SECURITIES AND EXCHANGE COMMISSION

FORM 10QSB

Optional form for quarterly and transition reports of small business issuers under section 13 or 15(d)

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FILER

VENDINGDATA CORP

CIK:**1004673**| IRS No.: **911696010** | State of Incorp.:**NV** | Fiscal Year End: **1231**
Type: **10QSB** | Act: **34** | File No.: **001-32161** | Film No.: **04968114**
SIC: **3990** Miscellaneous manufacturing industries

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended: June 30, 2004

OR

☐ **TRANSITION REPORT PURSUANT SECTION 13 OR 15(d) OF THE EXCHANGE ACT**

For the transition period from: ______________ to ______________

Commission file number: 001-32161

VendingData Corporation

(Exact name of small business issuer as specified in its charter)

Nevada	91-1696010
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

6830 Spencer Street, Las Vegas, Nevada 89119

(Address of principal executive offices)

(702) 733-7195

(Issuer' s telephone number)

(Former name, former address and former fiscal year, if changed since last report)

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 ☒ No ☐

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer' s classes of common equity, as of the latest practicable date: 17,187,799 shares of common stock, $.001 par value, as of June 30, 2004

Transitional Small Business Disclosure Format (check one): Yes ☐ No ☒

VENDINGDATA CORPORATION

FORM 10-QSB

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

VENDINGDATA CORPORATION
Balance Sheets

	June 30, 2004	December 31, 2003
ASSETS	(unaudited)	
Current assets:		
Cash and cash equivalents	$ 2,407,419	$ 11,526,664
Current portion of accounts receivable, trade, net of allowance for uncollectables of $124,561 and $125,530	3,535,365	2,354,054
Due from affiliate	18,407	31,802
Other receivables	67,133	29,836
Inventories	5,569,258	4,150,414
Prepaid expenses	331,882	52,028
	11,929,464	18,144,798
Equipment rented to customers, net of accumulated depreciation of $441,894 and $316,245	523,350	608,555
Property and equipment, net of accumulated depreciation of $2,060,740 and $1,859,206	998,270	1,063,951
Intangible assets, net of accumulated amortization of $360,081 and $288,203	1,208,051	1,282,088
Due from affiliate - non current	118,800	118,800
Accounts receivable, trade, net of current portion, less unamortized discount	1,623,926	1,140,984
Deferred expenses	444,825	250,697
Deposits	1,138,278	1,284,827
Other assets	–	265,478
	$ 17,984,964	$ 24,160,178
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of leases payable	$ 1,962,174	$ 2,237,073
Accounts payable	930,399	1,727,460
Accrued expenses	578,374	824,307
Deferred revenues, current portion	250,360	171,875
Short-term debt	238,250	270,743
Current portion of convertible debt	–	2,368,077
Customer deposits	198,560	178,805
	4,158,117	7,778,340
Deferred revenues, net of current portion	276,045	219,890
Leases payable, net of current portion	1,011,966	1,916,723
	5,446,128	9,914,953
Stockholders' equity:		
Preferred stock, $.001 par value, 10,000,000 shares authorized, no shares issued and outstanding	–	–
Common stock, $.001 par value, 25,000,000 shares authorized, 17,187,799 and 16,765,580 shares issued and outstanding	17,188	16,766
Additional paid-in capital	59,659,307	58,810,806
Deficit	(47,137,659)	(44,582,347)
Total stockholders' equity	12,538,836	14,245,225
Total liabilities and stockholders' equity	$ 17,948,964	$ 24,160,178

See accompanying notes to financial statements.

VENDINGDATA CORPORATION
Statements of Operations

(UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Revenues:				
Sales	$ 1,877,656	$ 1,619,055	$ 2,870,710	$ 3,223,980
Rental	161,110	300,430	372,173	630,743
Other	20,762	12	109,535	132
	2,059,528	1,919,497	3,352,418	3,854,855
Operating expenses:				
Cost of sales	1,068,888	887,082	1,849,625	2,134,286
Selling, general and administrative	1,451,912	1,732,033	2,877,946	3,064,524
Research and development	392,807	228,476	671,560	372,860
	2,913,607	2,847,591	5,399,131	5,571,670
Loss from operations	(854,079)	(928,094)	(2,046,713)	(1,716,815)
Interest expense, unrelated parties	231,479	556,095	494,101	1,053,771
Interest expense, related parties	540	149,572	15,063	309,393
Gain on disposition of assets	–	–	(567)	–
	232,019	705,667	508,597	1,363,164
Net loss	$ (1,086,098)	$ (1,633,761)	$ (2,555,310)	$ (3,079,979)
Basic and diluted loss per share	$ (0.06)	$ (0.21)	$ (0.15)	$ (0.40)
Weighted average shares outstanding	17,187,799	7,646,430	17,146,750	7,636,185

See accompanying notes to financial statements.

VENDINGDATA CORPORATION
STATEMENTS OF CASH FLOWS

(UNAUDITED)

	Six Months Ended June 30,	
	2004	**2003**
Operating activities:		
Net cash used in operating activities	$ (6,180,134)	$ (7,016,487)
Investing activities:		
Acquisition of intangible assets	(4,900)	(8,915)
Acquisition of plant and equipment	(156,381)	(450,525)
Acquisition of equipment produced for rental	–	(9,500)
Disposition of equipment produced for rental	–	502,791
Other	665	705
Deposits	–	(133,518)
Net cash used in investing activities	(160,616)	(98,962)
Financing activities:		
Proceeds from sale of stock	–	362,550
Reimbursement of offering expense	36,731	–
Proceeds from leases payable	–	924,107
Repayment of leases payable	(1,179,656)	(1,362,931)
Proceeds from short-term debt	–	1,000,000
Repayment of short-term debt	(32,493)	(180,000)
Proceeds from convertible debt	–	5,000,000
Repayment of convertible debt	(1,603,077)	–
Net cash provided by (used in) financing activities	(2,778,495)	5,743,726
Change in cash and cash equivalents:		
Decrease in cash	(9,119,245)	(1,371,723)
Cash and cash equivalents at beginning of period	11,526,664	1,778,297
Cash and cash equivalents at end of period	$ 2,407,419	$ 406,574

See accompanying notes to financial statements.

Note 1−Basis of Presentation

The accompanying unaudited financial statements of VendingData Corporation (the “Company”) have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions incorporated in Regulation S-B of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments and accruals) considered necessary for a fair presentation have been included.

The results of operations for the periods presented are not necessarily indicative of the results to be expected for the full year. The accompanying financial statements should be read in conjunction with the Company’ s audited financial statements for the year ended December 31, 2003, as included in the Company’ s Annual Report on Form 10-KSB as filed with the Securities and Exchange Commission from which the accompanying balance sheet information as of that date was derived. Certain reclassifications have been made to amounts presented in prior periods for comparability to the current period presentation.

Note 2−Segments

The revenue segments identified for geographic region-based enterprise-wide data are as follows:

	Three Months Ended June 30,		Six Months Ended June, 30,	
	2004	2003	2004	2003
United States	$ 1,297,863	$ 1,844,497	$ 2,456,361	$ 3,603,963
Asia	11,665	−	146,057	134,392
Europe	750,000	75,000	750,000	75,000
South America	−	−	−	41,500

The Company' s revenues, depreciation and operating income distribution by product are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Revenues				
SecureDrop®	$ 83,242	$ 185,223	$ 278,775	$ 1,334,733
Shuffler	584,672	1,517,008	1,041,947	2,261,824
Deck Checker™	1,370,852	215,649	1,922,161	228,212
Other revenue	20,762	1,617	109,535	30,086
	$ 2,059,528	$ 1,919,497	$ 3,352,418	$ 3,854,855
Depreciation and amortization				
SecureDrop®	$ 0	$ 0	$ 0	$ 0
Shuffler	56,220	129,229	111,782	285,017
Deck Checker™	7,207	0	13,867	0
Selling, general and administrative	145,592	116,253	300,332	219,934
	209,019	245,482	425,981	504,951
Operating income (loss)				
SecureDrop® gross margin	$ 18,813	$ (26,924)	$ 110,377	$ 654,029
Shuffler gross margin	451,877	1,218,455	814,392	1,702,546
Deck Checker™ gross margin	1,071,398	134,506	1,485,404	137,689
Other cost of goods sold	(551,448)	(293,622)	(907,380)	(773,695)
Selling, general and administrative	(1,451,912)	(1,732,033)	(2,877,946)	(3,064,524)
Research and development	(392,807)	(228,476)	(671,560)	(372,860)
	$ (854,079)	$ (928,094)	$ (2,046,713)	$ (1,716,815)

Note 3−Loss per Share (Basic and Diluted)

The basic loss per share is computed by dividing the net loss for the period by the weighted average number of common shares outstanding for the period. Loss per share is unchanged on a diluted basis since the assumed exercise of common stock equivalents would have an anti-dilutive effect due to the existence of operating losses.

Note 4−Debt

The company retired $2,368,077 of convertible debt during the six months ended June 30, 2004 with cash payments and conversions to common stock.

Note 5−Options

The Company currently has two stock option plans. No stock-based employee compensation expense for stock options was reflected in net income for years prior to 2003, as all stock options granted under those plans had an exercise price equal to or greater than the fair market value of the underlying common stock on the date of grant. The exercise price range is between $1.75 and $15.00 with a weighted average exercise price of $3.52. There were 2,008,470 options outstanding as of June 30, 2004.

Note 6−Liquidity Issues

The Company' s ability to maintain adequate liquidity may be dependent upon the success of management' s plans to address and overcome prior operating losses. Management has developed and refined its 2004 operating plan to increase its sales by expanding its product line and improving its sales efforts domestically and internationally. Increased sales in the year ended December 31, 2003 show increased acceptance of the Company' s product line. Management has adopted a program to reduce operating costs through the transfer of manufacturing operations to China and restructuring service functions to reduce labor and rental expense. Management focused on financial condition and liquidity improvements through its capital raising efforts in 2003 along with substantial debt reduction and debt conversion. As a result of anticipated sales improvements and operating cost initiatives, management believes that the Company will begin to generate positive operating cash flow during the second half of 2004. In addition, the Company' s financial advisors have expressed confidence that additional capital can be raised by the Company, if necessary, in 2004, and the Company has received a one-year commitment for a $3.0 million lease line of credit.

Note 7−Trade Receivables From Major Customers

As of and during the six months ended June 30, 2004, approximately 2.1% of trade receivables and 5.4 % of total sales and, as of and during the year ended December 31, 2003, approximately 17.6% of trade receivables and 13.3% of total sales were concentrated in the Nevada gaming industry among five customers under common ownership. The Company' s future operations could be affected by adverse changes in the financial condition of, or the Company' s relationships with, the commonly owned Nevada gaming customers, or economic, competitive and political conditions in our customers' respective local areas or the gaming industry, in general.

The Company manages its concentrations of credit risk by evaluating the creditworthiness of customers before credit is extended and monitoring it thereafter. The maximum losses that the Company would incur if a customer failed to pay amounts owed would be limited to the recorded receivables after any allowances provided.

Note 8−Contingencies

The Company is a party to certain claims, legal actions, and complaints, including a patent infringement action between the Company and one of its main competitors. The Company cannot predict the likely outcome of any such litigation or whether any such substantial litigation would have a material adverse effect on its business as presently conducted or as anticipated.

In early February 2004, the State of Nevada initiated a sales/use tax audit of Central and Madison Leasing, companies through which the Company has obtained lease financing. As of this filing the State of Nevada has not made a determination if there has been a shortfall in the payment of the sales/use tax. The Company has sold and leased back shufflers and Deck Checkers™ over the last five years. The auditor for the State of Nevada is trying to determine at what level a sales/use tax needs to be collected. The Company now collects from our customers in Nevada and remits payments to the State of Nevada. If the State of Nevada determines that the sales of the products to the leasing companies is the level at which sales/use tax should have been collected, liability of the leasing companies would be passed to the Company. The amount of this potential liability could range from a refund of $230,000 to the payment of sales/use tax with interest and penalties of up to $500,000. The Company intends to defend its position in this matter.

ITEM 2. MANAGEMENT' S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS.

Statement on Forward-Looking Information

Certain information included herein contains statements that may be considered forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, such as statements relating to plans for product development, product placement, capital spending and financing sources. Such forward-looking information involves important risks and uncertainties that could significantly affect anticipated results in the future and, accordingly, such results may differ from those expressed in any forward-looking statements made herein. These risks and uncertainties include, but are not limited to, those relating to our liquidity requirements, our ability to locate necessary sources of capital to sustain our operations, the continued growth of the gaming industry, the success of our product development activities, the acceptance of our products in the marketplace, vigorous competition in the gaming industry, our dependence on existing management, changes in gaming laws and regulations (including actions affecting licensing), our leverage and debt service (including sensitivity to fluctuations in interest rates) and domestic or global economic conditions.

OVERVIEW

Our strategy is to develop cost-effective niche products for the global gaming industry. We focus on products that increase the security, productivity and profitability of casino operations. Our strategy involves marketing certain of our products for sale or lease, depending on the product, the geographic location of the customer and other factors. We rely on our internal sales staff and distributor relationships for the sale and rental of our products. Although we anticipate significant sales development and revenue growth, there is no assurance that we will generate sufficient revenue, cash flow or profit to sustain our operations.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The following is a summary of what our management believes are the critical accounting policies related to our operations. The application of these policies, in some cases, requires our management to make subjective judgments regarding the effect of matters that are inherently uncertain.

The preparation of financial statements in conformity with generally accepted accounting principles requires our management to make estimates and assumptions that affect reported amounts and disclosures, some of which may require revision in future periods. Actual results could differ from these estimates. The following is a summary of what our management believes are the critical accounting policies related to our operations. The application of these policies, in some cases, requires our management to make subjective judgments and estimates regarding the effect of matters that are inherently uncertain.

Allowance for Doubtful Accounts.

In connection with the preparation of our financial statements, management reviews and evaluates the collectibility of our trade receivables and adjusts our allowance for estimated uncollectible accounts as deemed necessary in the circumstances. These estimates have the potential for critically affecting the determination of results of operations for any given period. Factors considered by management in making such estimates and adjustments include any concentrations among customers, changes in our relationships therewith, payment history and the apparent financial condition thereof.

Revenue Recognition.

We recognize revenue from the sale of our products upon installation and functional testing at customer locations because that is when the customer' s obligation becomes fixed and certain pursuant to our standard contracts for the sale of units of the SecureDrop® System, shufflers and Deck Checkers™. Sales are recognized immediately when shufflers that are rented are converted to purchases depending on the creditworthiness and payment history of the casino company since payment terms are from 20 to 48 months. The extended warranty and maintenance components that are part of long term sales contracts are unbundled and recognized as deferred revenue amortized over the remaining life of the sales agreement after the initial 90-day warranty as required by the *Emerging Issues Task Force Issue No. 00-21, Revenue Arrangements with Multiple Deliverables*. The useful life of our shufflers and Deck Checkers™ is five years with proper maintenance; the life can be extended with the replacement of component parts. If the customer does not possess the required creditworthiness or an established payment history with us, we would then book the revenue as an installment sale and recognize it over time as payments are received. Revenue from shuffler rentals is recorded at the first of each month in accordance with rental contract terms. All rental contracts are cancelable upon 30-day written notice by the customer. Maintenance expense for rental units is recorded in the period it is incurred. Although sales are not generally made with a right to return, upon occasion, usually associated with the performance warranty, sales returns and allowances are recorded after returned goods are received and inspected. We provide currently for estimated warranty repair costs associated with sales contracts. Although there are no extended warranties offered for our products, we do provide for maintenance contracts that are billed and recognized on a monthly basis.

Intangible Assets.

We have acquired patent rights for various products since 2001 and acquired the patent rights for the Deck Checker™ for $1,004,900 in the third quarter of 2003. We have estimated an economic useful life of 10 years for the Deck Checker™ patents. We currently amortize our intangible assets on a straight-line basis over the estimated useful lives of 10 years.

FINANCIAL CONDITION

Total assets decreased from $24,160,178 to $17,984,964 between December 31, 2003 and June 30, 2004, a decrease of $6,175,214 or 25.6%. The decrease in total assets was due primarily to the $9,119,245 decrease in cash, offset, in part, by an increase in our accounts receivable (trade) and an increase in our inventories. The decrease in cash was due to continuing negative operating cash flows and debt reduction. Accounts receivable (trade) increased by $1,181,311 between December 31, 2003 and June 30, 2004. The primary reasons for the increase in trade receivables were the sale of Deck Checkers™ on terms. Inventories have increased during the current period by $1,418,844 between December 31, 2003 and June 30, 2004. The increase is primarily due to the ramping up of manufacturing in China for Deck Checker™ units, shuffler production and the PokerOne™ Shuffler.

Total liabilities have decreased from $9,914,953 to $5,446,128 between December 31, 2003 and June 30, 2004, a decrease of $4,468,825 or 45.1%. Accounts payable decreased by $797,061 between December 31, 2003 and June 30, 2004 primarily due to the payment of the final $500,000 for the intellectual property rights for the Deck Checker™ and the payment of outstanding payables with funds received from the public offering in December of 2003. From December 31, 2003 to June 30, 2004, we eliminated our convertible debt of $2,368,077 through cash payments and conversions to common stock. Short-term debt decreased by $32,493 between December 31, 2003 and June 30, 2004 due to the repayment of short-term debt.

RESULTS OF OPERATIONS

Comparison of Three Months Ended June 30, 2004 and 2003

Revenue

For the three months ended June 30, 2004, total revenues increased from $1,919,497 to $2,059,528, compared to the three months ended June 30, 2003, an increase of $140,031 or 7.3%. The increase in total revenues was due primarily to increases in our Deck Checker™ revenue and other revenue, offset, in part, by decreases in our SecureDrop® revenue and our shuffler revenue.

Deck Checker™. Revenue related to the sale and rental of our Deck Checker™ product increased substantially compared to the three months ended June 30, 2003. Introduced in the second quarter of 2003, we expect Deck Checker™ revenue will continue to grow as the number of jurisdictions where we can sell the product increases along with the anticipated acceptance rate of the product in the casino industry. Since production has begun at our China facility at a much lower cost per unit, we will be able to establish a more aggressive price point while maintaining margins.

SecureDrop®. Our SecureDrop® revenue decreased by 51.1% during the three months ended June 30, 2004 in comparison to the three months ended June 30, 2003. The decrease was due to the a major installation of SecureDrop® products at three properties operated by Caesars Entertainment Inc. during the three months ended June 30, 2003. Although we are currently in negotiations for new contracts that would impact revenue in the second half of the year, we anticipate that we will continue to experience fluctuations in SecureDrop® revenue through the end of 2004.

Shufflers. Our shuffler sales revenue decreased during the three months ended June 30, 2004 in comparison to the three months ending June 30, 2003. Since the majority of the sales occurring in the second quarter of 2003 were from the conversion of shufflers on rent to purchases through long-term sales agreements that range from 24-48 months, we do not anticipate that conversions will contribute significantly to our shuffler sales in the future. We made a strategic decision to offer our customers the choice to either continue renting or to purchase our shufflers for the same monthly payments. This decision was based on competitive forces in the marketplace and the anticipated introduction of our next generation shufflers in 2004. By offering some of our customers the ability to trade up to our new shuffler, the RandomPlus™ Shuffler, when approved by the relevant regulatory bodies, we will be able to obtain binding purchase commitments for our shufflers and ensure that our products are not readily replaced with those of our competitors.

Our shuffler rental revenue for the three months ended June 30, 2004 decreased compared to the three months ended June 30, 2003 due to the reduced number of shufflers placed on a rental basis. The conversion of rental units to purchases reduced the number of shufflers that were rented throughout this quarter compared to the second quarter of 2003. With the introduction of the new RandomPlus™ shuffler in the fourth quarter 2004, we anticipate an increase in the number of units placed on a rental basis.

Other Revenues. Our other revenues for the three months ended June 30, 2004 increased compared to the three months ended June 30, 2003 due to increases in the sale of supplies for SecureDrop® and the Deck Checker™. The upward trend will continue for these consumables as we increase the installed base of these two product lines.

Cost of Sales

For the three months ended June 30, 2004, our cost of sales increased to $1,068,888, compared to $887,082 for the three months ended June 30, 2003, an increase of $181,806 or 20.5%. The gross margin on revenue for the three months ended June 30, 2004 was 48.1%. This compares to 53.8% for the three months ended June 30, 2003 and to 39.6% for the three months ended March 31, 2004. The decrease in gross margin from the same period of the prior year reflects the costs in transitioning our manufacturing to China. As this transition is completed, we expect to experience improvement in our gross margin percentage.

The gross margin percentage on revenue from Deck Checker™ sales revenue was 77.7% during the three months ended June 30, 2004, compared to 62.4% during the three months ended June 30, 2003. We originally purchased our inventory of Deck Checkers™ from a manufacturer located in New Zealand and, as of June 30, 2004, have sold most of these Deck Checkers™. We are now manufacturing our Deck Checkers™ at our China facility and, after initial transitional costs, anticipate lower costs per unit.

Our cost of SecureDrop® sales revenue decreased by 69.6%. The decrease is directly related to the decrease in SecureDrop® sales during the same period. The gross margin percentage on revenue from SecureDrop® sales revenue was 22.6% in the three months ended June 30, 2004 compared to a gross margin deficit percentage of 14.5% for the three months ended June 30, 2003.

Our cost of shuffler sales revenue for the three months ended June 30, 2004 decreased by 52% compared to the three months ended June 30, 2003. The decrease in the cost of shuffler sales revenue was due to the decreased sale of shuffler units during the three months ended June 30, 2004. The gross margin percentage on revenue from shuffler sales revenue was 83.2% in the three months ended June 30, 2004 compared to 86.1% for the three months ended June 30, 2003. The conversion of existing rental shufflers with low book values due to depreciation to purchases reduced the product cost in the prior year.

Selling, General and Administrative Expense

For the three months ended June 30, 2004, our selling, general and administrative expenses were $1,451,912, a decrease of $280,121, or 16.2%, from $1,732,033 for the three months ended June 30, 2003. The decrease in selling, general and administrative expenses related primarily to decreases in salaries and related expense, consulting and accounting expense, advertising expense, travel and entertainment expense, legal and regulatory expense and supplies expense.

Our general and administrative expenses for the three months ended June 30, 2004 consisted of the following: salaries and related costs of $526,556; consulting and accounting services of $67,053; advertising and marketing costs of $8,119; travel and entertainment costs of $173,172; gaming industry show costs of $68,033; rent of $91,469; repairs and maintenance expense of $20,682; supplies of $10,705; legal and regulatory expenses of $259,860; insurance expenses of $12,685; depreciation and amortization of $136,559; and other expenses of $77,019.

Research and Development Expenses

For the three months ended June 30, 2004, research and development expenses were $392,807, an increase of $164,332, or 71.9%, from $228,476 for the three months ended June 30, 2003. The increase in research and development expenses was due to the development of the RandomPlus™ shuffler and PokerOne™. Although research and development has been a significant cost, we anticipate that these costs will decrease in the future as most of the research and development functions have been or are being moved to our China facility.

Interest Expense

For the three months ended June 30, 2004, we incurred interest expenses of $232,019, compared to $705,667 for the three months ended June 30, 2003, a decrease of $473,648 or 67.1%. This decrease was primarily attributable to the reduced debt service as a result of a decrease in our outstanding indebtedness and the retirement and conversion of $20,331,995 convertible debt in 2003 and early 2004.

Net Loss

For the three months ended June 30, 2004, we had a net loss of $1,086,098 compared to a net loss of $1,633,761 for the three months ended June 30, 2003, a decrease of $547,663, or 33.5%. The decrease in net loss was primarily due to decreases in selling, general and administrative expense and interest expenses. Basic loss per share was $0.06 for the three months ended June 30, 2004, compared to $0.21 for the three months ended June 30, 2003.

Comparison of Six Months Ended June 30, 2004 and 2003

Revenue

For the six months ended June 30, 2004, our revenues were $3,352,418, compared to $3,854,855 for the six months ended June 30, 2003, a decrease of $502,437, or 13.0%. The decrease was due primarily to decreases in SecureDrop™ sales and shuffler sales and rentals incurred in the three months ended March 31, 2004 and the three months ended June 30, 2004, offset, in part by an increase in Deck Checker™ revenue during the same period.

Cost of Sales

For the six months ended June 30, 2004, our cost of sales was $1,849,625, compared to $2,134,286 for the six months ended June 30, 2003, a decrease of $172,539, or 8.1%. The gross margin on revenue for the six months ended June 30, 2004 was $1,502,793 or 44.8%, compared to the gross margin on revenue for the six months ended June 30, 2003 of $1,720,569, or 44.6%. The decrease in gross margin of $217,776 from the six months ended June 30, 2003 to the six months ended June 30, 2004 reflects a decrease in revenues during the period.

Selling, General and Administrative Expenses

For the six months ended June 30, 2004, our selling, general and administrative expenses were $2,877,946, compared to $3,064,524 for the six months ended June 30, 2003, a decrease of $186,578, or 6.1%. The decrease in selling, general and administrative expenses related primarily to decreases in salaries and related expense, consulting and accounting expense, advertising expense, travel and entertainment expense, legal and regulatory expense and supplies expense.

Our selling, general and administrative expenses for the six months ended June 30, 2004 consisted of the following: salaries and related costs of $1,098,170; consulting services of $158,371; advertising and marketing costs of $14,028; travel and entertainment costs of $277,646; gaming industry trade show costs of $109,131; rent of $179,281; repairs and maintenance expenses of $43,105; legal and regulatory expenses of $457,755; supplies of $30,399; insurance expenses of $40,324; depreciation and amortization of $290,120; and other expenses of $179,616.

Research and Development Expense

For the six months ended June 30, 2004, our research and development expenses were $671,560, compared to $372,860 for the six months ended June 30, 2003, an increase of $298,700, or 80.1%. The increase was due to the our continued development efforts on the RandomPlus™ and PokerOne™ shufflers.

Interest Expense

For the six months ended June 30, 2004, we incurred interest expense of $509,164, compared to $1,363,164 for the six months ended June 30, 2003, a decrease of $854,000, or 62.6%. This decrease was primarily attributable to the reduced debt service resulting from the substantial decrease in our outstanding indebtedness and the retirement and conversion into shares of common stock of $20,331,995 convertible debt in 2003 and in the three months ended March 31, 2004.

Net Loss

For the six months ended June 30, 2004, we had a net loss of $2,555,310, compared to a net loss of $3,079,979 for the six months ended June 30, 2003, a decrease of $524,669, or 17.0%. The decrease in net loss was primarily due to the decrease in interest expense, offset, in part, by the increase in loss from operations. Basic loss per share was $0.15 for the six months ended June 30, 2004, compared to $0.40 for the six months ended June 30, 2003.

LIQUIDITY AND CAPITAL RESOURCES

Because of our efforts to transition from a development stage company to an operating company, we have generated substantial cash flow deficits from operations, including cash used in operating activities of $6,180,134 and $7,016,487 in the six months ended June 30, 2004 and 2003, respectively. In addition, to fund our development and operating activities, we generated cash through financing activities in 2003 of $23,047,432. We have used cash of $2,778,495 in financing activities during the six months ending June 30, 2004 for the repayment of leases payable, short-term debt, and convertible debt.

Consequently, we have been substantially dependent on cash from financing activities to fund our development and operating activities. We will continue to require cash from financing activities for our current operating needs until our operations generate sufficient cash flow to provide for such cash requirements. As a result of anticipated sales improvements and operating cost initiatives, management believes that the Company will begin to generate positive operating cash flow during the second half of 2004. In terms of sources of additional capital, we have received a one-year commitment for a $3.0 million lease line of credit and have been advised by our financial advisors that additional capital can be raised, if necessary, in 2004.

Sources of Capital

In the event our cash on hand plus cash from operations should be insufficient during future periods, we anticipate relying upon private and institutional sources of debt and equity, and we may seek public, private and institutional sources of capital for working capital purposes. During the years ended December 31, 2003 and 2002, our sources of capital included a public stock offering, equipment financing from a third party, short-term notes from stockholders, convertible debentures and other private sources of capital.

With respect to our equipment financing where we have sold and leased back most of our furniture, equipment, tooling and shufflers held for rent, we have repaid $1,179,656 for the six months ended June 30, 2004, received proceeds of $2,988,385 and repaid $2,823,331 for the year ended December 31, 2002 and have received proceeds of $989,820 and repaid $2,754,607 for the year ended December 31, 2003. As of June 30, 2004, we had outstanding equipment financing of $2,974,140. These equipment leases have terms of 36 to 39 months and were not recorded as sales because each of the leases included a mandatory buy-back provision.

With respect to our short-term debt, we have received proceeds of $2,264,871 and repaid $650,000 for the year ended December 31, 2002 and have received proceeds of $7,400,000 and repaid $1,310,000 for the year ended December 31, 2003 and have repaid $32,493 for the six months ended June 30, 2004. As of June 30, 2004, we had outstanding short-term loans in the aggregate amount of $238,250. Prior to 2003, we were substantially dependent on short-term loans from our principal stockholder and other directors. Despite such reliance, neither our principal stockholder nor our directors are obligated to provide additional financing to us, and our principal stockholder and directors are free to decline to fund additional financings to us at any time. In such event and in the absence of third party financing sources, we may have substantial difficulties in raising additional financings.

With respect to our convertible debentures, we received proceeds of $4,903,076 and $11,050,000 during the years ended December 31, 2002 and 2003, respectively, and have completely retired the convertible debentures during the three months ended March 31, 2004.

With respect to the public offering of common stock in December 2003, we sold 5,500,000 shares at $5.00 per share for gross proceeds of $27,500,000. The net proceeds after all offering and commission expenses were $24,800,000.

Outlook

Our ability to maintain adequate liquidity is substantially dependent upon the success of management’ s plans to address and overcome prior operating losses. Management has developed and refined its 2004 operating plan to increase its sales by expanding its product line and improving its sales efforts domestically and internationally. Increased sales in the year ended December 31, 2003 show increased acceptance of our product line. Management has adopted efforts to reduce operating costs through the transfer of manufacturing operations to China and restructuring service functions to reduce labor and rental expense. Management has focused on financial condition and liquidity improvements through its capital raising efforts in 2003 along with substantial debt reduction and debt conversion, resulting in positive cash position and substantially reduced indebtedness at June 30, 2004. As a result of anticipated sales improvements and operating cost initiatives, management believes that we will begin to generate positive operating cash flow by the end of 2004. In addition, our financial advisors have expressed confidence that additional capital can be raised by us, if necessary, in 2004 and we have received a one-year commitment for a $3.0 million lease line of credit.

Based on presently known commitments and plans, we believe that we will be able to fund our operations and required expenditures through the fourth quarter of 2004 through cash on hand, cash flow from operations, and cash from private placements of debt or equity or from lease financing sources. In the event that such sources are insufficient or unavailable, we will need to seek cash from public or private placements of debt or equity, institutional or other lending sources, sell certain assets or change operating plans to accommodate such liquidity issues. No assurances can be given that we will successfully obtain liquidity sources necessary to fund our operations in the upcoming year. If we continue to generate significant losses from our operations and we are not able to located additional sources of liquidity, we may be unable to continue as a going concern.

RISK FACTORS

RISKS RELATED TO VENDINGDATA

Given our recurring losses and accumulated deficits, we must manage our liquidity.

Our financial statements report recurring losses and accumulated deficits. Based on presently known commitments and plans, we believe that we will be able to fund our operations and required expenditures through the fourth quarter of 2004 from cash on hand, cash flow from operations and cash from debt or equity financings or from lease financing sources. The completion of the offering of 5,500,000 shares of common stock in December 2003 allowed us to pay off all bridge financing, to convert approximately $5,730,000 of our convertible debt and accrued interest, to repay our convertible debt, to retire $7,500,000 of our convertible 10% senior notes and still have adequate funds available with which to fund additional product inventory, and use for general corporate purposes. If we are unable to generate a sufficient amount of sales of our products to fund our operations, we will need to seek cash from private or public placements of debt or equity, institutional or other lending sources, to sell certain assets or to change operating plans to accommodate our liquidity issues. We may not be able to obtain other liquidity sources as may be necessary to fund our operations in the future.

We have a history of significant operating losses and anticipate continued operating losses, and we may be unable to achieve profitability.

We have a history of significant operating losses and anticipate continued operating losses for the foreseeable future. For the six months ended June 30, 2004 and years ended December 31, 2003 and 2002, we have incurred net losses of $2,555,310, $7,812,089 and $6,192,786, respectively, and our operations have used $6,180,134, $11,731,150 and $5,206,489 of cash, respectively. As of June 30, 2004, December 31, 2003 and 2002, we had accumulated deficits of $47,137,659, $44,582,347 and $36,770,258, respectively. If we are unable to generate a positive cash flow in 2004, we will be required to locate additional sources of capital. If our revenues do not increase very substantially, or if our spending levels exceed our expectations, we will not become profitable. Revenues may not grow in the future, and we may not generate sufficient revenues for profitability. If we become profitable, we may not be able to sustain profitable operations.

Even if our operations do not become profitable, we will continue to be obligated to pay our management substantial salaries and benefits.

We currently compensate our executive officers and significant employees with substantial salaries and other benefits and, in the future, may pay increased salaries and benefits. In 2003, we paid an aggregate amount equal to approximately $1,300,000 to our executive officers and significant employees. In June and July 2003, we extended our employment agreements for an additional five years with Mr. Blad and an additional three years with seven other key employees. In February 2004, we expanded our management team with the hiring of H. Michael Jahnke as our Chief Operating Officer. We intend to continue to pay substantial salaries and benefits to Mr. Blad and our other key employees. The payment of such compensation and benefits may be a burden on us and may be a factor in limiting or preventing our profitability. Upon the expiration of those employment agreements, we may elect to continue compensating management with similar or higher salaries and other benefits.

The demand for our products may be insufficient to generate enough revenues to sustain our operations.

If we fail to generate sufficient demand for our products, we may be unable to sustain operations or generate a return to investors. Until January 2000, we were in the development stage and derived minimal revenues from our products. Currently we are an operating company that continues to develop new products. Since January 2000, our activities have been limited to analyzing and consulting with persons in the gaming industry, developing and manufacturing new products, establishing distribution networks for our products, marketing our products to the gaming industry, and commencing product sales. During such time, we have derived only limited revenues, which have been insufficient to sustain our operations. We may not generate sufficient revenue to sustain our operations. No independent organization has conducted market research providing management with independent assurance from which to estimate potential demand for our products. The overall market may not be receptive to our products, and we may not successfully compete in the target market for our products.

Due to the limited placement of our SecureDrop® System and the Deck Checker ™, we may not achieve significant market acceptance of these products and, as a result, general sufficient revenue to sustain our operations.

Although we installed our SecureDrop® System and have placed units of the Deck Checker™ at a limited number of properties, we not be able to achieve significant market acceptance of our SecureDrop® System or the Deck Checker™. We have only sold our SecureDrop® Hard Count Module to a small number of casinos. The SecureDrop® System Soft Count Module has been slow to sell outside Nevada. Due to the resistance of gaming companies to the implementation of unproven technologies and product flaws that we subsequently corrected, we have experienced longer than expected sales cycles for our SecureDrop® System. In addition, we have only placed 156 Deck Checker™ units (including 20 rentals) as of June 30, 2004. The commercial success of our SecureDrop® System and Deck Checker™ will depend upon the degree of market acceptance of these products in the gaming community and will depend on a number of factors, including:

- demonstration of effectiveness and reliability;
- the prevalence and severity of any quality problems or defects in the early stage of introduction that were not anticipated in the design of those products;
- effectiveness of our marketing and distribution capabilities;
- ability to promptly service and repair the products; and
- receipt of approval by respective gaming jurisdictions.

If we fail to expand our sales and leases for our SecureDrop® System and our Deck Checker™, we may be unable to generate sufficient revenues to continue to operate our business.

Our revenues and receivables are concentrated among a few major customers, which means that our financial condition could deteriorate if any meaningful reduction in the level of sales to any of these customers occurs.

We are substantially dependent upon sales to a few major customers. In the first two quarters 2004 and in the fiscal year 2003, Caesars Entertainment, Inc. (formerly Park Place Entertainment Corporation), our largest customer, accounted for more than 5% of our revenues. During the six months ending June 30, 2004, approximately 2.1% of trade receivables and 5.4% of total sales and during the year ended December 31, 2003, approximately 17.6% of trade receivables and 13.3% of total sales were concentrated in the Nevada gaming industry among five customers under the common ownership of Caesars Entertainment, Inc. Any adverse changes in the financial condition of our major customers, any loss of our major customers, or any meaningful reduction in the level of sales to any of these customers could have a materially adverse impact on us.

The acceptance and expansion of coinless gaming may adversely affect the demand for our SecureDrop® Hard Count Module.

Certain gaming operators have tested and employed as part of their current operations certain gaming devices that have totally eliminated the use of coins or tokens, or use a combination of coins and "cashless" vouchers. The acceptance and expansion of totally coinless gaming devices may reduce the demand for the SecureDrop® Hard Count Module, which is based on coin usage, and may adversely affect our operations in the future. For example, International Game Technology has introduced the EZ-Pay™ system, which attempts to reduce operating costs and machine downtime by providing gaming operators with machines that drop coins for smaller payouts and print tickets for larger, predetermined payouts. As a result of the issuance of tickets, players are not required to wait for attendants in order to be paid larger payouts and may use their tickets at other machines equipped with the EZ-Pay™ system or similar systems. Due to positive customer response, the number of slot operations with online systems that use coinless gaming systems continues to grow. However, while SecureDrop® Hard Count Module sales may be adversely impacted, we believe demand for our SecureDrop® Soft Count Module has been enhanced.

We place our leased shufflers in casinos under short-term lease arrangements, which makes these products susceptible to replacement due to pressure from competitors, changes in economic conditions, obsolescence and declining popularity.

All of our leased shufflers are placed with customers under short-term lease arrangements, which, unlike long-term leases or permanent sales of our products, can easily be terminated by a dissatisfied customer. The manner in which such short-term leases are structured puts our shufflers at greater risk of replacement due to pressure from competitors, changes in economic conditions, obsolescence and declining popularity. Casino operators may terminate the use of our products, and we may not be able to maintain and expand the number of installed shufflers through enhancement of existing shufflers, introduction of new shufflers, customer service or otherwise. Our ability to compete may be damaged, and our revenues may be reduced if we are unable to protect our intellectual property rights adequately.

Our success depends upon maintaining the confidentiality and proprietary nature of our intellectual property rights. Our ability to compete may be damaged, and our revenues may be reduced if we are unable to protect our intellectual property rights adequately. To protect these rights, we rely principally on a combination of:

contractual arrangements providing for non-disclosure and prohibitions on use;

patents and pending patent applications;

trade secret, copyright and trademark laws; and

certain built-in technical product features.

Patent, trade secret, copyright and trademark laws provide limited protection. The protections provided by laws governing intellectual property rights do not prevent our competitors from developing, independently, products similar or superior to our products and technologies. In addition, effective protection of copyrights, trade secrets, trademarks, and other proprietary rights may be unavailable or limited in certain foreign countries. We may be unaware of certain non-publicly available patent applications, which, if issued as patents, could relate to our services and products as currently designed or as we may modify them in the future. Legal or regulatory proceedings to enforce our patents, trademarks or copyrights could be costly, time consuming, and could divert the attention of management and technical personnel.

Adverse results in current litigation could result in substantial monetary damages and adversely impact the manufacture and sale of certain of our shuffler products.

Shuffle Master, Inc., our principal competitor in the shuffler market, has sued us for patent infringement and alleges that our shufflers violate two of its patents concerning registering use of a playing card shuffler apparatus and the displaying of the use on a display. Shuffle Master seeks treble damages, which, if awarded, could result in us owing it substantial sums of money, and, if large enough, could have a material adverse effect on our liquidity and our ability to conduct operations. Although we believe our position to be meritorious, litigation of this nature is a drain on our cash resources and our management' s time. Inasmuch as Shuffle Master has asserted patent infringement claims and we have reasonable defenses to the same, we cannot determine whether we will prevail in this litigation, nor whether damages, if awarded, would significantly impact our ability to continue to manufacture and sell particular products within the United States and its territories. If we do not prevail, we will be unable to sell our shuffler products unless we change certain components used in the shufflers or obtain a license from Shuffle Master to use the playing card shuffler apparatus and the display. Similarly, we cannot determine whether Shuffle Master will assert other litigation claims based upon other patents it may currently or in the future own, nor can we determine the likely outcome of any such litigation or whether any such substantial litigation would have a material adverse effect on our business as presently conducted or as anticipated.

We believe that it is likely that our PokerOne™ Shuffler will be the subject of future patent litigation if the product is sold and installed in the United States and, if commenced, could subject us to continuing litigation costs and risks.

Other than the allegations made by Shuffle Master, Inc. discussed above, we are not aware of any claims or basis for our current products infringing on the proprietary rights of third parties. To the extent that we introduce new products that incorporate the same or similar technology, it is likely that Shuffle Master, Inc. will bring one or more claims against us seeking damages, injunctive or other equitable relief, or both. Moreover, we believe that it is reasonably likely that if we introduce the PokerOne™ Shuffler in the United States, Shuffle Master will bring one or more claims against us seeking various remedies at equity or law. We cannot predict the outcome of any future litigation that may occur.

If our future products incorporate technology that infringes the proprietary rights of third parties and we do not secure licenses from them, we could be liable for substantial damages that would cause a material reduction in revenues and impair our prospects for achieving growth and profitability.

In furtherance of the development of our services or products, we may need to acquire licenses for intellectual property to avoid infringement of third party rights or claims of infringement. These licenses may not be available on commercially reasonable terms, if at all. Claims for infringement, if made, could damage our business prospects, our results of operations and financial condition, whether or not the claims have merit, by:

consuming substantial time and financial resources required to defend against them;

diverting the attention of management from growing our business and managing operations;

resulting in costly litigation; and

disrupting product sales and shipments.

If any third party prevails in an action against us for infringement of its proprietary rights, we could be required to pay damages and either enter into costly licensing arrangements or redesign our products so as to exclude the infringing technology. As a result, we would incur substantial costs and delays in product development, sales and shipments, our revenues may decline substantially and we may not be able to achieve the growth required for us to achieve profitability.

Our failure to compete successfully against innovative competitors or new entrants could adversely impact our ability to sell our products and generate revenues.

Our market is characterized by changing technology, periodic product obsolescence and continuous protection of proprietary technology. Our success will depend upon our ability to sell our current products, and to develop successor systems. We will need to introduce new products and features in a timely manner to meet evolving customer requirements. We may not succeed in these efforts. Even if we succeed, products or technologies developed by others may render our products or technologies noncompetitive or obsolete, which would impair our ability to sell our products and reduce our revenue.

Our inability to complete the development of our specialty game shuffler could adversely impact potential revenue growth.

We may not be able to complete development of the PokerOne™ Shuffler. We are continuing to fine tune this product, and we plan to start the testing phase in Asia by the end of the second quarter of 2004. We have expended significant time and resources into the development of this product, and our failure to bring about a viable product may limit our long-term revenue growth in our shuffler product line.

Scrutiny and attempts by third parties to compromise our products' security, if successful, could injure product demand and force us to take back impacted products.

In the event that our products become susceptible to attacks by third parties that result in a decrease or compromise of the security of our customers' operations, we will most likely be required to take back our products from existing customers and will lose sales and rentals from prospective customers. Although we have tested our products for security and our products have been tested by certain gaming regulators as part of the approval process, our products may be susceptible to schemes by third parties to defraud the properties where our products are used. Vulnerabilities in the security of our products will almost certainly reduce demand for these products. Our shufflers may become vulnerable to card counters or expert players, and the use of our shufflers may result in financial losses for our customers. The occurrence of any of these events would likely have a material adverse effect on our sales revenues.

Any conditions that adversely affect the gaming industry could also have a material adverse effect on demand for our products.

The success of our business depends solely on the gaming industry where revenues are sensitive to general economic conditions and generally rise or fall rapidly in relation to the condition of the overall economy. Although we cannot accurately estimate the economic impact of past or future terrorist attacks or current international conflicts at this time, the gaming industry has been negatively affected by the reduction in air travel and tourism, and we expect that any significant decline in the economic health or growth of the gaming industry will reduce demand for our products.

We are unable to predict the future impact that extraordinary events, such as terrorism, the uncertainty of war and worldwide health concerns, may have on our business and operations.

Extraordinary events, such as terrorist attacks, acts of war or worldwide health concerns, may cause damage or disruption to our operations, which, in turn, could significantly impact our revenues, costs and expenses, and financial condition. The terrorist attacks that took place in the United States on September 11, 2001 were unprecedented events that have created many economic and political uncertainties, especially to the gaming industry, some of which have materially adversely affected our business, results of operations, and financial condition and may do so again in the future. In particular, the gaming industry has been affected by the downturn in the tourist industry as a result of the September 11, 2001 attacks. Because our business is directly tied to the gaming industry, the long-term effects from the September 11, 2001 attacks are unknown. The potential for future terrorist attacks, the national and international responses to terrorist attacks, other acts of war or hostility and concerns about the spread of certain diseases, including severe acute respiratory syndrome, or SARS, have created many economic and political uncertainties, which could materially adversely affect our business, results of operations and financial condition in ways that we currently cannot predict.

Supply interruption from our manufacturing facility in China could cause us to fail to supply customer orders on a timely basis.

We have centralized most phases of the manufacturing process for our products at our own facility in Xiaolan Town in Zhongshan City, China. We will be adversely impacted if there is an interruption in our ability to receive components or inventory from, or a material increase in labor costs in, China. Factors that may cause a supply interruption include political unrest, closure of ports, worldwide health concerns, including SARS, and other events beyond our control. In the event that our manufacturing operations in Xiaolan Town are interrupted, our ability to fill orders, ship such orders and realize the revenues therefrom could be adversely affected.

Our efforts to expand into international markets pose special risks that could adversely affect all of our business.

As a result of the opening of our manufacturing facility in China, we are currently operating in international markets, and we propose to further expand our international sales and operations. Engaging in business outside the United States will subject us to the customary risks of doing business in foreign countries. These risks include fluctuations in foreign currency exchange rates and controls, competitive disadvantages to established foreign businesses with significant current market share and business/customer relationships, nationalization and other economic, tax and regulatory policies of local governments and the possibility of trade embargoes, political instability or war or other hostility, as well as the laws and policies of the United Sates affecting foreign trade and investment. Any one or more of these factors could materially adversely affect our ability to conduct business outside the United States and therefore our business as whole.

Our reliance on distributors in international markets and our limited sales experience in foreign countries could cause us to lose sales and collections on such sales.

In general, substantially all sales of our products outside the United States are achieved through distributor relationships. We believe the distributors that we have engaged are experienced and reputable, however, if we are unable to manage these relationships, our ability to generate revenue and profits in the non-U.S. market may be adversely affected. To the extent that we engage in direct sales outside the United States, we have limited sales experience and history in foreign markets.

Due to our management's controlling interest in our common stock, our management has the power to control all matters submitted to our stockholders, which renders non-management stockholders' efforts to effect substantial changes in our company more difficult.

Our executive officers and members of our board beneficially own approximately 9,060,278 shares of common stock, or approximately 50.3% of the outstanding shares of our common stock, assuming exercise or conversion of all options, warrants and convertible debentures held by our executive officers and members of our board that are exercisable within 60 days of June 30, 2004. Accordingly, these stockholders have the power to control all matters requiring approval by our stockholders, including the election of directors and approval of mergers and other significant corporate transactions. This concentration of ownership also has the effect of delaying, preventing or expediting, as the case may be, a change in control of our company.

The loss of our executive officers, significant employees or certain members of our management could adversely impact our operations.

Our success is substantially dependent upon the efforts and skills of Steven J. Blad, our chief executive officer and president, and H. Michael Jahnke, our chief operating officer. We have entered into employment agreements with Messrs. Blad and Jahnke and nine other significant employees. However, if we were to lose the services rendered by any of our executive officers or significant employees, key management, product development and sales functions could be adversely affected. In addition, we compete with other potential employers for employees, and we may not succeed in hiring and retaining the executives and other employees that we need. An inability to hire and retain quality employees could have a material adverse effect on our business, financial condition and results of operations.

RISKS RELATED TO OUR INDUSTRY

We face intense competition from companies with longer operating histories, greater resources and more established brand names that could use such advantages to lower our market share and reduce our revenues.

There is significant competition in the shuffler market, where we compete with established companies and other entities, most of which possess substantially greater resources than we do. Almost all of the companies with which we compete in the shuffler market are substantially larger, have more substantial histories, backgrounds, experience and records of successful operations, greater financial, technical, marketing and other resources, more employees and more extensive facilities than we now have, or will have in the foreseeable future. It is also likely that other competitors will emerge in the near future. Other companies may develop products competitive to our SecureDrop® System. We may not be able to compete successfully with other established gaming product manufacturers. Our inability to compete successfully will likely result in loss of market share and lower revenues, or increases in operating costs, such as marketing costs.

We face extensive regulation from gaming and other government authorities.

The gaming industry is a highly regulated industry and is subject to numerous statutes, rules and regulations administered by the gaming commissions or similar regulatory authorities of each jurisdiction. Generally, companies that seek to introduce gaming products or concepts into such jurisdictions may be required to submit applications relating to their activities or products (including detailed background information concerning controlling persons within their organization), which are then reviewed for approval. In this regard, we may incur significant expenses in seeking to obtain licenses for our gaming products and concepts, and our products may not be approved in all jurisdictions. The failure to obtain such approval in any jurisdiction in which we may seek to introduce our products or concepts could have a material adverse effect on our business. In addition, any change to the applicable statutes, rules and regulations that restricts or prevents our ability to operate could have an adverse effect on us.

Any person who is the beneficial owner of our common stock or with whom we have a material relationship that fails or refuses to apply for a finding of suitability, or that is found unsuitable for licensing, would be required to dispose of all of our stock.

Certain gaming regulatory agencies to which we are subject may investigate any beneficial holder of our voting securities (regardless of the numbers of shares owned), and any individual who has a material relationship or involvement with us, in order to determine whether such individual is suitable or should be licensed as a business associate of ours. In addition, the gaming authorities of various jurisdictions may require our officers, directors and certain key employees to be licensed or found suitable by these gaming authorities, which would require these officers, directors and key employees to submit detailed background information. Any person who fails or refuses to apply for a finding of suitability or a license after being ordered to do so by gaming regulatory agencies may be found unsuitable, and we could be subject to adverse regulatory action. In the event that the gaming authorities were to find an officer, director, key employee, stockholder, or any other individual that has a material relationship with us, unsuitable for licensing or unsuitable to continue having a relationship with us, we would have to sever all relationships with that individual, and that individual would be required to dispose of all of our stock. This could result in the loss of key persons critical to our success or in significant selling pressure on our stock if such persons are required to dispose of shares of our common stock in an amount that exceeds typical trading volumes in our shares.

Our focus on products for the gaming industry subjects us to greater risk than we would have if we marketed our products to multiple industries.

We design and manufacture products and concepts solely for the gaming industry and depend almost exclusively on our ability to generate revenues from the rental or sale of our products to customers in the gaming industry. The economic health of the gaming industry, and, therefore, our revenues, are affected by a number of factors beyond our control, including:

- general economic conditions, such as recession, inflation, business cycle fluctuations and interest rates;
- levels of disposable income of gaming property patrons;
- acts of terrorism and anti-terrorism efforts;
- increased transportation costs resulting in decreased travel by gaming patrons;
- changes or proposed changes in tax laws;
- legal and regulatory issues affecting the development, operation and licensing of our gaming customers; and
- competitive conditions in the gaming industry.

These factors may adversely impact the demand for our products and materially affect the revenues that we realize on the sale or placement of our products.

RISKS RELATED TO OUR COMMON STOCK

There has only recently been a public market for our common stock, so our stockholders may be unable to dispose of their investment, or may lose the total value of their investment.

There had been no trading market for our common stock until September 10, 2003, when our common stock became eligible for quotation on the OTC Bulletin Board. Due to the limited trading history of our common stock, an active trading and/or a liquid market may not be maintained. Moreover, in the event that we are unable to continue as a going concern and we are dissolved or otherwise terminated, you could lose your entire investment in our common stock. Investment in our common stock is at risk of complete loss if our operations are unsuccessful.

Historically, our common stock has been deemed to be "penny stock" as that term is defined in Rule 3a51-1 promulgated under the Securities Exchange Act of 1934, or the Exchange Act. Penny stock may be more difficult for investors to resell. Penny stocks are stocks:

with a price of less than $5.00 per share;

that are not traded on a "recognized" national exchange (exchange-listed securities must still have a price of not less than $5.00 per share);

whose prices are not quoted on the Nasdaq automated quotation system (Nasdaq-listed stock must still have a price of not less than $5.00 per share); or

from issuers with net tangible assets less than $2.0 million (if the issuer has been in continuous operation for at least three years) or $5.0 million (if in continuous operation for less than three years), or with average revenues of less than $6.0 million for the last three years.

Although our AMEX listing application has been approved and our common stock began trading on the AMEX on May 4, 2004, since the closing price for our common stock was less than $5.00 per share as of June 30, 2004, our common stock is deemed to be penny stock for purposes of Section 15(b)(6) of the Exchange Act. Federal rules and regulations generally impose additional sale practice and disclosure requirements and penalties on broker/dealers and persons associated with or seeking to become associated with such broker/dealers who sell or recommend penny stocks to certain investors. These requirements may reduce the potential market for our common stock by reducing the number of potential investors, and any or all of these factors may make it more difficult for investors in our common stock to sell shares to third parties or to otherwise dispose of them and could cause our stock price to decline. Moreover, broker/dealers are required to determine whether an investment in a penny stock is a suitable investment for a prospective investor and receive the investor' s written consent to the transaction.

Investors seeking guaranteed dividend-paying investments should not invest in our common stock.

Our operations may not become profitable. If we become profitable, we intend to use any earnings that may be generated to finance the growth of our business. Any payment of future dividends will be at the discretion of our board of directors and will depend on, among other things, our earnings, financial condition, capital requirements, level of indebtedness, statutory and contractual restrictions applying to the payment of dividends, and other considerations that our board of directors deems relevant. Accordingly, stockholders may have to sell some or all of their common stock in order to generate cash flow from their investment. Stockholders may not realize a gain on their investment, and they may lose all or a significant amount of their investment when they sell their common stock.

If we are unable to generate sufficient revenue to provide the cash required to fund our operations in the future, we may be required to issue additional equity or convertible debt securities to provide our operations with additional working capital, which, in turn, will have the effect of diluting the relative ownership of our existing stockholders.

We have supplemented the cash deficit arising from our operations with the proceeds of our December 2003 offering of 5,500,000 shares of common stock and have received a one-year commitment for a $3 million lease line of credit, and will, if necessary, continue to supplement with cash from private or public placements of debt or equity, institutional or other lending sources. We have also utilized convertible debt securities and warrants to raise capital in the past. The issuance of additional equity or convertible debt securities will have the effect of reducing the percentage ownership of our current stockholders. In addition, these equity or convertible debt securities may have additional rights, preferences or privileges to those of our common stock, such as registration rights and preferences in liquidation. In the event we are required to raise additional funds to support our operations, additional funds may not be available on terms favorable to our company, or at all. If adequate funds are not available or are not available on acceptable terms, we may not be able to fund our operations or otherwise continue as a going concern.

Shares eligible for sale in the near future may cause the market price for our common stock to decline.

In addition to the number of shares registered on behalf of the Selling Stockholders, we have approximately 7,595,200 shares of common stock that are either freely tradable pursuant to Rule 144(k) of the Securities Act of 1933, or the Securities Act, or have previously been registered by us through a registration statement filed with the SEC. As such, the future sale of a substantial number of shares of our common stock in market transactions, or the perception that these sales could occur, may depress the market price for our common stock. These sales could also impair our ability to raise additional capital through the sale of our equity securities in the future.

Our board of directors may issue blank check preferred stock, which may affect the voting rights of our holders and could deter or delay an attempt to obtain control of us.

Our board of directors is authorized, without stockholder approval, to issue preferred stock in series and to fix and state the voting rights and powers, designation, preferences and relative, participating, optional or other special rights of the shares of each such series and the qualifications, limitations and restrictions thereof. Preferred stock may rank prior to our common stock with respect to dividends rights, liquidation preferences, or both, and may have full or limited voting rights. Accordingly, issuance of shares of preferred stock could adversely affect the voting power of holders of our common stock and could have the effect of deterring or delaying an attempt to obtain control of us.

ITEM 3. CONTROLS AND PROCEDURES

(a) *Evaluation of Disclosure Controls.* We evaluated the effectiveness of our disclosure controls and procedures as of the end of the three months ended June 30, 2004. This evaluation was done with the participation of our chief executive officer and our acting chief financial officer. Disclosure controls and procedures are 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, as appropriate to allow timely decisions regarding required disclosure.

Our management does not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, but not absolute, assurance that the objectives of a control system are met. Further, any control system reflects limitations on resources, and the benefits of a control system must be considered relative to its 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, 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 a control. The design of a control system is also based upon certain assumptions about the likelihood of future events, there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and may not be detected.

Based on this evaluation, we concluded that, subject to the limitations noted above, our disclosure controls and procedures are effective to ensure that information we are required to disclose in 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.

(b) *Changes in Disclosure Controls and Procedures.* Although there have been no significant changes in internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation, we are continuously evaluating means of enhancing our internal controls. During the twelve months ended December 31, 2003, we added qualified staff to our accounting department, we improved our approval process for accounting entries, and we commenced implementation of MAS-500 integrated financial and manufacturing software application. MAS-500 has been implemented in Las Vegas to provide an integrated control process for purchasing, inventory control and manufacturing and should improve the accuracy and timeliness of our financial reporting. With respect to our China facility, we completed the implementation of and training on MAS-500 during the second quarter of 2004.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On March 27, 2002, Shuffle Master, Inc., or Shuffle Master, filed a complaint (Case No. CV-S-02-0438-JCM-PAL) against VendingData in the United States District Court, District of Nevada. The amended complaint alleges, among other things, claims for patent infringement and requests treble damages, an injunction enjoining us from infringing on two of Shuffle Master's patents, an accounting of our gains and profits that resulted from our alleged infringement, and for interest, costs and attorneys' fees. The Shuffle Master patents that are at issue in the litigation concern registering use of a playing card shuffler apparatus and the displaying of the use on a display. We have filed our answer, counterclaims, and amended counterclaims against Shuffle Master. In our answer, we deny Shuffle Master's allegation of patent infringement and request that Shuffle Master's complaint be dismissed. We also seek, in our amended counterclaim, a declaration that we do not infringe Shuffle Master's patents and that Shuffle Master's patents and certain of its related claims are invalid. We further assert counterclaims against Shuffle Master for breach of contract and violation of the Uniform Trade Secrets Act. On May 20, 2002, the United States District Court, District of Nevada denied Shuffle Master's motion for preliminary injunction against us. Discovery in this litigation is now closed. On May 28, 2003, we filed a motion for summary judgment requesting that the court dismiss the case against us. The hearing for our motion for summary judgment was taken off calendar pending a ruling by a magistrate judge with respect to a October 24, 2003 claim construction hearing to determine the scope and definition of the patent claims at issue. On March 31, 2004, the magistrate judge issued an order with regard to claim interpretation, to which we have filed written objections. On June 25, 2004, the District Court affirmed the magistrate judge's order. Although we anticipate that in due course the District Court will rule on our arguments for summary judgment against the patent claims of Shuffle Master, if this matter is not resolved as a result of our motion for summary judgment, the District Court will set a date for trial.

ITEM 2. CHANGES IN SECURITIES.

On December 18, 2003, we completed a public offering of 5,000,000 shares of our common stock. The placement agent for the offering was Philadelphia Brokerage Corporation. Our shares of common stock sold in the offering were registered under the Securities Act in a Registration Statement on Form SB-2, as amended (File No. 333-109115), or the Registration Statement. The Securities and Exchange Commission, or the Commission, declared the Registration Statement effective on December 11, 2003.

The public offering price was $5.00 per share for an aggregate sales price of $27,500,000. We paid commissions of $1,925,000 to our placement agent, a non-accountable expense allowance of $25,000 to our placement agent and offering expenses of approximately $750,000. None of the expenses related to the initial public offering were paid directly or indirectly to any of our directors, officers, general partners or their associates, or to any persons owning 10% or more of any class of our equity securities, or to any of our affiliates. We received net proceeds from the public offering of approximately $24,800,000 after deducting the underwriting discounts and commissions and the offering expenses.

From the effective date of the Registration Statement through the six months ended June 30, 2004, we have used approximately $22,400,000 of the $24,800,000 of net proceeds from the initial public offering as follows:

USE OF PROCEEDS TO DATE	AMOUNT
Retirement of loan from Mellon Bank HBV SPV, LLC	$ 2,775,000
Retirement of loan from Triage Capital Management LP	850,000
Retirement of loan from Triage Offshore Fund, Ltd.	1,000,000
Retirement of loan from LC Capital Master Fund, Ltd.	1,000,000
Retirement of a portion of 10% convertible senior notes	7,100,000
Repayment of convertible senior notes	1,600,000
Lease payments	1,200,000
Funding to increase product inventory	1,500,000
Purchase of fixed assets	160,000
Payment of operating expenses	5,215,000
TOTAL	**$ 22,400,000**

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

Not applicable.

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

Not applicable.

ITEM 5. OTHER INFORMATION.

Not applicable.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits.

31.1 Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of President and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).

(b) Reports on Form 8-K.

During the three months ended June 30, 2004, we filed the following:

Current Report on Form 8-K filed on May 10, 2004 reporting the approval of our common stock for listing on the American Stock Exchange under the ticker symbol, “VNX”;

Current Report on Form 8-K filed on May 14, 2004 reporting our financial results for the period ended March 31, 2004; and

Current Report on Form 8-K filed on May 27, 2004 reporting the separation agreements entered into with John R. Spina, our former Chief Financial Officer, and Stacie L. Brown, our former Secretary and Corporate Counsel.

SIGNATURE

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

VENDINGDATA CORPORATION
(Registrant)

Date: August 10, 2004

By: /s/ Steven J. Blad
____

Steven J. Blad
Its: Chief Executive Officer and President
(Principal Executive Officer and Duly Authorized Officer)

EXHIBIT 31.1

CERTIFICATIONS

I, Steven J. Blad, Chief Executive Officer and President of VendingData Corporation, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of VendingData Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;

4. The small business issuer' s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Evaluated the effectiveness of the small business issuer' s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    c. Disclosed in this report any change in the small business issuer' s internal control over financial reporting that occurred during the small business issuer' s most recent fiscal quarter (the small business issuer' s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer' s internal control over financial reporting; and

5. The small business issuer' s other certifying officer and I have disclosed, based on our most recent evaluation, to the small business issuer' s auditors and the audit committee of small business issuer' s board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer' s ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer' s internal control over financial reporting.

Date: August 10, 2004

By: /s/ Steven J. Blad

____

Steven J. Blad, Chief Executive Officer and President

EXHIBIT 31.2

CERTIFICATIONS

I, Douglas H. Caszatt, Acting Chief Financial Officer and Controller of VendingData Corporation, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of VendingData Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;

4. The small business issuer' s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Evaluated the effectiveness of the small business issuer' s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    c. Disclosed in this report any change in the small business issuer' s internal control over financial reporting that occurred during the small business issuer' s most recent fiscal quarter (the small business issuer' s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer' s internal control over financial reporting; and

5. The small business issuer' s other certifying officer and I have disclosed, based on our most recent evaluation, to the small business issuer' s auditors and the audit committee of small business issuer' s board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer' s ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer' s internal control over financial reporting.

Date: August 10, 2004

By: /s/ Douglas H. Caszatt

Douglas H. Caszatt, Acting Chief Financial Officer and Controller

EXHIBIT 32.1

CERTIFICATION PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of VendingData Corporation (the "Company") on Form 10-QSB for the quarterly period ended June 30, 2004, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, Steven J. Blad, Chief Executive Officer and President of the Company, and Douglas H. Caszatt, Acting Chief Financial Officer and Controller of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

By:	/s/ Steven J. Blad __________________	Dated:	August 10, 2004
Title:	Steven J. Blad Chief Executive Officer and President		

By:	/s/ Douglas H. Caszatt __________________	Dated:	August 10, 2004
Title:	Douglas H. Caszatt Acting Chief Financial Officer and Controller		

This certification is made solely for the purposes of 18 U.S.C. Section 1350, subject to the knowledge standard contained therein, and not for any other purpose.