 (the "Stock Purchase Agreement"), iGames acquired all of the issued and outstanding shares of capital stock of Available Money, a provider of cash access services based in Los Angeles, California. The purchase price of this transaction was \$6,000,000, \$2,000,000 of which was paid in cash at closing, \$1,850,000 of which was paid in cash on April 12, 2004, and \$2,000,000 of which was paid by issuance of 1,470,590 shares of iGames common stock on April 12, 2004.

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IGAMES ENTERTAINMENT, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION (CONTINUED)

The Stock Purchase Agreement provides for adjustment of the purchase price in the event that certain of Available Money's customer contracts do not renew or that the former stockholders of Available Money do not provide iGames with assistance in obtaining renewals of such contracts. We are withholding payment of the remaining \$150,000 of the purchase price in accordance with these provisions of the Stock Purchase Agreement.

The primary assets acquired as a result of this transaction are Available Money's contracts to provide automatic teller machines to 18 customers, 15 of which are traditional casino operations. The former stockholders of Available Money retained the right to receive all payments subsequent to the closing date that relate to services provided by Available Money through December 31, 2003 and are jointly and severally liable for all costs and expenses incurred by

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Available Money relating to services rendered on or before December 31, 2003.

2. UNAUDITED INTERIM INFORMATION

The accompanying unaudited financial statements have been prepared in accordance with generally accepted accounting principles for interim financial statements and pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). The accompanying financial statements for the interim periods are unaudited and reflect all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the periods presented. These financial statements should be read in conjunction with the financial statements and related footnotes for the fiscal year ended March 31, 2004 and notes thereto contained in the annual report on Form 10-KSB as filed with the Securities and Exchange Commission. The results of operations for the three months ended June 30, 2004 are not necessarily indicative of the results for the full fiscal year ending March 31, 2005.

3. NOTES AND LOANS PAYABLE

Notes and loans payable at June 30, 2004 consisted of the following:

	2004

On March 1, 2002, the Company issued a convertible promissory note to an individual in the principal amount of \$100,000. From July 2003 through June 2004, the Company repaid \$90,000 of this debt. The remaining principal balance of this note of \$10,000 continues to bear interest at 10% per annum and is due upon demand.	\$10,000
The Company borrowed \$2,000,000 from Chex Services, Inc. to pay the first \$2,000,000 to the former owners of Available Money. The loan is non-interest bearing and currently in litigation, see note 10.	2,000,000
This represents the remaining \$150,000 of the Available Money Purchase Price. As stated in Note 1 this amount is being withheld from Helene Reagan and Samuel Freshman in accordance to the agreements provisions with regard to the extensions of various contracts.	150,000

	\$2,160,000
	=====

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IGAMES ENTERTAINMENT, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

4. LINES OF CREDIT:

On April 12, 2004 we entered into a term note in the principal amount of \$2,050,000 payable to Mercantile Capital. The note with Mercantile bears interest at 17% and is payable over a 24 month period.

5. STOCKHOLDERS' DEFICIT

We incurred \$6,000,000 of debt associated with our acquisition of Available Money. \$2,000,000 of this indebtedness was paid by tender of an aggregate of 1,470,590 shares of our common stock to the previous shareholders of Available Money. The terms of the Stock Purchase Agreement allow for certain purchase price adjustments associated with this indebtedness that may lower the actual amount we are required to pay. The actual amount paid will not be determined until certain events outlined in the Stock Purchase Agreement have materialized.

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As of the date of this report, we have withheld \$150,000 of the purchase price set forth in the Stock Purchase Agreement due to non-renewal of certain Available Money contracts and claims against Available Money for reimbursement of expenses that they are obligated to pay pursuant to the Stock Purchase Agreement. We have been informed that one of Available Money's casino customers intends to terminate its contract with Available Money prior to the conclusion of the term of the contract. We are confident this termination is outside the provisions of our agreement and the customer has communicated to us that this termination was not due to service or compliance issues, but rather as a part of a contract concession to its lender, who also provides cash access services. At this time, we do not believe that the termination of this contract will have a material adverse effect on our revenues, net income or cash flow from operations. We also believe that we are entitled to a substantial reduction in the purchase price paid pursuant to the Stock Purchase Agreement if this contract is ultimately terminated. We are continuing discussions with this customer and believe that this issue will be resolved during the second quarter of fiscal 2005.

In May 2004, pursuant to the terms an executive's employment contract, the Company granted 62,500 options to purchase shares of our common stock at an exercise price of \$.70 per share.

Pursuant to the terms of a common stock offering with registration rights, the company has accrued penalties in the amount of 37,500 shares. The Company has valued these shares at \$31,960.

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iGAMES ENTERTAINMENT, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

5. STOCKHOLDERS' DEFICIT (CONTINUED)

Stock option and warrant activity for the three months ended June 30, 2004 is summarized as follows:

	Number of Shares	Weighted Average Exercise Price
	-----	-----
Outstanding at March 31, 2004	7,269,064	\$.95
Granted	62,500	.70
Exercised	-	-
Canceled	-	-
	-----	-----
Outstanding at June 30, 2004	7,331,564	\$.95
	=====	=====

The following table summarizes the Company's stock options and warrants outstanding at June 30, 2004:

Options and Warrants Outstanding			
Range of Exercise Price	Number	Weighted Average Remaining Life	Weighted Average Exercise Price
-----	-----	-----	-----
\$2.40 - 4.00	237,500	4.00	\$ 3.24
4.00-6.00	1,286,564	2.25	5.00

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8.00	125,000	9.75	8.00
.01	5,620,000	9.75	.01
.70	62,500	10.00	.70

	7,331,564		
	=====		

All outstanding options and warrants are exercisable at June 30, 2004. Compensation expense, net income or earnings per share would not have changed had the Company applied SFAS No. 123 instead of APB No. 25.

6. COMMITMENTS

a. LEASE COMMITMENTS

In conjunction with converting all of the Available Money ATM's, the Company now pays rent to various mall properties where it has ATM machines. These monthly rents average \$42,000 per month.

The Company is party to a three year lease agreement pursuant to which it rents office space in Pennsylvania at a monthly rent of \$2,200. The first three months of this lease will only require payment of monthly operating expenses.

The Company's total rent expense under operating leases was approximately \$141,703 and \$3,123 for

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IGAMES ENTERTAINMENT, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

6. COMMITMENTS (CONTINUED)

the three months ended June 30, 2004 and 2003, respectively.

7. CONCENTRATION OF CREDIT RISK

The Company maintains cash in bank accounts which exceed federally insured limits. At June 30, 2004, the Company had deposits in excess of federally insured amounts aggregating approximately \$5,325,000 at various financial institutions. The Company believes it has its cash deposits at high quality financial institutions. In addition, the Company maintains a significant amount of cash at each of the casinos. Management believes that the Company has controls in place to safeguard these on-hand amounts, and that no significant credit risk exists with respect to cash.

For the three months ended June 30, 2004, 27% of total revenues were derived from operations at one casino.

8. DUE TO OFFICER

Amounts due to officer are evidenced by notes in the aggregate amounts of \$335,785 that bear interest at a rate of 10% per annum, payable monthly and are due on demand. This amount consists of \$100,000 loaned to the Company by the officer in fiscal year 2004. This amount also includes a bonus due the officer in the amount of \$6,771 from 2002, sales commissions due the officer in the amount of \$21,029 from 2001, sales commissions due the officer in the amount of \$5,000 from fiscal year 2003 and the officer's fiscal year 2004 bonus per his employment agreement in the amount of \$205,800. Payments in the amount of \$2,815 paid to the officer have been netted to this note.

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9. GOING CONCERN

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. The Company has an accumulated deficit of \$10,848,236 as of June 30, 2004 and had net losses for the three months ended June 30, 2004 and a negative working capital of \$5,905,446. These conditions raise substantial doubt about the Company's ability to continue as a going concern.

Management is in the process of implementing its business plan. Additionally, management is actively seeking additional sources of capital, but no assurance can be made that capital will be available on reasonable terms. Management believes the actions it is taking allow the Company to continue as a going concern. The financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

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IGAMES ENTERTAINMENT, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

10. LITIGATION

On March 24, 2004, we filed a complaint in United States District Court for the District of Delaware against Equitex, Inc. and its wholly-owned subsidiary, Chex Services, Inc. d/b/a Fastfunds ("Chex"). In the complaint, we allege that Equitex and Chex committed numerous breaches of the terms of the November 3, 2003 Stock Purchase Agreement pursuant to which we were to have acquired Chex from Equitex, entitling us to terminate the Stock Purchase Agreement and receive a \$1,000,000 termination fee and reimbursement of our transaction costs from Equitex and Chex, that Chex wrongfully and tortiously declared a default under the \$2,000,000 promissory note that we issued to Chex in connection with our acquisition of Available Money, and that Equitex and Chex tortiously interfered with our relationship with our senior lender. We seek to recover the \$1,000,000 termination fee and transaction costs together with significant damages that resulted from the defendants' breaches and tortuous conduct.

On March 23, 2004, Equitex filed an action in Delaware state court concerning the same Stock Purchase Agreement at issue in the Delaware federal action that we filed, alleging that Equitex was entitled to terminate the Stock Purchase Agreement and receive a \$1,000,000 termination fee and reimbursement of transaction costs. We removed this action to the Delaware federal district court. We are vigorously defending this action and believe that Equitex's and Chex's claims are unfounded. We have filed a counterclaim that restates the claims made in the federal action that we filed. We expect that the two Delaware federal actions will be combined into a single case.

On March 15, 2004, Chex filed a complaint in the District Court of the State of Minnesota for the County of Hennepin against us alleging that we defaulted on interest payments on a \$2,000,000 promissory note evidencing our obligation to repay a loan that Chex extended to us in connection with our acquisition of Available Money (the "Minnesota Complaint"). The complaint seeks payment of the principal balance of the loan and accrued interest thereon. Chex further alleged that we are liable to them for a penalty fee of \$1,000,000 as the result of the alleged termination by Equitex of the November 3, 2003 Stock Purchase Agreement. We subsequently removed the Minnesota Complaint to the United States District Court for the District of Minnesota. On June 23, 2004, the United States District Court for the District of Minnesota transferred this action to the United States District Court for the District of Delaware. We anticipate that this action will be consolidated with the other actions listed above that are pending in to the United States District Court for the District of Delaware. We

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are vigorously defending this action, which is still in the pleadings stage, and believe that Chex's claims lack merit.

On July 15, 2004, the former stockholders of Available Money, Inc. filed a lawsuit in the United States District Court for the District of Delaware against us and Christopher M. Wolfington, our Chief Executive Officer. The complaint arises out of our purchase of the capital stock of Available Money, Inc. pursuant to the Stock Purchase Agreement and alleges that we failed to make required payments of the purchase price set forth in the Stock Purchase Agreement. In addition, the former stockholders of Available Money also filed a Motion for a Standstill Order/Temporary Restraining Order that the court denied without a hearing. As we have paid \$3,850,000 and tendered 1,470,590 shares of common stock to the former Available Money stockholders which represents all consideration due to them under the Stock Purchase Agreement, we believe that this lawsuit is frivolous. Accordingly, we believe that the suit was filed for inappropriate purposes and will vigorously defend against this action and seek sanctions for filing of a frivolous suit. We also anticipate filing counterclaims against Howard Regen, Helene Regen and Samuel K. Freshman seeking substantial reduction in the purchase price and other damages and remedies based on fraud and misrepresentations by them in connection with the transaction.

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iGAMES ENTERTAINMENT, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

10. LITIGATION (CONTINUED)

In addition, we are from time to time, during the normal course of our business operations, subject to various litigation claims and legal disputes. We do not believe that the ultimate disposition of any of these matters will have a material adverse effect on our consolidated financial position, results of operations or liquidity.

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CAUTIONARY STATEMENT FOR FORWARD-LOOKING STATEMENTS

THIS QUARTERLY REPORT ON FORM 10-QSB INCLUDES 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. WE HAVE BASED THESE FORWARD-LOOKING STATEMENTS ON OUR CURRENT EXPECTATIONS AND PROJECTIONS ABOUT FUTURE EVENTS. THESE FORWARD-LOOKING STATEMENTS ARE SUBJECT TO KNOWN AND UNKNOWN RISKS, UNCERTAINTIES AND ASSUMPTIONS ABOUT US THAT MAY CAUSE OUR ACTUAL RESULTS, LEVELS OF ACTIVITY, PERFORMANCE OR ACHIEVEMENTS TO BE MATERIALLY DIFFERENT FROM ANY FUTURE RESULTS, LEVELS OF ACTIVITY, PERFORMANCE OR ACHIEVEMENTS EXPRESSED OR IMPLIED BY SUCH FORWARD-LOOKING STATEMENTS. IN SOME CASES, YOU CAN IDENTIFY FORWARD-LOOKING STATEMENTS BY TERMINOLOGY SUCH AS "MAY," "WILL," "SHOULD," "COULD," "WOULD," "EXPECT," "PLAN," "ANTICIPATE," "BELIEVE," "ESTIMATE," "CONTINUE," OR THE NEGATIVE OF SUCH TERMS OR OTHER SIMILAR EXPRESSIONS. FACTORS THAT MIGHT CAUSE OR CONTRIBUTE TO SUCH A DISCREPANCY INCLUDE, BUT ARE NOT LIMITED TO, THOSE INCLUDED IN OUR ANNUAL REPORT ON FORM 10-KSB FILED ON JULY 13, 2004. THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH OUR CONSOLIDATED FINANCIAL STATEMENTS AND RELATED NOTES THERETO INCLUDED ELSEWHERE IN THIS REPORT.

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

The following discussion of the results of operations, financial condition and liquidity should be read in conjunction with our financial

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statements and notes thereto for the fiscal year ended March 31, 2004 appearing in our most recent annual report on Form 10-KSB as filed with the Securities and Exchange Commission on July 13, 2004.

HISTORY

iGames was incorporated in the State of Florida on May 9, 2001 under the name Alladin Software, Inc. On June 25, 2001, it changed its name to iGames Entertainment, Inc. On July 10, 2001, iGames Entertainment, Inc. was incorporated in Nevada, and iGames Entertainment, Inc., a Florida corporation, became a wholly-owned subsidiary. On January 2, 2004, iGames acquired Money Centers pursuant to the merger of Money Centers with a wholly-owned subsidiary of iGames formed for that purpose. In addition, on January 6, 2004, iGames acquired the stock of Available Money, the operator of free-standing ATM machines in casinos. The business operations of Available Money have been combined with those of Money Centers.

The merger with Money Centers was accounted for as a reverse acquisition. Although we were the legal acquirer in the merger, Money Centers was the accounting acquirer since its shareholders acquired a majority ownership interest in our company. Consequently, the historical financial information included in the financial statements prior to January 2004 is that of Money Centers. All significant intercompany transactions and balances have been eliminated. We do not present pro forma information as the merger is a recapitalization and not a business combination.

From inception until the acquisition of Money Centers, we were engaged in developing, marketing, and distributing gaming and security applications for the casino, hospitality, and entertainment industries. However, with the acquisition of Money Centers and Available Money, we have ceased these activities and have focused on the development and expansion of Money Centers' business.

Money Centers was incorporated in the State of Delaware in 1997, but was inactive until 1999. Money Centers' business model is to be an innovator and industry leader in cash access and financial management services for the gaming industry. Within the funds transfer and processing industries there exists niche markets that are capable of generating substantial operating margins without the requirement to process billions of dollars in transactions that is the norm for the industry. We believe there is significant value to having a proprietary position in each phase of the transaction process in the niche markets where management has a proven track record. The gaming industry is an example of such a market and is currently where we derive the majority of our revenues. We have identified other markets with similar opportunities, however we have not executed any plans to exploit these markets at this time.

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From October 1999 until March 2001, Money Centers was a development company focusing on the completion of a Point of Sale ("POS") transaction management system for the gaming industry. In March 2001, Money Centers commenced operations with the launch of the POS system at the Paragon Casino in Marksville, LA. With the acquisition of Available Money, we currently provide services in 22 locations across the United States.

CURRENT OVERVIEW

We completed our acquisitions of Money Centers and Available Money in January 2004. We are continuing to aggressively pursue our integration of these acquisitions into our business and to complete the conversion of all of processing of the Available Money cash services business over to the systems

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utilized by Money Centers. These conversions are timely and expensive, as they include the purchase of new ATM hardware. We anticipate that this conversion will cost us approximately \$700,000 in fiscal 2005. Through June 30, 2004, we had incurred approximately \$200,000 in connection with this conversion and believe that the conversion is approximately 25% complete.

We have also executed a plan to restructure our management team in an effort to streamline our operations and reduce our selling, general and administrative expenses. We believe that the changes resulting from this restructuring plan will save us approximately an additional \$200,000 more per year than we had originally anticipated. We expect to start realizing these savings in the second quarter of fiscal year 2005.

In fiscal 2005, we have met or exceeded our projected number of transactions in each of our product lines. In addition, we believe that we have sufficient capacity to handle additional customer accounts at our present level of staffing and using our current systems and infrastructure. While our interest expense has been higher than we anticipated, we are attempting to re-finance our lines of credit to obtain more favorable financing arrangements, which will lower our expenses and contribute to our profitability.

We seek to avoid litigation and to minimize our exposure to potential claims arising in the normal course of our business and as a result of our acquisitions. Despite these efforts, we have been named as a defendant in several legal proceedings described in Part II, Item 1. Legal Proceedings beginning on page 21 of this report. We are confident that it is in our best interests to defend these claims and to pursue counterclaims where we believe that we are likely to obtain a favorable result. During the three months ended June 30, 2004, we have incurred approximately \$138,000 in legal fees related to these legal proceedings and anticipate incurring a substantial amount of additional legal fees related to these legal proceedings throughout fiscal year 2005.

We generate revenues from transaction fees associated with each unique service we provide, including ATMs, credit card advances, POS Debit, check cashing, markers and various other financial instruments. We receive our fees from either the casino operator or the consumer who is requesting access to their funds. The pricing of each transaction type is determined by evaluating risk and costs associated with the transaction in question. Accordingly, our transaction fees have a profit component built into them. This is why the gaming industry, which is recognized for its high transaction volume, is such a lucrative market. Furthermore, reimbursement for electronic transactions are guaranteed by the credit or debit networks and associations that process the transactions as long as procedures are followed, thereby virtually eliminating trade accounts receivable.

Companies providing cash access services to the gaming industry face some unique challenges and opportunities in the next ten years. Many companies in the industry have merged, been acquired or have recapitalized in order to capitalize on the trends identified in the gaming industry.

Historically, providers of cash access services to the gaming industry recognized cash flow margins that were unmatched in the funds transfer and processing industries. Growing competition and the maturing of the market has resulted in a decline in these margins as companies have begun marketing their services based on price rather than innovation or value added services. This trend is highlighted by the number of companies that promote revenue growth and an increased account base but experience little increase in net income. This trend is magnified by the fact that the largest participant in the industry has close to 70% market share and has begun to forgo margin in order to retain business. Companies that can adapt to the changing market and can create innovative products and services stand at the forefront of new wave in revenue

and profit growth.

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Substantially all gaming facilities provide ATM services, credit card cash advances, debit, and/or check cashing services to their customers. Services are typically outsourced and provided on an exclusive basis for an average of two to five years. Each year, approximately 400 accounts totaling \$300 million in revenue are put out to bid. Currently there are five major companies, including us, that have proprietary systems to compete for this business. Although this market has matured from a pricing perspective, the demand for the services from the end user is still strong.

Like most maturing markets, the companies that succeed are those that are capable of reinventing themselves and the markets they serve. We believe that smaller gaming properties will always look to have cash access services provided in the traditional manner. There are several major trends occurring in the gaming industry that will have a major impact on our industry and will determine which companies emerge as industry leaders:

1. Consolidation of major casino companies that will put pressure on other major casino companies to follow suit and will put pressure on smaller casino companies to focus on service and value added amenities in order to compete.

The consolidation of the major gaming companies will make it difficult to continue to offer our services in the traditional manner. The economics are too compelling for the gaming operators not to consider internalizing these operations in order to generate additional revenue and profits to service the debt associated with the consolidation. We have prepared for this change and have already begun to offer our systems and services through the issuance of Technology and Use Agreements. Instead of outsourcing the cash services operations, we have begun to offer turn-key processing capabilities for internal use by the casino. This means casinos will license our technology so they can operate and maintain their own cash access services, including the addition of their merchant card processing. Our size makes us uniquely capable of adapting to this change. Though the license agreements do not have the same revenue potential as a traditional cash services contract, the net income derived from these agreements is higher, the user agreements are for a longer period of time and we do not have the same capital expenditures or vault cash requirements that we experience in performing traditional cash access services. Furthermore, our larger competitors have spent years trying to conceal the economic benefits of this type of offering because their large infrastructure is designed to only support an outsourced solution.

2. Ticket In-Ticket Out technology growth exceeding expectations.

The first major casino company to remove coins from the casino floor was Caesars Palace in Atlantic City, NJ. Since then, slot machine manufacturers have developed a technology that prints and accepts bar-coded tickets at the slot machine instead of accepting or dispensing coins. It was originally anticipated that it would take 10-15 years for the industry to fully adopt this technology. It appears it may only take half this amount of time. This presents a problem to casino operators. They now have tens of thousands of bar-coded tickets a day that need to be redeemed for cash. This has paved the way for self-service ticket redemption technology so customers do not have to go to the casino cage in order to redeem their tickets. The initial ticket redemption machines placed in service have proven to be too big and too expensive. Most casino operators have to wait until budget season to appropriate the necessary funds in order to even consider the acquisition of the required equipment. We believe this functionality will ultimately reside on the ATM machine thus

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eliminating the requirement to purchase new equipment and eliminating the need to remove a slot machine to make room for a stand-alone ticket redemption device. We are developing technology that will allow ticket-redemption functionality on our cash access devices. There is still the problem of security with the bar-coded ticket, which is as good as cash. Many casino operators will refuse to allow vendors to handle the tickets for security and fraud concerns. This is an additional economic benefit of our plan to have the casino operator internalize their cash access services because only the casino's personnel will handle the tickets in the situations where they are licensing our services.

3. Execution of long-term and stable compacts for Indian Casinos in numerous state jurisdictions has made traditional capital more readily available paving the way for a new wave of expansion and the resulting need for new sources of revenue and customer amenities.

Recent shortfalls in state budgets have brought the tribal and state governments together to execute long-term compacts that meet the financial needs of both parties. In recent years, California, Arizona, New Mexico and Wisconsin are just a few examples of this development. The added financial stability for Indian casinos has made

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traditional capital more readily available to tribes, leading many tribes to undertake expansion of casino facilities and operations.

In order to support this expansion, Indian casino operators will seek new sources of revenues and new amenities to attract and retain more quality customers. One of the most critical customer amenities in casino operations is the availability of credit. Traditional gaming markets, such as Las Vegas and Atlantic City, rely on credit issuance for up to 40% of their revenues. These markets issue credit internally and rely on specialized credit reporting in their risk management decisions. Significant capital investment in technology is required for these transactions to be executed efficiently. However, within the \$15 billion dollar Indian Gaming market there are virtually no credit services currently available. Approximately 26 of 29 states that have approved Indian Gaming do not allow the Tribes or their respective casinos to issue credit. The lack of credit play is also due to the lack of a third party credit issuer that is capable of facilitating the transactions. Our Credit Plus platform allows Indian casinos to issue credit to players, providing Indian casinos with a guest amenity that is already widely accepted in traditional jurisdictions.

Our Cash Services Host Program is uniquely aimed at capitalizing on the need for new profitable guest amenities. Where most guest amenities require additional expenses, this service helps the casino operator generate more revenues. This service allows customers to facilitate cash access transactions from the slot machine or gaming table. Our hosts are available to bring the transaction to the guest, which is viewed as a valuable customer amenity, while driving more money to the gaming floor for the casino operator.

Organic growth through sales by internal salespeople is usually the most efficient and profitable growth strategy in the cash services business. Much of Money Centers' historical growth has occurred in this manner. We realize that recognizing industry trends is no assurance of success. We continue to view strategic acquisitions as part of our business plan to obtain the critical mass we believe is necessary to compete effectively in our industry.

This parallel strategy of sales, acquisitions and product development is capital intensive and presents substantial risk. There is no guarantee that we will be able to manage all three strategies effectively.

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We believe that it is necessary to increase our working capital position so that we can capitalize on the profitable trends in the industry while maintaining and servicing our current customer base. A major risk to our business is that we utilize working capital for future growth at the expense of executing on our integration and conversion plans. This would result in substantially higher operating costs without the assurance of additional revenues to support such costs.

CRITICAL ACCOUNTING POLICIES

In presenting our financial statements in conformity with accounting principles generally accepted in the United States, we are required to make estimates and assumptions that affect the amounts reported therein. Several of the estimates and assumptions we are required to make relate to matters that are inherently uncertain as they pertain to future events. However, events that are outside of our control cannot be predicted and, as such, they cannot be contemplated in evaluating such estimates and assumptions. If there is a significant unfavorable change to current conditions, it will likely result in a material adverse impact to our consolidated results of operations, financial position and in liquidity. We believe that the estimates and assumptions we used when preparing our financial statements were the most appropriate at that time. Presented below are those accounting policies that we believe require subjective and complex judgments that could potentially affect reported results.

Check Cashing Bad Debt. The principal source of bad debts that we experience are due to checks presented by casino patrons that are ultimately returned by the drawer's bank for insufficient funds. We account for these check cashing bad debts on a cash basis. Fees charged for check cashing are recorded as income on the date the check is cashed. If a check is returned by the bank on which it is drawn, we charge the full amount of the check as a bad debt loss. If the check is subsequently honored by the bank, we recognize the amount of the check as a negative bad debt. This conservative accounting policy may at times overstate the impact of bad checks on our financial results, and adoption of a different accounting policy could have a material impact on our reported results.

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Goodwill and Long-Lived Intangible Assets. The carrying value of goodwill as well as other long-lived intangible assets such as contracts with casinos is reviewed if the facts and circumstances suggest that they may be impaired. With respect to contract rights in particular, which have defined terms, this will result in an annual adjustment based on the remaining term of the contract. If this review indicates that the assets will not be recoverable, as determined based on our discounted estimated cash flows over the remaining amortization period, then the carrying values of the assets are reduced to their estimated fair values in accordance with Statement of Financial Accounting Standards No. 144, ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS ("FAS 144"). The calculation of fair value includes a number of estimates and assumptions, including projections of future income and cash flows, the identification of appropriate market multiples and the choice of an appropriate discount rate.

Stock Based Compensation. We account for stock based compensation utilizing Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), which encourages, but does not require, companies to record compensation cost for stock-based employee compensation plans at fair value. We have chosen to account for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees", and related interpretations.

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Accordingly, compensation cost for stock options is measured as the excess, if any, of the estimated fair market value of our stock at the date of the grant over the amount an employee must pay to acquire the stock. We have adopted the "disclosure only" alternative described in SFAS 123 and SFAS 148 (See New Accounting Pronouncements), which require pro forma disclosures of net income and earnings per share as if the fair value method of accounting had been applied.

RESULTS OF OPERATIONS

THREE MONTHS ENDED JUNE 30, 2004 VS. THREE MONTHS ENDED JUNE 30, 2003

	Three Months Ended June 30, 2004 (\$)	Three Months Ended June 30, 2003 (\$)	Change (\$)
	-----	-----	-----
Net Income (Loss)	(623,842)	37,698	(661,540)
Revenues	4,614,557	1,327,088	3,287,469
Operating Expenses	3,455,553	963,159	2,492,394
Selling, General and Administrative Expenses ...	806,232	266,957	539,275
Other Income (Expenses)	(976,614)	(59,274)	(917,340)

Our net loss increased during the three months ended June 30, 2004 due to non-recurring expenses related to the integration of our acquisitions of Money Centers and Available Money into our business, higher interest expenses related to our increased sales volume and high legal expenses related to legal proceedings that we anticipate may continue throughout fiscal year 2005.

Our revenues increased by approximately 248% during the three months ended June 30, 2004 as compared to the three months ended June 30, 2003. Our revenues increased during the three months ended June 30, 2004 due to a 6% increase in Money Centers' sales over the prior period and the acquisition of Available Money at the beginning of the fourth quarter of fiscal 2004, adding 91 ATM's at 18 locations throughout the United States. In addition, Money Centers experienced increased transaction volume. In calendar year 2003, Money Centers' POS system facilitated 892,915 transactions (75% increase over calendar year 2002) totaling \$140,536,954 (44% increase over calendar year 2002) generating over \$5.5 million in revenue (63% increase over calendar year 2002). Assuming no additional customer sales, for calendar year 2004 we are on pace to facilitate over 5.0 million transactions totaling over \$578,000,000. During the six months ended June 30, 2004, Money Centers' POS system facilitated approximately 3,571,000 transactions totaling

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approximately \$373,000,000. Our results of operations and revenue growth exceeded expectations though our number of new accounts was lower than anticipated. However, at the end of fiscal year 2004, we were successful in launching two major products that are essential to our future success; CreditPlus and our Cash Services Host Program, both of which are currently generating new revenues and profits.

Our operating expenses increased during the three months ended June 30, 2004 due to the transaction processing expenses and casino commissions related to the increase in our transaction volume. In addition, some of the new casino contracts provided for higher casino commissions than under our existing contracts.

Our selling, general and administrative expenses increased during the three months ended June 30, 2004 primarily due to \$140,000 in expenses related

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to the conversion of all of processing of the Available Money cash services business over to the systems utilized by Money Centers, \$140,000 of rent expense related to Available Money contracts and mall properties, and \$138,000 in legal fees related to pending legal proceedings.

Our other expenses increased during the three months ended June 30, 2004 mostly due to a \$628,803 increase in interest expense. This increase was due to us having \$5,260,710 of our lines of credit used at June 30, 2004 at an average interest rate of 14.9% as opposed to \$2,438,038 of our lines of credit used at June 30, 2004 at an average interest rate of 12.5%. These additional draws on our lines of credit were necessary to satisfy our increased transaction volume and to make the second cash payment of purchase price to the former stockholders of Available Money. We are in the process of evaluating our options to re-finance our existing lines of credit at a lower rate of interest. In addition, our vault cash expense related to the conversion of Available Money's ATMs to Money Centers' systems has been approximately three times higher than the anticipated level. We have identified the problem and are in the process of resolving it. We anticipate that we will continue to incur this higher interest expense related to the conversion of the ATMs through the second quarter of fiscal 2005 but are confident that we will lower this expense to anticipated levels in the third quarter of fiscal 2005. Our other expenses also increased during the three months ended June 30, 2004 due to a \$287,707 increase in depreciation and amortization expenses. These expenses increased due to an increase in amortization expense due to the amortization of Available Money's contract rights over their terms.

OFF-BALANCE SHEET ARRANGEMENTS

There were no off-balance sheet arrangements during the fiscal quarter ended June 30, 2004 that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to our investors.

CHANGES IN FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES

	Three Months Ended June 30, 2004 (\$)	Three Months Ended June 30, 2003 (\$)	Change (\$)
Net Cash Provided by			
Operating Activities	252,756	375,106	(122,350)
Net Cash Used in			
Investing Activities	(9,962)	(245,577)	235,615
Net Cash Used in			
Financing Activities	(79,779)	(103,179)	23,400

Net cash provided by operating activities decreased during the first three months of June 30, 2004 primarily due to our significant net loss and increases in accounts receivable and prepaid expenses, offset by increased depreciation and amortization and a significant increase in accounts payable.

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Net cash used in investing activities decreased during the first three months of fiscal year 2005 due to a significant decline in the amount of tangible and intangible assets purchased and the amount of deferred financing costs.

Net cash used in financing activities decreased during the first three months of fiscal year 2005 due to our decrease in notes payable and increase in restricted cash offset by an increase in the amounts drawn on our lines of

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credit.

Our available cash equivalent balance at June 30, 2004 was approximately \$395,033 and was approximately \$84,724 at July 31, 2004. From inception through March 31, 2003, we raised an aggregate of approximately \$2,500,000 in capital through the sale of our equity securities. In addition, we issued two 10% convertible promissory notes in the aggregate principal amount of \$250,000 to one investor. In October 2002, this investor converted a \$150,000 note into 300,000 shares of our common stock, and from July 2003 through December 2003, we repaid an additional \$90,000 of this debt. We intend to repay the remaining principal balance of this note of \$10,000 in fiscal 2005.

In January 2004, we completed our merger with Money Centers and our acquisition of Available Money. Each of Money Centers and Available Money have established operations. In addition, Money Centers has an existing vault cash line of credit of \$3,000,000. All of this line of credit is available to fund our vault cash needs. We must obtain the consent of the lender to use any of this line to fund our other operating expenses. Management believes that these sources of cash flow will be sufficient to fund our operations for at least the next twelve months.

A significant portion of our existing indebtedness is associated with our line of credit of \$3,000,000 with Mercantile Capital, L.P., which we use to provide vault cash for our operations. Vault cash is not working capital but rather the money necessary to fund the float, or money in transit, that exists when customers utilize our services but we have yet to be reimbursed from the Debit, Credit Card Cash Advance, or ATM networks for executing the transactions. Although these funds are generally reimbursed within 24-48 hours, due to the magnitude of our transaction volume, a significant amount of cash is required to fund our operations. Our vault cash loan accrues interest at the base commercial lending rate of Wilmington Trust Company of Pennsylvania plus 10.75% per annum on the outstanding principal balance, with a minimum rate of 15% per annum, and has a maturity date of May 31, 2005. Our obligation to repay this loan is secured by a first priority lien on all of our assets.

We incurred \$6,000,000 of debt associated with our acquisition of Available Money. \$2,000,000 of this indebtedness was paid by tender of an aggregate of 1,470,590 shares of our common stock to the previous shareholders of Available Money. The terms of the Stock Purchase Agreement allow for certain purchase price adjustments associated with this indebtedness that may lower the actual amount we are required to pay. The actual amount paid will not be determined until certain events outlined in the Stock Purchase Agreement have materialized. As of the date of this report, we have withheld \$150,000 of the purchase price set forth in the Stock Purchase Agreement due to non-renewal of certain Available Money contracts and claims against Available Money for reimbursement of expenses that they are obligated to pay pursuant to the Stock Purchase Agreement. We have been informed that one of Available Money's casino customers intends to terminate its contract with Available Money prior to the conclusion of the term of the contract. We are confident that the contract does not permit early termination and this customer has communicated to us that this termination was not due to service or compliance issues but as the result of a contract concession to its lender, who also provides cash access services. At this time, we do not believe that the termination of this contract will have a material adverse effect on our revenues, net income or cash flow from operations. We also believe that we are entitled to a substantial reduction in the purchase price paid pursuant to the Stock Purchase Agreement if this customer ultimately terminates this contract. We are continuing discussions with this customer and believe that this issue will be resolved during the second quarter of fiscal 2005.

An additional \$2,000,000 of this indebtedness is a loan provided by Chex Services, Inc. We have filed suit against Chex Services regarding certain

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breaches to the term note evidencing our obligation to repay this loan and breaches to a Stock Purchase Agreement entered into by the parties in November 2003. It is our position that the damages we suffered as a result of the breaches by Chex Services, Inc. exceed the principal amount of this loan. We will continue to record this note as a liability until a judgment is rendered in the lawsuit.

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The final \$2,000,000 of this indebtedness is a bridge loan provided by Mercantile Capital, L.P. This bridge loan accrues interest at an annual rate of 17% and has a maturity date of May 1, 2005. Our obligation to repay this loan is secured by a first priority lien on all of our assets. We intend to refinance this obligation in fiscal 2005. We paid a facility fee of \$41,000 in connection with this loan.

Though we anticipate our operating profits will be sufficient to meet our current obligations under our credit facilities, if we become unable to satisfy these obligations, then our business will be adversely affected as Mercantile Capital will execute its lien and sell our assets to satisfy any amount of outstanding indebtedness under our line of credit loan or our term loan that we are unable to repay.

We also have a substantial amount of accounts payable and accrued expenses. To the extent that we are unable to satisfy these obligations as they come due, we risk the loss of services from our vendors and possible lawsuits seeking collection of amounts due.

In addition, we have an existing obligation to redeem 37,500 shares of our common stock from an existing stockholder at an aggregate price of \$41,250. This obligation arose in connection with our purchase of certain gaming software products for 75,000 shares of our common stock. In order to complete this transaction under these terms, our former management granted this stockholder the option to have 37,500 shares of his stock redeemed. This stockholder has elected to exercise this redemption option.

We are also in the process of converting out all of the former Available Money ATMs that are presently processed by Fifth Third Bank and replacing them with new ATMs, which we will process through our own systems. As part of this process we will replace all of the ATMs at the locations that Available Money presently provides ATM service. Under the agreement with Fifth Third Bank, Fifth Third Bank recognized all revenues and expenses from these ATMs, and Available Money recognized only its share of net income generated by these ATMs. Following this conversion. We will recognize all revenues and expenses from the ATMs, resulting in increased revenues and operating expenses of approximately \$9,800,000 and \$8,200,000, respectively, per year. We anticipate that this conversion will cost approximately \$700,000 to complete in fiscal 2005. As we plan to process all transactions at these ATMs, we will recognize all fees generated as revenues. If we did not convert these ATM's and allowed their transactions to be processed by a third party, then we would only be permitted to record the fees net of processing costs as revenues.

Our goal is to change the way our customers view cash access services through transforming the way casinos find, serve and retain their customers. We will strive to make our customers the best they can be by continuing to grow and improve everything we do. We require significant capital to meet these objectives. Our capital requirements are as follows:

- o **Equipment:** Each new account requires hardware at the location level and some additions to network infrastructure at our central server farm.

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- o Vault Cash: All contracts in which we provide full service money centers and ATM accounts for which we are responsible for cash replenishment require vault cash. Vault cash is the money necessary to fund the float that exists when we pay money to patrons but have yet to be reimbursed from the Debit, Credit Card Cash Advance, or ATM networks for executing the transactions.
- o Acquisition Financing: We presently have little to no cash for use in completing additional acquisitions. To the extent that we cannot complete acquisitions through the use of our equity securities, we will need to obtain additional indebtedness or seller financing in order to complete such acquisitions.
- o Working Capital: We will require substantial working capital to pay the costs associated with our expanding employee base and to service our growing base of customers.
- o Technology Development: We will continue to incur development costs related to the design and development of our new products and related technology. We presently do not have an internal staff of engineers or software development experts and intend to outsource this function.

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We are actively seeking various sources of growth capital and strategic partnerships that will assist us in achieving our business objectives. We are also exploring various potential financing options and other sources of working capital. There is no assurance that we will succeed in finding additional sources of capital on favorable terms or at all. To the extent that we cannot find additional sources of capital, we may be delayed in fully implementing our business plan.

The holders of our Series A Preferred Stock have redemption rights that, if exercised, would require us to redeem our issued and outstanding shares of Series A Preferred Stock and 2,500,000 issued and outstanding stock purchase warrants in exchange for the issued and outstanding common stock of Money Centers of America, Inc. If these redemption rights are exercised, we will lose a significant portion of our existing operations and our results of operations will decline. In addition, there would also be significant risk that our remaining operations would be eliminated as the vault cash lines of credit and debt that we incurred in connection with our acquisition of Available Money are guaranteed by the majority holder of the Series A Preferred Stock. These credit facilities could potentially go into default as a result of the exercise of the Series A Preferred redemption rights, which would leave us without the vault cash necessary to operate our remaining business. A special committee of our board of directors has reached an agreement with the holders of our Series A Preferred Stock pursuant to which we will complete a recapitalization which will, among other things, result in the termination of these redemption rights and effective conversion to common stock of the Series A Preferred Stock and certain warrants issued in our acquisition of Money Centers. Following the recapitalization, the holders of our Series A Preferred Stock and those warrants will own an aggregate of approximately 85% of our issued and outstanding capital stock (calculated on a fully diluted basis) as opposed to the approximately 81% they presently own.

We do not pay and do not intend to pay dividends on our common stock. We believe it to be in the best interest of our stockholders to invest all available cash in the expansion of our business. We presently have a liability for dividends payable of \$23,875 related to dividends declared by Money Centers prior to our merger that have not yet been paid.

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Due to our accumulated deficit of \$10,224,394 as of March 31, 2004, our net losses and cash used in operations of \$6,634,586 and \$158,948, respectively, for the year ended March 31, 2004, our independent auditors have raised substantial doubt about our ability to continue as a going concern. At June 30, 2004, our accumulated deficit was \$10,848,236. During the three months ended June 30, 2004, our net losses were \$623,842. However, net cash provided by operating activities was \$252,756. While we believe that our present plan of operations will be profitable and will generate positive cash flow, there is no assurance that we will generate net income or positive cash flow in fiscal year 2005 or at any time in the future.

ITEM 3 - CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of June 30, 2004 (the "Evaluation Date"), and, based on their evaluation, our chief executive officer and chief financial officer have concluded that these controls and procedures were effective as of the Evaluation Date. There were no significant changes in our internal controls or in other factors that could significantly affect these controls during the quarter ended June 30, 2004.

Disclosure controls and procedures (as defined in the Exchange Act Rules 13a-14(c) and 15d-14(c)) are controls and other procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act are recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to management to allow timely decisions regarding required disclosure.

The Certifying Officers have also indicated that there were no significant changes in our internal controls or other factors that could significantly affect such controls subsequent to the date of their evaluation, and there were no corrective actions with regard to significant deficiencies and material weaknesses.

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Our management, including each of the Certifying Officers, does not expect that our disclosure controls or our internal controls will prevent all error and fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. In addition, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the control. The design of any systems of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of these inherent

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limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

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PART II - OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS

On March 24, 2004, we filed a complaint in United States District Court for the District of Delaware against Equitex, Inc. and its wholly-owned subsidiary, Chex Services, Inc. d/b/a Fastfunds ("Chex"). In the complaint, we allege that Equitex and Chex committed numerous breaches of the terms of the November 3, 2003 Stock Purchase Agreement pursuant to which we were to have acquired Chex from Equitex, including (i) false representations and warranties related to terminated Chex casino contracts and over \$600,000 in bad debts, (ii) material misrepresentations in SEC filings, (iii) entering into a material financing transaction in violation of the covenant not to enter into transactions outside the ordinary course of business, and (iv) failure to proceed in good faith toward closing, including notifying iGames that Equitex could not close on the transaction as structured. These breaches entitled us to terminate the Stock Purchase Agreement and receive a \$1,000,000 termination fee and reimbursement of our transaction costs (estimated at over \$750,000) from Equitex and Chex. Our complaint also states that Chex wrongfully and tortiously declared a default under the \$2,000,000 promissory note that we issued to Chex in connection with our acquisition of Available Money, and that Equitex and Chex tortiously interfered with our relationship with our senior lender. We seek to recover the \$1,000,000 termination fee and transaction costs together with significant damages that resulted from the defendants' breaches and tortuous conduct.

On March 23, 2004, Equitex filed an action in Delaware state court concerning the same Stock Purchase Agreement at issue in the Delaware federal action that we filed, alleging that Equitex was entitled to terminate the Stock Purchase Agreement and receive a \$1,000,000 termination fee and reimbursement of transaction costs. We removed this action to the Delaware federal district court. We are vigorously defending this action and believe that Equitex's and Chex's claims are unfounded. We have filed a counterclaim that restates the claims made in the federal action that we filed. We expect that the two Delaware federal actions will be combined into a single case.

On March 15, 2004, Chex filed a complaint in the District Court of the State of Minnesota for the County of Hennepin against us alleging that we defaulted on interest payments on a \$2,000,000 promissory note evidencing our obligation to repay a loan that Chex extended to us in connection with our acquisition of Available Money (the "Minnesota Complaint"). The Minnesota Complaint seeks payment of the principal balance of the loan and accrued interest thereon. Chex further alleged that we are liable to them for a penalty fee of \$1,000,000 as the result of the alleged termination by Equitex of the November 3, 2003 Stock Purchase Agreement. We subsequently removed the Minnesota Complaint to the United States District Court for the District of Minnesota. On June 23, 2004, the United States District Court for the District of Minnesota transferred this action to the United States District Court for the District of Delaware. We anticipate that this action will be consolidated with the other actions listed above that are pending in to the United States District Court for the District of Delaware. We are vigorously defending this action, which is still in the pleadings stage, and believe that Chex's claims lack merit.

We are involved in litigation with the former owners of Available Money, Inc. We have determined that we may be entitled to a substantial reduction in the purchase price and that the former owners made material

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misrepresentations to us in connection with the Stock Purchase Agreement and our acquisition of Available Money, Inc. In response to our efforts to resolve the matter, on July 15, 2004, the former owners of Available Money, Inc. filed a lawsuit in the United States District Court for the District of Delaware against us and Christopher M. Wolfington, our Chief Executive Officer, alleging that we failed to make required payments of the purchase price set forth in the Stock Purchase Agreement. In addition, the former stockholders of Available Money also filed a Motion for a Standstill Order/Temporary Restraining Order that the court denied without a hearing. We have paid or tendered to the former Available Money stockholders all consideration now due to them under the Stock Purchase Agreement, we believe that this lawsuit is frivolous and was filed for inappropriate purposes. We will vigorously defend against this action and seek sanctions for filing of a frivolous suit. We also anticipate filing counterclaims against Howard Regen, Helene Regen and Samuel K. Freshman seeking substantial reduction in the purchase price and other damages and remedies based on fraud and misrepresentations by them in connection with the transaction.

In addition, we are from time to time, during the normal course of our business operations, subject to various litigation claims and legal disputes. We do not believe that the ultimate disposition of any of these matters will have a material adverse effect on our consolidated financial position, results of operations or liquidity.

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ITEM 2 - CHANGES IN SECURITIES AND USE OF PROCEEDS

Effective as of April 12, 2004, we issued 735,295 shares of our common stock to each of Helene Regen and Samuel K. Freshman as the final payment due pursuant to the Stock Purchase Agreement dated January 6, 2004 that we entered into with Ms. Regen and Mr. Freshman. These shares were issued pursuant to Section 4(2) of the Securities Act.

In May 2004, we granted options to purchase 62,500 shares of our common stock at an exercise price of \$.70 per share to our former chief executive officer pursuant to the terms of his employment agreement. These shares were issued pursuant to Section 4(2) of the Securities Act.

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES

None.

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

None.

ITEM 5 - OTHER EVENTS

None.

ITEM 6 - EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits required by Item 601 of Regulation S-B

- 3.1 Articles of Incorporation of iGames Entertainment, Inc. (incorporated by reference to Exhibit 3.1 of our Registration Statement on Form SB-2 filed on January 18, 2002).
- 3.2 By-laws of iGames Entertainment, Inc. (incorporated by reference to Exhibit 3.2 of our Registration Statement on Form SB-2 filed on January 18, 2002).

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- 3.3 Articles of Amendment to Articles of Incorporation (incorporated by reference to Exhibit 3.3 of Amendment No. 1 to our Registration Statement on Form SB-2 filed on March 8, 2002).
- 4.1 Stock Pledge and Registration Rights Agreement by and between iGames Entertainment, Inc. and Mercantile Capital, L.P. dated as of November 26, 2003.
- 4.2 Form of Specimen Stock Certificate (incorporated by reference to Exhibit 4.2 of our Registration Statement on Form SB-2 filed on January 18, 2002).
- 10.1 Amendment No. 1 to Loan and Security Agreement by and between iGames Entertainment, Inc. and Mercantile Capital, L.P. dated April 30, 2004.
- 10.2 Term Loan Note payable to the order of Mercantile Capital, L.P. in the principal amount of \$2,050,000 dated April 30, 2004.
- 31.1 Certification dated August 16, 2004 pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a) of the Principal Executive Officer and Principal financial Officer as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, by Christopher M. Wolfington, Chief Executive Officer and Chief Financial Officer.

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- 32.1 Certification dated August 16, 2004 pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, made by Christopher M. Wolfington, Chief Executive Officer and Chief Financial Officer.

(b) Reports on Form 8-K

On May 13, 2004, we filed a Current Report on Form 8-K reporting that we had issued a press release announcing that we had agreed with Christopher M. Wolfington, the holder of a majority of the issued and outstanding shares of our Series A Preferred Stock, to extend until September 30, 2004, the deadline for the Series A Preferred Stockholders to exercise their redemption rights.

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SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant has caused this report to be signed on its behalf by the undersigned, thereto duly authorized.

IGAMES ENTERTAINMENT, INC.

Date: August 16, 2004

By: /s/ Christopher M. Wolfington

Christopher M. Wolfington

Chief Executive Officer and
Chief Financial Officer

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(principal financial officer and
principal accounting officer)