

SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

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FILER

SMITH MICRO SOFTWARE INC

CIK: **948708** | IRS No.: **330029027** | State of Incorpor.: **DE** | Fiscal Year End: **1231**
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTER ENDED SEPTEMBER 30, 1996

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

COMMISSION FILE NUMBER 0-26536

SMITH MICRO SOFTWARE, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE 33-0029027
(STATE OR OTHER JURISDICTION OF (I.R.S. EMPLOYER INCORPORATION OR
ORGANIZATION) IDENTIFICATION NUMBER)

51 COLUMBIA, SUITE 200, ALISO VIEJO, CA 92656
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (714) 362-5800

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT: NONE

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT: COMMON STOCK,
\$.001 PAR VALUE

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES (X) NO ()

As of October 31, 1996, there were 14,074,700 shares of Common Stock outstanding.

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SMITH MICRO SOFTWARE, INC.

FORM 10-Q

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FORWARD LOOKING STATEMENTS

The statements contained in this Quarterly Report on Form 10-Q (the "Form 10-Q") which are not statements of historical fact may be forward looking statements subject to a number of risks and uncertainties. The following factors are amount those that could cause actual results of the Company to materially differ from those anticipated by forward looking statements set forth in this Form 10-Q: demand for communication software; demand for modems and other electronic communication devices; national, regional and international economic conditions affecting the supply of and demand for communication software or offerings by the Company; the Company's ability to compete in and sell its products through the retail channel and OEM distribution channel; demand for the Company's products; the Company's ability to maintain its customer base and to expand that base; and the Company's ability to anticipate and adjust to technological shifts and changes in the electronic communication software and hardware industries. All forward looking statements contained in this Form 10-Q should be considered in light of these and any other factors which might cause the Company's future performance to materially differ from that anticipated by this Form 10-Q.

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PART I - FINANCIAL INFORMATION

SMITH MICRO SOFTWARE, INC. CONSOLIDATED BALANCE SHEETS (IN THOUSANDS)

<TABLE>

<CAPTION>

	SEPTEMBER 30, 1996 ----- (UNAUDITED) <C>	DECEMBER 31, 1995 ----- <C>
CURRENT ASSETS		
Cash & Cash Equivalents	\$14,635	\$19,020
Accounts Receivable, net of allowances for doubtful accounts and other adjustments of \$1,973 (1996) and \$518 (1995)	5,422	3,400
Income Tax Receivable	938	-
Deferred Tax Asset	40	40
Inventory	537	443
Prepays and Other Assets	291	207
	-----	-----
Total Current Assets	21,863	23,110
Equipment and Improvements, net	552	552
Intangible Assets	459	-
	-----	-----
TOTAL ASSETS	\$22,874	\$23,662
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts Payable	\$ 542	\$ 908
Accrued Liabilities	1,065	495
Income Tax Payable	-	79
Distributions Payable to Shareholders	-	1,935
	-----	-----
Total Current Liabilities	1,607	3,417
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY		
Preferred stock, par value \$.001 per share: authorized 5,000,000 shares; none issued and outstanding		
Common stock, par value \$.001 per share: authorized 20,000,000 shares; issued and outstanding 14,074,700 (1996) and 13,700,000 (1995)	14	14
Additional paid-in capital	21,250	18,146
Retained Earnings	3	2,085
	-----	-----
Total Stockholder's Equity	21,267	20,245

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY

\$22,874

\$23,662

</TABLE>

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

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SMITH MICRO SOFTWARE, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE DATA)

<TABLE>
<CAPTION>

	FOR THE THREE MONTHS ENDED SEPTEMBER 30, (UNAUDITED)		FOR THE NINE MONTHS ENDED SEPTEMBER 30, (UNAUDITED)	
	1996	1995	1996	1995
<S>	<C>	<C>	<C>	<C>
Net Revenues	\$ 3,841	\$ 5,054	\$17,147	\$13,077
Cost of Sales	778	1,704	5,541	4,187
Gross Margin	3,063	3,350	11,606	8,890
Operating Expenses:				
Sales & Marketing	574	458	1,857	1,468
Research & Development	957	409	2,409	1,201
General & Administrative	1,088	667	2,829	1,980
Total Operating Expenses	2,619	1,534	7,095	4,649
Operating Income before acquired R&D expenses	444	1,816	4,511	4,241
Acquired Research & Development expense	-	-	5,169	-
Other Income, net	205	37	674	60
Income Before Income Tax	649	1,853	16	4,301
Income Tax Expense	259	142	2,097	176
Net Income (Loss)	\$ 390	\$ 1,711	(\$2,081)	\$ 4,125
PROFORMA INFORMATION				
Net Income before Taxes	\$ 649	\$ 1,853	\$ 16	\$ 4,301
Pro Forma Provision for Income Taxes	259	741 (1)	2,097	1,643 (1)
Pro Forma Net Income (Loss)	390	1,112	(2,081)	2,658
Pro Forma Net Income (Loss) per share	0.03	0.09	(0.15)	0.21
Pro Forma Net Income prior to acquired R&D expenses	\$ 390	\$ 1,112	\$ 3,088 (2)	\$ 2,658
Pro Forma Net Income per Share prior to acquired R&D expenses	0.03	0.09	.22	0.21
Weighted Average Shares Outstanding	14,085	12,678	14,049	12,678

</TABLE>

Note 1: Prior to the public offering of the Company's common stock, the Company was taxed as an S Corporation for Federal and State tax purposes. Concurrent with the public offering concluded in September, 1995, the Company began to be taxed as a C Corporation. Pro Forma income data is presented to show the tax provision as if the Company had been a C Corporation throughout all periods. Pro Forma amounts for 1995 do not reflect a reduction in Founder's compensation which was concurrent with the company going public.

Note 2: During the first quarter of 1996, Smith Micro acquired Performance Computing, Inc. This resulted in a one-time pre-tax charge in the quarter of \$5.169 million. Proforma income data is presented to show the comparable business operations exclusive of this one-time charge.

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

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SMITH MICRO SOFTWARE, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

<TABLE>
<CAPTION>

	FOR THE NINE MONTHS ENDED SEPTEMBER 30, (UNAUDITED)	
	1996	1995
	-----	-----
<S>	<C>	<C>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income (Loss)	(\$2,081)	\$4,125
Adjustments to reconcile net income to net cash provided by operating activities:		
Write-off of in process research and development due to Performance Computing Incorporated acquisition	5,169	-
Depreciation and Amortization	316	160
Provision for doubtful accounts and other adjustments to accounts receivable	1,204	143
Deferred income taxes		(123)
Change in Operating Accounts:		
Accounts Receivable, net	(3,016)	(971)
Income Tax Receivable	(938)	-
Interest receivable		(11)
Inventories	(94)	(8)
Prepaid Expenses and Other Current	(73)	(120)
Accounts Payable	(475)	1,046
Accrued Liabilities	(210)	499
Income Tax Payable	(135)	230
Interest payable on distribution	-	2
	-----	-----
Net Cash Provided (Used) by Operating Activities	(333)	4,972
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of PCI	(2,100)	-
Capital Expenditures	(177)	(248)
	-----	-----
Net Cash Provided (Used) by Investing Activities	(2,277)	(156)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from stock offering	-	18,148
Distributions to S Corporation stockholders	-	(3,839)
Proceeds from the Exercise of Stock Options	160	-
Repayment of Notes Payable to Founders	(1,935)	-
	-----	-----
Net Cash Provided (Used) by Financing Activities	(1,775)	14,309
	-----	-----
NET CHANGE IN CASH & CASH EQUIVALENTS	(\$4,385)	\$19,033
CASH & CASH EQUIVALENTS, Beginning of Period	\$19,020	\$ 632
	-----	-----
CASH & CASH EQUIVALENTS, End of Period	\$14,635	\$19,665
	=====	=====

</TABLE>

<TABLE>
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	FOR THE NINE MONTHS ENDED SEPTEMBER 30, (UNAUDITED)	
	1996	1995
	-----	-----
<S>	<C>	<C>
Detail of businesses acquired in purchase transactions:		
Acquired in-process research and development costs	\$ 5,169	n/a
Fair value of assets acquired	\$ 796	n/a

Common Stock Issued in acquisition	\$ 2,944	n/a
Cash paid for acquisition	\$ 2,100	n/a
Liabilities assumed or created	\$ 921	n/a

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

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SMITH MICRO SOFTWARE, INC.
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation - The accompanying unaudited financial statements have been prepared by Smith Micro Software, Inc. (the "Company") pursuant to Securities and Exchange Commission regulations. On March 14, 1996, the Company acquired Performance Computing Incorporated (PCI), a video software application provider. The periods presented in the financial statements include PCI's operations from the date of acquisition (Note 4). In the opinion of management, such information contains all adjustments, necessary for a fair presentation of the results of such periods. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with the audited financial statements included in the Company's report on Form 10-K for the year ended December 31, 1995.

Cash Equivalents - Cash equivalents are considered to be highly liquid investments with initial maturities of 3 months or less.

Accounts Receivable - The Company sells its products worldwide. The Company performs ongoing credit evaluations of its customers and generally does not require collateral. The Company maintains reserves for potential credit losses, and those losses have been within management's expectations. Allowances for product returns and price protection are included in other adjustments to accounts receivable on the accompanying balance sheets.

Inventories - Inventories consist principally of manuals and diskettes and are stated at the lower of cost (determined by the first-in, first-out method) or market.

Research and Development - Research and development costs are expensed as incurred. The current accounting rule, Accounting for Costs of Computer Software to be Sold, Leased, or Otherwise Marketed, does not materially affect the Company.

Revenue Recognition - The Company recognizes revenues from sales of its software as completed products are shipped, and from royalties from customers who are authorized to duplicate the Company's software as the individual duplication rights are granted, in accordance with Statement of Position 91-1, Software Revenue Recognition. The Company generally allows its retail distributors to exchange unsold products for other products and provides inventory price protection in the event of price reductions by the Company. Allowances for product returns and price protection are estimated based on previous experience and are recorded as a reduction of revenue at the time sales are recognized. The Company provides technical support and customer services to its customers. The Company expenses such costs as incurred as such costs have historically been insignificant.

Income Taxes - The Company accounts for income taxes under Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes ("SFAS 109"). This statement requires the recognition of deferred tax assets and liabilities for future consequences of events that have been recognized in the Company's financial statements or tax returns. The measurement of the deferred items is based on the enacted tax laws. In the event the future consequences of differences between financial reporting bases and the tax bases of the Company's assets and liabilities result in a deferred tax asset, SFAS 109 requires an

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evaluation of the probability of being able to realize the future benefits

indicated by such asset. A valuation allowance related to a deferred tax asset will be recorded when it is more likely than not that some portion or all of the deferred tax asset will not be realized.

Beginning November 1, 1992, the Company and its predecessor, Smith Micro Software, Inc., a California corporation, elected to be treated as an S Corporation under Subchapter S of the Internal Revenue Code of 1986, as amended, and comparable state tax laws. With the exception of Smith Micro Software, Inc. of Colorado (which was taxed as a C Corporation prior to its merger with the Company), substantially all of the Company's earnings from November 1, 1992 until the termination of the Company's S Corporation status on September 21, 1995 generally have been taxed, for federal and state income tax purposes, directly to the Company's existing stockholders rather than to the Company.

2. SUPPLEMENTAL PRO FORMA INFORMATION

Income Taxes - As described in Note 1, the Company has not been subject to most federal and most state income taxes. On September 21, 1995, the Company terminated its status as an S Corporation and became subject to federal and state income taxes. The pro forma information presented on the statement of income reflect a provision for such income taxes as if the Company had been taxed as a C Corporation assuming effective tax rates that would have been in effect for the periods indicated. The principal difference between the effective pro forma tax rate and the statutory federal tax rate relates to state taxes and research and development tax credits.

Acquired Research and Development - On March 14, 1996, the Company acquired the ongoing research and development activities of Performance Computing, Inc. This resulted in a one-time pre-tax charge of \$5.169 million in the first quarter of 1996. The proforma income data is shown to compare the ongoing business operations exclusive of this one-time pre-tax charge.

Pro Forma Net Income Per Share - Pro forma net income per share is based on the weighted average number of shares of common stock and common stock equivalents (stock options) outstanding during the period. The dilutive effect of such common stock equivalents is computed using the treasury stock method. For purposes of such computation, 691,469 shares included for options issued since May, 1995 at an average exercise price of \$7.93 per share are treated as outstanding for all periods presented.

3. INCOME TAXES

As discussed in Note 1, the Company and its predecessor, Smith Micro Software, Inc., a California corporation, elected to be treated as an S Corporation for federal and California franchise tax purposes effective November 1, 1992. Smith Micro Software of Colorado, Inc. was a C Corporation from inception to the time it was merged with the Company and recorded income tax expense for both federal and state purposes during that time. On September 22, 1995, the date of the public offering of the Company's common stock, the Company reverted to C Corporation status. At that time, the Company recorded a \$122,800 deferred tax asset arising principally from cash to accrual timing differences and non-deductible reserves. The difference between the effective tax rate of the Company and the statutory federal tax rate is primarily attributable to income tax as an S Corporation and the establishment of deferred taxes.

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4. ACQUISITION OF PERFORMANCE COMPUTING INCORPORATED

On March 14, 1996, the Company acquired all outstanding shares of Performance Computing Incorporated for \$5,965,053 in cash and stock. The transaction was accounted for as a purchase and the Company obtained an independent valuation of the net assets acquired. In accordance with FASB Interpretation No. 4, the Company is required to write-off acquired in-process research and development in the period in which the acquisition is consummated. As a result, the company recorded a one-time pre-tax charge to earnings of \$5,169,000. In addition, the Company recorded an issuance of 350,000 additional common stock shares, acquired assets of \$245,000, intangible assets of \$551,000 (consisting of covenants not to compete of \$381,000, current technology of \$154,000 and goodwill of \$16,000), assumed liabilities of \$321,000, and accrued anticipated obligations of \$600,000 pursuant to the acquisition.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

GENERAL

Smith Micro was founded in March 1982 to design and market financial software. In the mid-1980s, the Company shifted its focus to communication software for modem manufacturers. The Company shipped its first data communication software product in 1985 and, since that time, the Company's growth in revenues has been the result of the market acceptance of its data, fax and video communication software products.

The Company recognizes revenues from sales of its software as completed products are shipped and from royalties from customers who are authorized to duplicate the Company's software. The Company expects that revenues from its QuickLink products will continue to account for a substantial portion of the Company's revenues. The Company believes that the video and retail based products will also represent a substantial portion of the revenue in the future. Any material reduction in demand for the Company's products would have a material adverse effect on the Company's business, results of operations and financial condition. The Company has continued to expand its business by introducing new products and its future success will depend in part on the continued introduction of new and enhanced OEM and retail products that achieve market acceptance. Revenues are net of estimated returns and other adjustments at the time the products are shipped. The Company has allowed its customers to return unused software, constituting 3.7% and 2.3% of the Company's net revenues for 1994 and 1995, respectively.

From November 1, 1992 through September 21, 1995 (the closing date of the Company's initial public offering), the Company elected to be treated as an S Corporation for federal income tax purposes. As a consequence, the Company generally did not have, during this period, an income tax liability and the Company's earnings have been treated as being distributed to the existing stockholders for income tax reporting purposes. Until the initial public offering of the Company's stock, William Smith and Rhonda Smith had been the sole stockholders of the Company from its inception. They have drawn compensation on an irregular basis from the Company, portions of which were paid to satisfy tax liabilities arising from the allocation of the Company's earnings to William Smith and Rhonda Smith as a result of the Company's S Corporation status. The timing of the compensation has had the effect of creating sizable quarterly fluctuations in general and administrative expenses and, consequently, the Company's historical operating results.

A small number of customers have historically accounted for a substantial portion of the Company's revenues. Sales to U.S. Robotics (including, for 1995, sales to Megahertz which U.S. Robotics acquired in February 1995), in particular, which became a customer in the fourth quarter of 1993, accounted for approximately 5%, 36%, 52% and 51% of the Company's net revenues for the years ended 1993, 1994, 1995, and the nine months ended September 30, 1996, respectively. During 1993, 1994 and 1995, the Company's three largest customers, including U.S. Robotics, accounted for approximately 38%, 57% and 67%, respectively, of net revenues. For the nine months ended September 30, 1996 the Company's three largest customers, including U.S. Robotics, accounted for approximately 72% of net revenues. Any reduction, delay or change in orders from such customers could have a material adverse effect on the Company's business, results of operations and financial condition.

In March 1996, the Company entered into a one-year OEM agreement with U.S. Robotics Access Corp., one of several wholly-owned subsidiaries of U.S. Robotics Corporation which agreement superseded the previous agreement between the parties. This agreement was amended and restated in June of 1996 and runs until April 1997. Under the terms of the new agreement, the Company granted certain pricing incentives to U.S. Robotics Access Corp. in consideration for which the Company became the exclusive provider of fax, data, voice and telephony communications software for certain U.S. Robotics modems. In addition, under the terms of the agreement, U.S. Robotics Access Corp. has agreed to place Smith Micro retail products and commercials for such products on certain U.S. Robotics compact disks. The agreement renews automatically at the end of each one year term unless either party provides at least 60 days notice of its intention to terminate the agreement at the end of the

then-current term. Moreover, the agreement does not require U.S. Robotics Access Corp. or any other U.S. Robotics-affiliated entity to purchase any minimum quantity of Smith Micro products and may be terminated by U.S. Robotics at any time for any reason upon 90 days written notice. As a result, there can be no assurance that U.S. Robotics will continue to purchase the Company's products. While the Company believes that it has been the principal supplier of OEM communication software products to U.S. Robotics (excluding Megahertz), there can be no assurance that U.S. Robotics will not seek additional sources for such products in the future. Accordingly, there can be no assurance that sales to U.S. Robotics will reach or exceed historical levels in any future period. A substantial decrease or delay in sales to U.S. Robotics would have a material adverse effect on the Company's business, results of operations and financial condition. Assuming the number of products sold to U.S. Robotics Access Corp. were to remain at 1995 levels, in light of the pricing incentives provided in the agreement, gross revenues from U.S. Robotics with respect to products covered by the agreement could be adversely affected, although the Company believes that net income attributable to such sales would not be impacted negatively.

The Company entered into a one-year agreement with Motorola in January 1996 to provide retail and OEM products to Motorola's PCMCIA Division and Information Systems Group. This agreement is automatically renewable for consecutive one-year terms, but either party may terminate the agreement at the end of the then-current term by providing 60 days notice to the other party. Moreover, as with the U.S. Robotics Access Corp. agreement, the Motorola agreement does not require Motorola to purchase any minimum quantity of Smith Micro products and, as a result, there can be no assurance that Motorola will order any additional products or that it will develop into a substantial customer of the Company.

The OEM product ordering cycle beginning from placement of an order to shipping is very short. OEM customers generally operate under a just-in-time system and order software to be delivered as needed by their manufacturing operations. The Company's products are generally shipped as orders are received and, accordingly, the Company has historically operated with little backlog, and does not consider backlog to be a significant indication of future performance. As a result, sales in any quarter are dependent on orders booked and shipped in that quarter and are not predictable with any degree of certainty. Moreover, the Company does not generally produce software in advance of orders and therefore has not maintained a material amount of inventory.

As the Company's retail sales have grown there has been an increase of inventory held by distributors and retail stores. As inventory in the retail channel builds it

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increases the Company's exposure to product returns. This exposure is considered when the allowance is made for product returns. Substantial returns of product from the retail channel could have a material adverse effect on the Company's business, results of operations and financial condition.

On March 14, 1996, the Company acquired Performance Computing Incorporated for \$5,965,053 in cash and stock. The Company obtained an independent valuation of the net assets acquired. In accordance with FASB Interpretation No. 4, the Company is required to write-off in-process research and development in the period in which the acquisition is consummated. In accounting for the acquisition, the Company recorded a one-time pre-tax charge to earnings of \$5,169,000 to account for the in-process research and development. In addition, the Company recorded in issuance of 350,000 additional Common Stock Shares, acquired assets of \$245,000, intangible assets of \$551,000 (consisting of covenants not to compete of \$381,000, current technology of \$154,000 and goodwill of \$16,000), and assumed liabilities of \$321,000 as well as a milestone agreement initiated with the acquisition of \$600,000.

The following discussion should be read in conjunction with, and is qualified in its entirety by, the Financial Statements and related notes thereto included elsewhere. Historical results of operations, percentage relationships and any trends that may be inferred from the discussion below are not necessarily indicative of the operating results for any future period.

RESULTS OF OPERATIONS

The following table sets forth for the periods indicated, the percentages of net revenues represented by each item in the Company's statement of income. The proforma information for 1996, includes activity for Performance Computing Incorporated since March 15, 1996.

<TABLE>

<CAPTION>

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	1996	1995	1996	1995
<S>	<C>	<C>	<C>	<C>
Net revenues	100.0%	100.0%	100.0%	100.0%
Cost of sales	20.3	33.7	32.3	32.0
Gross profit	79.7	66.3	67.7	68.0
Operating expenses:				
Sales and marketing	14.9	9.1	10.8	11.2
Research and development	24.9	8.1	14.0	9.2
General and Administrative	28.3	13.2	16.5	15.1
Total operating expenses	68.1	30.4	41.4	35.6
Operating income	11.6	35.9	26.3	32.4
In-Process R&D Expense	.-	.-	30.1	.-
Other income (expense), net	5.3	.7	(3.9)	.5
Income before income tax expense	16.9	36.7	.1	32.9
Income tax expense	6.8	2.8	12.2	1.3
Net income	10.1%	33.9%	(12.1%)	31.5%

</TABLE>

NET REVENUES

Net revenues decreased 24%, from \$5.1 million in the three months ended September 30, 1995 to \$3.8 million in the three month period ended September 30, 1996. This decrease was primarily due to a broad based slowdown in the Company's OEM business. Offsetting some of this decrease was the continued expansion of the Company's retail business.

Net revenues increased 31%, or \$4.0 million, from \$13.1 million in the nine months ended September 30, 1995 to \$17.1 million in the nine month period ended September 30, 1996. This increase in revenue represented a \$2 million increase in OEM sales, and a \$2 million increase in retail sales. The increased retail sales were driven primarily by the Company's POTS (Plain Old Telephone Lines) based videoconferencing software product, Audiovision and the fax software product, Hotfax, as well as a new product introduced in the most recent quarter, HotFax Message Center, a fully integrated fax, data and voice application supporting Windows, Windows 95 and Windows NT.

Certain of the Company's significant customers and other modem manufacturers have recently announced that during the most recently completed quarter there was an increase of inventory in the channel which may reduce their rates of growth in subsequent quarters. The rate at which this inventory moves out of the channel could have a significant impact on the Company's net revenues and operating results in subsequent quarters.

GROSS PROFIT

Gross profit represents net revenues, less cost of sales, which includes costs of materials, costs related to the operations of the Company's duplicating facilities, freight charges and royalties to licensors. Gross profit decreased \$287 thousand from \$3.4 million in the three months ended September 30, 1995, to \$3.1 million, in the three months ended September 30,

1996. As a percentage of net revenues, gross profits increased 13% from 66% in the three months ended September 30, 1995, to 80% in the three months ended September 30, 1996.

Gross profit increased 31% from \$8.9 million in the nine months ended September 30, 1995, to \$11.6 million, in the nine months ended September 30, 1996. As a percentage of net revenues, gross profits remained unchanged at 68% during the nine months ended September 30, 1996. In the first quarter of 1996, the Company began supplying a substantial portion of its software to one of its largest customers on CD ROM format, which costs considerably more than the conventional diskette format, which was the primary reason for lower margins in the first quarter. During the second quarter of 1996, the Company changed the product format for this customer to a royalty based arrangement, which along with increased retail sales, improved the margins in the second and third quarters.

SALES AND MARKETING EXPENSES

Sales and marketing expenses consist primarily of personnel costs, advertising costs, sales commissions and trade show expenses. These expenses vary considerably from quarter to quarter based on the timing of trade shows and new product introductions. Sales and marketing expenses increased 25% from \$458,000 in the three months ended September 30, 1995, to \$574,000 in the three months ended September 30, 1996. The increase in sales and marketing expenses is primarily due to additional personnel as well as promotional campaigns in the retail channel. As a percent of net revenues, sales and marketing expenses increased to 15% from 9% of net revenues, primarily due to the decline in revenues.

Sales and marketing expenses increased 26% from \$1,468,000 in the nine months ended September 30, 1995, to \$1,857,000 in the nine months ended September 30, 1996. The increase in sales and marketing expenses is primarily due to additional personnel as well as promotional campaigns in the retail channel. As a percent of net revenues, sales and marketing expenses remained unchanged at 11% of net revenues.

RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses consist primarily of personnel and supply costs required to conduct the Company's software development activities. Research and development expenses rose 134% from \$409,000 in the three months ended September 30, 1995, to \$957,000 in the three months ended September 30, 1996. This increase was primarily due to the addition of staff as a result of the acquisition of Performance Computing Inc., late in the first quarter of 1996 as well as addition of software engineers in the company's Texas, Colorado, and California offices. As a percent of net revenues, research and development expenses increased to 25% from 8% of net revenues, as the Company dedicated more resources to product development, and also as a result of the decrease in revenues.

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Research and development expenses rose 101% from \$1,201,000 in the nine months ended September 30, 1995, to \$2,409,000 in the nine months ended September 30, 1996. This increase was primarily due to the addition of staff as a result of the acquisition of Performance Computing Inc., late in the first quarter of 1996 as well as addition of software engineers in the Company's Texas, Colorado, and California offices as the Company continues to dedicate more resources to product development. As a percent of net revenues, research and development expenses increased to 14% from 9% of net revenues, due to the additional personnel.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses encompass expenses related to general operations, which are not included as costs of sales, sales and marketing or research and development. General and administrative expenses rose 63%, from \$667,000 in the three months ended September 30, 1995, to \$1,088,000 in the three months ended September 30, 1996. The increase is primarily attributable to general expenses related to the expansion of the Company's facilities and the addition of administrative personnel to support the Company's growth. As a percent of net revenues, general and administrative expenses increased to 28% from 13% of net revenues, primarily due to the decrease in revenues

General and administrative expenses rose 43%, from \$1,980,000 in the nine months ended September 30, 1995, to \$2,829,000 in the nine months ended September 30, 1996. The increase is primarily attributable to general expenses

related to the expansion of the Company's facilities and the addition of administrative personnel to support the Company's growth. As a percent of net revenues, general and administrative expenses increased to 16% from 15% of net revenues.

INCOME TAXES

Prior to its initial public offering on September 22, 1995, the Company was treated as an S Corporation for federal and certain state tax purposes. Subsequent to the offering, the company is taxed as a C Corporation at an effective tax rate of approximately 40%. As such, income tax expense was \$259,000 in the quarter ended September 30, 1996 as compared to \$142,000 in the quarter ended September 30, 1995.

LIQUIDITY AND CAPITAL RESOURCES

Since its inception, the Company has financed its operations primarily through cash generated from operations. Net cash used by operating activities was \$333,000 in the nine month period ended September 30, 1996 as compared to \$5.0 million provided by operations in the nine month period ended September 30, 1995. In the nine month period ended September 30, 1996, the increase in receivable balances was the primary use of cash in operations. During the nine month period ended September 30, 1996, the Company used \$2.3 million in investing activities, primarily for the acquisition of Performance Computing Incorporated in the first quarter of 1996. During the nine months ended September 30, 1996, \$1.8 million was used in financing activities, which primarily consisted of the retirement of a loan payable to the company's founders.

At September 30, 1996, the Company had \$14.6 million in cash and cash equivalents and \$20.2 million of working capital. The Company had \$5.4 million of accounts receivable, net of allowance for doubtful accounts and other adjustments. The Company has no

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significant capital commitments and currently anticipates that growth in capital expenditures will not vary significantly from recent periods.

RISK FACTORS

In addition to the other information contained in this Form 10-Q, the following risk factors should be considered in evaluating the Company and a decision to invest in the Company. This Form 10-Q contains forward looking statements which involve risks and uncertainties and the Company's actual results may materially differ from the results anticipated in those statements. Factors that might cause such a difference include, without limitation, those discussed in this section and elsewhere in this Form 10-Q.

Fluctuations in Quarterly Operating Results. Certain of the Company's significant customers and other modem manufacturers have announced in recent quarters that there was an increase of inventory in the channel which may reduce their rates of growth during subsequent quarters. The rate at which this inventory is moved out of the channel could have a significant impact on the Company's operating results in future quarters. The Company's operating results have in the past fluctuated, and may in the future fluctuate, from quarter to quarter as a result of a number of factors including, but not limited to, the size and timing of orders from, and shipments to, major customers; the ability of the Company's customers to obtain financing for the purchase of the Company's products; changes in pricing policies or price reductions by the Company or its competitors; variations in the Company's sales channels or the mix of product sales; the timing of new product announcements and introductions by the Company or its competitors; the availability and cost of supplies; the financial stability of major customers; market acceptance of new products, applications and product enhancements; the Company's ability to develop, introduce and market new products, applications and product enhancements; the Company's ability to control costs; possible delays in the shipment of new products; the Company's success in expanding its sales and marketing programs; deferrals of customer orders in anticipation of new products, applications, product enhancements or operating systems; changes in Company strategy; personnel changes; and general economic factors. The Company's software products are generally shipped as orders are received and accordingly, the Company has historically operated with little backlog. As a result, sales in any quarter are dependent on orders booked and shipped in that quarter and are not predictable with any degree of certainty. In addition, the Company's expense levels are based, in part, on its expectations as to future revenues.

If revenue levels are below expectations, operating results are likely to be adversely affected. The Company's net income may be disproportionately affected by a reduction in revenues because of fixed costs related to generating its revenues. While the Company has not historically experienced seasonality in its sales, many of the Company's OEM customers experience seasonality in their sales, and the Company's sales may, in the future, be subject to seasonality particularly as its sales of retail products increase. Quarterly results in the future may be influenced by these or other factors and, accordingly, there may be significant variations in the Company's quarterly operating results. Further, the Company's historical operating results are not necessarily indicative of future performance for any particular period and there can be no assurance that the Company's recent revenue growth or its profitability will continue on a quarterly or annual basis. Due to all of the foregoing factors, it is possible that in some future quarter the Company's operating results may be below the expectations of public market analysts and investors. In such event, the price of the Company's Common Stock would likely be materially adversely affected.

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Reliance on U.S. Robotics. In 1993, 1994 and 1995, U.S. Robotics (including, with respect to 1995, Megahertz, which U.S. Robotics acquired in February 1995), represented 4.9%, 35.8% and 52.1%, respectively, of the Company's net revenues. The Company expects that U.S. Robotics, which became a customer in the fourth quarter of 1993, will continue to account for a significant portion of the Company's revenues in future periods. In March 1996, the Company entered into a new one-year OEM agreement with U.S. Robotics Access Corp., one of several wholly-owned subsidiaries of U.S. Robotics Corporation. This agreement was amended and restated in June of 1996 and runs until April 1997. This OEM agreement superseded the previous agreement between the parties. Under the terms of the new agreement, the Company granted certain pricing incentives to U.S. Robotics Access Corp. in consideration for which the Company became the exclusive provider of fax, data, voice and telephony communications software for certain U.S. Robotics modems. In addition, under the terms of the agreement, U.S. Robotics Access Corp. has agreed to place Smith Micro retail products and commercials for such products on certain U.S. Robotics compact disks. The agreement renews automatically at the end of each one year term unless either party provides at least 60 days notice of its intention to terminate the agreement at the end of the then-current term. Moreover, the agreement does not require U.S. Robotics Access Corp. or any other U.S. Robotics-affiliated entity to purchase any minimum quantity of Smith Micro products and moreover may be terminated by U.S. Robotics at any time for any reason upon 90 days written notice. As a result, there can be no assurance that U.S. Robotics will continue to purchase the Company's products. While the Company believes that it has been the principal supplier of OEM communication software products to U.S. Robotics (excluding Megahertz), there can be no assurance that U.S. Robotics will not seek additional sources for such products in the future. Accordingly, there can be no assurance that sales to U.S. Robotics will reach or exceed historical levels in any future period. A substantial decrease or delay in sales to U.S. Robotics would have a material adverse effect on the Company's business, results of operations and financial condition. Assuming the number of products sold to U.S. Robotics Access Corp. were to remain at 1995 levels, in light of the pricing incentives provided in the agreement, gross revenues from U.S. Robotics with respect to products covered by the agreement could be adversely affected.

Concentration of Customer Revenues. In addition to its reliance on U.S. Robotics, the Company has in the past derived, and expects in the future to derive, a significant portion of its revenues from a relatively small number of customers. Approximately 37.6%, 56.7% and 66.8% of the Company's net revenues in 1993, 1994 and 1995, respectively, were derived from sales of products to the Company's three largest customers, including U.S. Robotics. The Company expects that it will continue to be dependent upon relatively large orders from these customers and a limited number of other OEM customers for a significant portion of its revenues in future periods, although none of them is obligated to purchase any products. Accordingly, there can be no assurance that any sales to these entities, individually or as a group, will continue or, if continued, will reach or exceed historical levels in any future period. Any substantial decrease or delay in sales to one or more of these entities would have a material adverse effect on the Company's business, results of operations and financial condition. In addition, certain of the Company's OEM customers have in the past and may in the future acquire competitors or be acquired by competitors, causing further consolidation in the modem industry. Hayes Microcomputer Products ("Hayes"), one of the Company's significant OEM customers, previously acquired Practical Peripherals, another OEM customer of the Company. Hayes (including Practical Peripherals) accounted for 15.4% and 9.8% of the Company's net revenues for 1994 and 1995, respectively. Previous

acquisitions in the modem industry have often caused the purchasing departments of the combined companies to reevaluate their purchasing decisions. There can be no assurance that such acquisitions will not result in a change in a current customer's

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purchasing habits, including a loss of the customer, a decrease in orders from that customer or a delay in orders previously made by the customer. Moreover, acquisitions involving existing OEM customers may cause the concentration of the Company's customer revenues to increase if the combined companies continue to purchase the Company's software products. Although the Company maintains adequate allowances for doubtful accounts, the insolvency of one or more of the other major customers of the Company could substantially impair the Company's business, results of operations and financial condition.

Product Concentration. The Company has in the past derived, and may in the future derive, a significant portion of its revenues from a relatively small number of products. In 1995, 83.9% of the Company's net revenues were derived from the sale of various versions of QuickLink II Fax and 9.6% of the Company's net revenues were derived from MacComCenter, which is the QuickLink II Fax equivalent for the Macintosh market. The Company expects that revenues from these products will continue to account for a substantial portion of the Company's total revenues in the foreseeable future. Declines in the revenues from these software products, whether as a result of competition, technological change, price pressures or other factors, would have a material adverse effect on the Company's business, results of operations and financial condition. Further, life cycles of the Company's products are difficult to estimate due in large measure to the recent emergence of the Company's market, the effect of new products, applications or product enhancements, technological changes in the communication software industry in which the Company operates and future competition. The Company's future financial performance will depend in part on the successful development, introduction and market acceptance of new products, applications and product enhancements. There can be no assurance that the Company will continue to be successful in marketing its current products or any new products, applications or product enhancements.

Technological Change. The communication software market for personal computers is characterized by rapid technological change, changing customer needs, frequent product introductions and evolving industry standards. The introduction of products incorporating new technologies and the emergence of new industry standards could render the Company's existing products obsolete and unmarketable. The Company's future success will depend upon its ability to develop and introduce new software products (including new releases, applications and enhancements) on a timely basis that keep pace with technological developments and emerging industry standards and address the increasingly sophisticated needs of its customers. There can be no assurance that the Company will be successful in developing and marketing new products that respond to technological changes or evolving industry standards, that the Company will not experience difficulties that could delay or prevent the successful development, introduction and marketing of these new products, or that its new products will adequately meet the requirements of the marketplace and achieve market acceptance. If the Company is unable, for technological or other reasons, to develop and introduce new products in a timely manner in response to changing market conditions or customer requirements, the Company's business, results of operations and financial condition would be materially adversely affected.

There can be no assurance that the Company will successfully develop new versions of its software products that will operate on Windows 95, or that any such development, even if successful, will be completed concurrently with or prior to introductions by competitors of communication software products for Windows 95. Any such failure or delay could affect the Company's competitive position or lead to product obsolescence in the future. While the Company ships software to a number of computer manufacturers, its primary OEM customers are modem manufacturers. The Company is aware that technology is

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being developed to enable the functions of the modem to be performed by a chip embedded into the computer. This development, if and when it comes to market, could impair the business of those of the Company's customers that rely on the

existence of a separate modem component for their continued success. A downturn in the business of one or more of its principal customers could adversely affect the Company's business, results of operations and financial condition.

Competitive Threat from Microsoft Windows 95 and Other Operating Systems. The Company faces competition from Microsoft, which dominates the personal computer software industry. Due to its market dominance and the fact that it is the publisher of the most prevalent personal computer operating platforms, DOS and Windows, Microsoft represents a significant competitive threat to all personal computer software vendors, including the Company. In addition, Windows 95, the new Microsoft operating system, includes capabilities now provided by certain of the Company's OEM and retail software products, including the Company's principal product, QuickLink II Fax. Other operating systems, such as OS/2, offer communications capabilities as well. If the communications capabilities of Windows 95 or other operating systems are adopted by users, sales of the Company's products could decline.

Competition. The markets in which the Company operates are highly competitive and subject to rapid changes in technology. The strategic directions of major personal computer hardware manufacturers and operating system developers are also subject to changes. The Company competes with other software vendors for access to distribution channels, retail shelf space and the attention of customers. The Company also competes with other software companies in its efforts to acquire software technology developed by third parties. These factors may result in increased price competition. Additionally, there can be no assurance that competitors will not develop or acquire products that are superior to the Company's products or that achieve greater market acceptance.

Reliance on Retail Channel. As the Company's retail sales have grown there has been an increase of inventory held by distributors and retail stores. As inventory in the retail channel builds it increases the Company's exposure to product returns. This exposure is considered when the allowance is made for product returns. Substantial returns of product from the retail channel could have a material adverse affect on the Company's business, results of operations and financial condition.

The Company expects that its new retail products will face significant competition. In the retail market, HotFax, the Company's principal retail product competes directly with Symantec/Delrina's WinFax Pro 7.0. Symantec/Delrina is well established in the retail distribution channel. There can be no assurance that HotFax, Audiovision, HotPage or any other of the retail product line will capture a significant share of the retail market for communication software. In the OEM distribution channel, the Company has several strong competitors, among them Symantec/Delrina and Global Village. Some of the Company's competitors have a retail emphasis and offer OEM products with a reduced set of features. The opportunity for retail upgrade sales may induce these and other competitors to make OEM products available at their own cost or even at a loss. Such a pricing strategy could have an adverse affect on the Company's business, results of operations and financial condition.

Symantec/Delrina currently make certain products that are complementary with products sold by each other. The combined entity may be able to enhance its competitive position by bundling certain of these products to attract customers seeking integrated, cost-effective software applications. The Company also believes that the market in which it competes has been characterized by the consolidation of established communication

software suppliers and that this trend, which may lead to the creation of additional large and well-financed competitors, may continue. In addition, other competitors have entered the market. Moreover, because there are low barriers to entry into the software market, the Company believes that competition will increase in the future. To remain competitive, the Company believes that it will need to make continuing investments in research and development and sales and marketing. There can be no assurance that the Company will have sufficient resources to make such investments, or that it will be successful in its research and development or sales and marketing efforts.

Symantec/Delrina and many of the Company's current and prospective competitors have significantly greater financial, marketing, service, support, technical and other resources than the Company. Moreover, these companies may introduce additional products that are competitive with those of the Company, and there can be no assurance that the Company's products would compete effectively with such products. The Company believes that its ability to compete depends on elements both within and outside its control, including the

success and timing of new product development, product performance and price, distribution and customer support and introduction by the Company and its competitors of new products. There can be no assurance that the Company will be able to compete successfully with respect to these and other factors. The Company believes that the market for its software products has been and will continue to be characterized by significant price competition. A material reduction in the price of the Company's products could negatively affect the Company's profitability.

Many of the Company's existing and potential OEM customers are major manufacturers of modems and have substantial technological capabilities. These customers may currently be developing, or may in the future develop, products that compete directly with the Company's products and may, therefore, discontinue purchases of the Company's products. The Company's future performance is substantially dependent upon the extent to which existing OEM customers elect to purchase communication software from the Company rather than design and develop their own software. In light of the fact that the Company's customers are not contractually obligated to purchase any of the Company's products, there can be no assurance that the Company's existing OEM customers will continue to rely, or expand their reliance, on the Company as an external source for communication software.

Dependence on New Product Offerings. The Company's future success will depend, in significant part, on its ability to successfully develop and introduce new software products and improved versions of existing software products on a timely basis and in a manner that will allow such products to achieve broad customer acceptance. As a result of its acquisition of PCI, the Company expects to begin offering a personal computer-based video conferencing product to its OEM customers in the near future. There can be no assurance that this and other new products will be introduced on a timely basis, if at all. If new products are delayed or do not achieve market acceptance, the Company's business, results of operations and financial condition will be materially adversely affected. In the past, the Company has also experienced delays in purchases of its products by customers anticipating the launch of new products by the Company. There can be no assurance that material order deferrals in anticipation of new product introductions will not occur. There can also be no assurance that the Company will be successful in developing, introducing on a timely basis and marketing such software or that any such software will be accepted in the market.

Retail Product Strategy Unproven. The Company's revenues have increased during the past five years almost entirely on the strength of its OEM sales. The Company is

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developing retail products with expanded functionality from its OEM products, and the Company expects to introduce other products in the retail distribution channel as well, including a retail video conferencing product with enhanced features. The ability to maintain distributor and retailer relationships is largely a function of volumes. If the Company does not meet certain minimum volume requirements, it will not be able to maintain its relationships. With unproven products and its distribution system at early stages, there can be no assurance that the Company's retail marketing plan will succeed. Further, while retail products provide higher unit revenues than OEM products, retail distribution entails significantly higher costs. These costs include advertising, trade shows, public relations and the expenses related to the development and maintenance of a sales force dedicated to the retail distribution effort. Accordingly, there can be no assurance that retail sales will provide the margins that the Company has been able to achieve on its OEM sales or that distributor and retailer minimum volume requirements will be met.

In implementing its retail sales strategy, the Company expects to rely on distributors, retailers and value added resellers (collectively, "resellers") for the marketing and distribution of HotFax for Windows and Windows 95 and its other retail products. The Company's agreements with resellers are not expected to be exclusive and in many cases may be terminated by either party without cause. Many of the Company's resellers carry product lines that are competitive with those of the Company. There can be no assurance that these resellers will give a high priority to the marketing of the Company's products or that resellers will continue to carry the Company's products. These resellers typically are allowed to return products without charge or penalty. A component of the Company's revenue recognition policy is that the Company calculates an allowance for product returns based on its historical experience. If retail sales of the Company's products increase, the risk of product returns will increase. While the Company's revenue recognition policy contemplates this risk, it is possible that returns may occur in excess of the Company's previous experience, causing the Company to revise its

estimates and increase the allowances for such returns. Excessive or unanticipated returns could materially adversely affect the Company's business, results of operations and financial condition. The Company's results of operations could also be materially adversely affected by changes in reseller inventory strategies, which could occur rapidly, and in many cases, may not be related to end user demand. There can be no assurance that the Company will be successful in recruiting resellers to represent it. Any of these anticipated changes in the Company's distribution channels could materially adversely affect the Company's business, results of operations and financial condition.

Potential for Undetected Errors. Software products as complex as those offered by the Company may contain undetected errors. The Company has in the past discovered software errors in certain of its products and has experienced delayed or lost revenues during the period required to correct these errors. There can be no assurance that, despite testing by the Company and by current and potential customers, errors will not be found in new or existing products after commencement of commercial shipments, resulting in loss of or delay in market acceptance or the recall of such products, which could have a material adverse effect upon the Company's business, results of operations and financial condition. The Company provides customer support for most of its products. The Company is preparing to launch several new products. If these products are flawed or are more difficult to use than traditional Company products, customer support costs could rise and customer satisfaction levels could fall.

Pre-Load Software Market. The Company primarily sells its software in a form that includes a disk and a manual. Some of its customers "pre-load" the Company's software onto

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a hard disk. This arrangement eliminates the need for a disk and may eliminate the need for a manual. These pre-load arrangements produce smaller unit revenues for the Company and eliminate the Company's ability to generate revenues from its production facilities. The Company believes these facilities contribute profits to the Company. Currently, the Company produces its products on 3 1/2-inch diskettes. The Company does not currently have the capability to produce CD-ROMs and the cost to develop such production capability may be prohibitive. In the event of a shift of this kind, more of the Company's relationships would involve product pre-loads and the Company's business, results of operations and financial condition could be adversely affected.

Dependence Upon Key Personnel. The Company's future performance depends in significant part upon the continued service of William Smith and Rhonda Smith, the Company's co-founders, and other key technical and senior management personnel. The Company is dependent on its ability to identify, hire, train, retain and motivate high quality personnel, especially highly skilled engineers involved in the ongoing research and development required to develop and enhance the Company's communication software products and introduce enhanced future applications. The industry is characterized by a high level of employee mobility and aggressive recruiting of skilled personnel. There can be no assurance that the Company's current employees will continue to work for the Company. Loss of services of key employees could have a material adverse effect on the Company's business, results of operations and financial condition. In addition, the Company may need to grant additional options and provide other forms of incentive compensation to attract and retain key personnel.

Management of Growth. The Company has recently experienced a period of significantly expanding operations and headcount, which has placed, and will continue to place, a significant strain on the Company's limited personnel and other resources. One of the Company's executive officers commenced employment with the Company in March 1996. The Company's ability to manage any future increases in the scope of its operations or headcount, should they occur, will depend on significant expansion of its manufacturing, research and development, marketing and sales, management and financial and administrative capabilities. The failure of the Company's management to effectively manage any expansion in its business could have a material adverse effect on the Company's business, results of operations and financial condition.

Acquisition-Related Risks. The recent acquisition of PCI by the Company will present it with numerous challenges, including difficulties in the assimilation of the operations, technologies, products and personnel of the acquired company and managing separate geographic operations. The process of integrating PCI's business into the Company's operations may result in unforeseen operating difficulties and expenditures and may absorb significant management attention that would otherwise be available for the ongoing development of the Company's business. If the Company's management does not respond to these challenges effectively, the Company's business, results of

operations and financial condition could be adversely affected. Moreover, there can be no assurance that the anticipated benefits of the acquisition will be realized. In particular, Smith Micro's interest in PCI is based primarily on the Company's evaluation of the market potential for PCI's new personal computer-based, video conferencing products which have yet to be proven in the marketplace. Delays in or non-completion of the development of these new products, or lack of market acceptance of such products, could have an adverse impact on the Company's business, results of operations and financial condition and result in a failure to realize anticipated benefits of the acquisition.

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Duplication of Software. The Company duplicates nearly all of its software at its Aliso Viejo, California facility. The Company believes that its internal duplication capability provides it with a competitive advantage since it eliminates the profit margin required by outside duplication sources and enables a high degree of scheduling control. This concentration of production does, however, expose the Company to the risk that production could be disrupted by natural disaster or other events, such as the presence of a virus in the Company's duplicators. The Company believes that it could retain outside duplication alternatives quickly, but there is no assurance that it could do so or, if such arrangements could be made, that duplication could take place in an economical or timely manner.

Reliance on Third Party Suppliers; Shortage of Modem Chips. The Company relies on third party suppliers who provide the components used in its kitted products. These components include disks, CD's and printed manuals. Disk shortages have occurred in the past and there can be no assurance that shortages will not recur. If the Company cannot obtain a sufficient quantity of disks or other components, or cannot obtain disks or other components at prices at least comparable to prices paid currently, the Company's business, results of operations and financial condition could be adversely affected.

Modem manufacturers purchase chips from a relatively limited number of chip manufacturers. Production problems or product quality problems experienced by a chip manufacturer could reduce modem sales or slow the growth of modem sales. Chip manufacturers have a limited capacity to produce chips. This capacity cannot be quickly expanded and the capital investment to expand capacity is high. If chip suppliers are unable to meet demand, the growth of modem sales will slow. The Company believes that chip suppliers currently lack sufficient capacity to meet the demand for certain chips used by modem manufacturers, including the Company's OEM customers. If this shortage continues, it could adversely affect sales of the Company's OEM communication software.

International Sales. The Company presently operates in foreign markets and intends to expand its international presence. For the twelve months ended December 31, 1995, the Company generated 16.6% of its net revenues outside of the United States, up from 12.7% for the twelve months ended December 31, 1994, of these amounts, 4.8% and 5.5%, respectively, were attributable to sales to modem manufacturers located in Taiwan. International business is subject to risks in addition to those inherent in the Company's United States business including substantially different regulatory requirements in different jurisdictions, varying technical standards, tariffs and trade barriers, political and economic instability, reduced protection for intellectual property rights in certain countries, difficulties in staffing and maintaining foreign operations, difficulties in managing distributors, potentially adverse tax consequences, foreign currency exchange fluctuations, the burden of complying with a wide variety of complex foreign laws and treaties and the possibility of difficulties in collecting accounts receivable. There can be no assurance that the Company will be able to continue to generate significant international sales. While the Company does not currently accept payment in foreign currencies and invoices all of its sales in U.S. dollars, there can be no assurance that the Company will be able to continue this policy if it is able to grow international sales. If the Company begins to receive payment in foreign currencies, it is likely to be subjected to the risks of foreign currency losses due to fluctuations in foreign currency exchange rates. In addition, in the event the Company is successful in doing business outside of the United States, the Company may also face economic, political and foreign currency situations that are substantially more volatile than those commonly experienced in the United States. There can be no assurance that any of these factors will

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not have a material adverse effect on the Company's business, results of operations and financial condition.

Intellectual Property Rights. The Company's success is dependent upon its software code base, its programming methodologies and other intellectual properties. To protect its proprietary technology, the Company relies on a combination of trade secret, nondisclosure and copyright and trademark law which may afford only limited protection. The Company owns United States trademark registrations for certain of its trademarks, including QUICKLINK GOLD, but has not yet obtained registrations for all of its trademarks in the United States or other countries, such as for the mark QUICKLINK II FAX. Until recently, the Company did not require its employees to sign proprietary information and inventions agreements stipulating, among other things, software ownership rights. There can be no assurance that the steps taken by the Company will be adequate to deter misappropriation of its proprietary information, will prevent the successful assertion of an adverse claim to software utilized by the Company or that the Company will be able to detect unauthorized use and take effective steps to enforce its intellectual property rights. In selling its products, the Company relies primarily on "shrink wrap" licenses that are not signed by licensees and, therefore, may be unenforceable under the laws of certain jurisdictions. In addition, the laws of some foreign countries do not protect the Company's proprietary rights to as great an extent as do the laws of the United States. There can be no assurance that the Company's means of protecting its proprietary rights will be adequate or that the Company's competitors will not independently develop similar technology. Further, although the Company believes that its services and products do not infringe on the intellectual property rights of others, there can be no assurance that such a claim will not be asserted against the Company in the future. The failure of the Company to protect its proprietary information could have a material adverse effect on the Company's business, results of operations and financial condition.

From time to time, the Company has received and may receive in the future communications from third parties asserting that the Company's trade name or that features, content, or trademarks of certain of the Company's products infringe upon intellectual property rights held by such third parties. For example, the Company has received correspondence from a third party asserting that the use by the Company of the mark QUICKLINK in the United States and Canada constitutes trademark infringement and unfair competition. The Company believes that it has meritorious defenses to the claims asserted, particularly in light of the length of time the Company has continuously used its QUICKLINK-based marks. While no litigation has been initiated by this party, the Company is attempting to resolve all such assertions. Should there be a successful challenge to the Company's use of the QUICKLINK mark or any other mark, the Company could incur significant expenses in connection with changing the name and experience a loss of goodwill related to its QUICKLINK product line. As the number of trademarks, patents, copyrights and other intellectual property rights in the Company's industry increases, and as the coverage of these patents and rights and the functionality of products in the market further overlap, the Company believes that products based on its technology may increasingly become the subject of infringement claims. Such claims could materially adversely affect the Company, and may also require the Company to obtain one or more licenses from third parties. There can be no assurance that the Company would be able to obtain any such required licenses upon reasonable terms, if at all, and the failure by the Company to obtain such licenses could have a material adverse effect on its business, results of operations and financial condition. In addition, the Company licenses technology on a non-exclusive basis from several companies for inclusion in its products and anticipates that it will continue to do so in the future. The inability of the Company

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to continue to license these technologies or to license other necessary technologies for inclusion in its products, or substantial increases in royalty payments under these third party licenses, could have a material adverse effect on its business, results of operations and financial condition.

Litigation in the software development industry has increasingly been used as a competitive tactic both by established companies seeking to protect their existing position in the market and by emerging companies attempting to gain access to the market. If the Company is forced to defend itself against a claim, whether or not meritorious, the Company could be forced to incur substantial expense and diversion of management attention, and may encounter market confusion and reluctance of customers to purchase the Company's software products.

Concentration of Ownership. As of September 30, 1996, William Smith and Rhonda Smith beneficially own, as community property, approximately 69.6% of the outstanding shares of the Company. William Smith and Rhonda Smith are married to one another and, acting together, will have the ability to elect the Company's directors and determine the outcome of any corporate action requiring stockholder approval, irrespective of how other stockholders of the Company may vote. This concentration of ownership may have the effect of delaying or preventing a change in control of the Company.

Potential Effect of Anti-Takeover Provisions. The Company's Certificate of Incorporation and Bylaws contain provisions that may discourage or prevent certain types of transactions involving an actual or potential change in control of the Company, including transactions in which the stockholders might otherwise receive a premium for their shares over then current market prices, and may limit the ability of the stockholders to approve transactions that they may deem to be in their best interest. In addition, the Board of Directors has the authority to fix the rights and preferences of shares of the Company's Preferred Stock and to issue such shares, which may have the effect of delaying or preventing a change in control of the Company, without action by the Company's stockholders. Certain provisions of Delaware law applicable to the Company, including Section 203 of the Delaware General Corporation Law, could also have the effect of delaying, deferring or preventing a change of control of the Company. It is possible that the provisions in the Company's Certificate of Incorporation and Bylaws, the ability of the Board of Directors to issue the Company's Preferred Stock, and Section 203 of the Delaware General Corporation Law may have the effect of delaying, deferring or preventing a change of control of the Company without further action by the stockholders, may discourage bids for the Company's Common Stock at a premium over the market price of the Common Stock and may adversely affect the market price of the Common Stock and the voting and other rights of the holders of Common Stock.

Possible Volatility of Stock Price. The trading price of the Common Stock is likely to be subject to significant fluctuations in response to variations in quarterly operating results, the gain or loss of significant orders, changes in management, announcements of technological innovations or new products by the Company, its customers or its competitors, legislative or regulatory changes, general trends in the industry and other events or factors. In addition, the stock market has experienced extreme price and volume fluctuations which have particularly affected the market price for many high technology companies similar to Smith Micro, and which have often been unrelated to the operating performance of these companies. These broad market fluctuations may adversely affect the market price of the Company's Common Stock. Further, factors such as announcements of new contracts or product offerings by the Company or its competitors and market conditions for

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stocks similar to that of the Company could have significant impact on the market price of the Common Stock.

Shares Eligible for Future Sale. Sales of substantial amounts of Common Stock in the public market could adversely affect the market price of the Common Stock. At September 30, 1996, the Company had 14,074,700 shares of Common Stock outstanding. Of this amount, the 9,790,000 shares held by William Smith and Rhonda Smith will be available for sale in the public market (subject to the volume and other applicable restrictions of Rule 144) following the expiration of a two year lock-up agreement with the Representatives of the Underwriters of the initial public offering consummated on September 1995. However, this lock-up agreement does not preclude William Smith and Rhonda Smith from selling shares in an underwritten offering meeting certain parameters commencing no sooner than 180 days after September 19, 1995. In February 1996, options covering 2,500 shares of Common Stock became exercisable. In addition, based on options outstanding as of September 30, 1996, in May 1996, options covering an additional 41,950 shares of Common Stock became exercisable; in July 1996, options covering an additional 43,000 shares became exercisable; in September 1996, options covering an additional 2,375 shares will become exercisable; commencing January 1997, options covering an additional 5,061 shares will become exercisable; commencing February 1997, options covering an additional 7,500 shares will become exercisable; and commencing March 1997, options covering an additional 58,606 shares will become exercisable. Thereafter, options covering approximately 14,406 shares will become exercisable each month until approximately March 2001, based on options outstanding as of September 30, 1996, under the Company's 1995 Stock Option/Stock Issuance Plan.

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PART II -- OTHER INFORMATION

ITEM 1. EXHIBITS AND REPORTS ON FORM 8-K

<TABLE>		
<CAPTION>		
EXHIBIT	TITLE	METHOD OF FILING
NO.	-----	-----

<S>		<C>
3.1	Amended and Restated Certificate of Incorporation of the Company	Incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement No. 33-95096
3.2	Amended and Restated Bylaws of the Company.	Incorporated by reference to Exhibit 3.2 to the Registrant's Registration Statement No. 33-95096
4.1	Specimen certificate representing shares of Common Stock of the Company.	Incorporated by reference to Exhibit 4.1 to the Registrant's Registration Statement No. 33-95096
10.1	Form of Indemnification Agreement.	Incorporated by reference to Exhibit 10.1 to the Registrant's Registration Statement No. 33-95096
10.2	1995 Stock Option/Stock Issuance Plan.	Incorporated by reference to Exhibit 10.2 to the Registrant's Registration Statement No. 33-95096
10.3	Form of Notice of Grant of Stock Option under 1995 Stock Option/Stock Issuance Plan.to the Registrant's Registration Statement	Incorporated by reference to Exhibit 10.3 No. 33-95096
10.4	Form of 1995 Stock Option Agreement under 1995 Stock Option /Stock Issuance Plan.	Incorporated by reference to Exhibit 10.4 to the Registrant's Registration Statement No. 33-95096
10.5	Form of 1995 Stock Purchase Agreement under 1995 Stock Issuance Plan.	Incorporated by reference to Exhibit 10.5 to the Registrant's Registration Statement No. 33-95096

</TABLE>

27

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<TABLE>		
<CAPTION>		
EXHIBIT	TITLE	METHOD OF FILING
NO.	-----	-----

<S>		<C>
10.6	Distribution License Agreement dated September 30, 1991, by and between the Company and Crandell Development Corporation.	Incorporated by reference to Exhibit 10.6 to the Registrant's Registration Statement No. 33-95096
10.7	Application Program Interface Retail License Agreement July 28, 1992 by and between the Company and Rockwell International Corporation.	Incorporated by reference to Exhibit 10.7 to the Registrant's Registration Statement No. 33-95096
10.8	Application Program Interface License Agreement July 28, 1992 by and between the Company and Rockwell International Corporation.	Incorporated by reference to Exhibit 10.8 to the Registrant's Registration Statement No. 33-95096
10.9	Rockwell High Speed Interface License Agreement dated June 2, 1994, by and between the Company and Rockwell International Corporation.	Incorporated by reference to Exhibit 10.9 to the Registrant's Registration Statement No. 33-95096
10.10	Letter Agreement dated February 22, 1994, by and between the Company and Rockwell International Corporation.	Incorporated by reference to Exhibit 10.10 to the Registrant's Registration Statement No. 33-95096

10.111	Letter Agreement dated April 22, 1993, by and between the Company and Rockwell International Corporation.	Incorporated by reference to Exhibit 10.11 to the Registrant's Registration Statement No. 33-95096
10.12	Software Distribution Agreement dated May 8, 1995, by and between the Company and International Business Machines Corporation.	Incorporated by reference to Exhibit 10.12 to the Registrant's Registration Statement No. 33-95096
10.13	Office Building Lease, dated June 10,	Incorporated by reference to Exhibit 10.13

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29	<TABLE> <S> <C> 1992, by and between the Company and Developers Venture Capital Corporation.	<C> to the Registrant's Registration Statement No. 33-95096
10.14	Amendment No. 1 To Office Building Lease, dated July 9, 1993, by and between the Company and Pioneer Bank.	Incorporated by reference to Exhibit 10.14 to the Registrant's Registration Statement No. 33-95096
10.15	Amendment No. 2 To Office Building Lease, dated August 15, 1994, by and between the Company and T&C Development.	Incorporated by reference to Exhibit 10.15 to the Registrant's Registration Statement No. 33-95096
10.16	Fourth Addendum to Office Building Lease, dated April 21, 1995, by and between the Company and T&C Development.	Incorporated by reference to Exhibit 10.16 to the Registrant's Registration Statement No. 33-95096
10.17	Form of Promissory Note related to S Corporation Distribution.	Incorporated by reference to Exhibit 10.17 to the Registrant's Registration Statement No. 33-95096
10.18	Smith Micro Software, Inc. Authorized OEM Agreement, dated July 1, 1995, by and between the Company and U.S. Robotics Access Corp.	Incorporated by reference to Exhibit 10.18 to the Registrant's Registration Statement No. 33-95096

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30	<TABLE> <CAPTION> EXHIBIT	
NO.	TITLE	METHOD OF FILING
---	-----	-----
<S>	<C>	<C>
10.19	Office Building Lease, dated March 1, 1994, by and between Performance Computing Incorporated and Petula Associates, Ltd./KC Woodside.	Incorporated by reference to Exhibit 10.19 to the Registrant's Form 10K filled with the Commission on April 1, 1996.
10.20	Agreement and Plan of Merger by and between Smith Micro Software, Inc., Performance Computing Incorporated and PCI Video Products, Inc. dated as of March 14, 1996.	Incorporated by reference to Exhibit 2 to the Registrant's Current Report on Form 8-K filed with the Commission on March 28, 1996
10.21	Smith Micro Software, Inc. Amended and Restated Software Licensing and Distribution Agreement dated April 18, 1996	Filed Herewith (this exhibit is subject to a request for confidential treatment filed with the Securities and Exchange Commission)
21.1	Subsidiaries of Registrant.	Incorporated by reference to Exhibit 21.1 to the Registrant's Form 10K filed with the Commission on April 1, 1996.
27	Financial Data Schedule.	Filed Herewith

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SIGNATURES

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

SMITH MICRO SOFTWARE, INC.

November 13, 1996

By /s/ WILLIAM
W. SMITH, JR.
William W. Smith, Jr.
Chairman, President and Chief
Executive Officer
(Principal Executive Officer)

November 13, 1996

By /s/ ROBERT E. GRICE, JR.
Robert E. Grice, Jr.
Chief Financial Officer
(Principal Financial Officer)

SMITH MICRO SOFTWARE, INC.

AMENDED AND RESTATED SOFTWARE LICENSING AND DISTRIBUTION AGREEMENT

THIS AMENDED AND RESTATED SOFTWARE LICENSING AND DISTRIBUTION AGREEMENT, including Appendices A, B, and C attached hereto (hereinafter the "Agreement"), is made this 18 day of April, 1996 and amends and restates the Software Licensing and Distribution Agreement dated March 20, 1996, which date also shall be the effective date of this agreement (the "Effective Date"), by and between SMITH MICRO SOFTWARE, INC., a corporation organized and existing under the laws of the State of Delaware (hereinafter referred to as "SMSI"), and U.S. Robotics Access Corp., a corporation organized and existing under the laws of the State of Delaware. This Agreement shall apply solely to the Personal Communications Division, which hereinafter shall be referred to as "USR".

1. Termination of Prior Agreement.

The parties hereto hereby terminate the Authorized OEM Agreement between the parties dated July 1, 1995. The new pricing in Appendix A shall take effect as of the Effective Date of this Agreement. The parties further agree that this termination shall not obligate USR to comply with Paragraph 6.3 of the Authorized OEM Agreement. This Agreement also supersedes the Software licensing and distribution Agreement dated March 20th, 1996.

2. Rights and Licenses Granted to USR, Services, Term.

2.1 SMSI publishes the software programs listed in Appendix "A" and documentation and instruction manuals related to the software programs (the "Licensed Products"). SMSI hereby grants USR a non-exclusive, non-transferable right to market, distribute and sublicense the Licensed Products to distributors, re-sellers, OEM customers of USR and end users, solely in conjunction with the sale of modems of USR, and not as separate, unbundled products. SMSI shall have exclusive rights to duplicate floppy diskettes for one year for the Licensed Products in Appendix A. The term of this Agreement shall be one (1) year from the date hereof, and shall renew automatically for additional one year periods unless either party gives the other party written notice of cancellation at least sixty (60) days prior to the end of the then current term. In addition, USR may terminate this Agreement - and any USR division or entity executing an addendum hereto may terminate that addendum - in its entirety or with respect to any one or more Licensed Products, at any time for any reason upon ninety (90) days written notice.

3. Obligations.

3.1 USR's Obligations with Respect to Sales and Support. USR shall license Fax Data/Voice and Telephony software for all modem products that are currently shipping with SMSI products, sold under the USR name, from SMSI on a non-exclusive basis. For each modem model that currently ships with SMSI software, USR shall include a copy of the Licensed Products with each modem shipped during the term of this agreement. The Licensed Product shall be subject to the end user license agreement provided by SMSI. USR may include the promotional literature (either in electronic or hard copy form), furnished by SMSI with respect to other products of SMSI including products which provide enhancement upgrades to the Licensed Products. Such promotional material shall be subject to approval by USR, which approval shall not be unreasonably withheld. USR shall promote the fact that the Licensed Products are included with modems shipped by including references to SMSI and the Licensed Products on modem product packaging, advertising and promotional literature. USR shall provide technical support in the operation of the Licensed Products to its distributors, re-sellers, OEM customers, end users and others to whom USR provides the Licensed Products. In the event USR changes the design of any modem product with which it ships the Licensed Products, USR shall promptly supply a sample of such modem, as changed, to SMSI at no charge. If the changes are only in firmware, then the new firmware will be forwarded to SMSI promptly at no charge. Should such design changes require software modifications, SMSI reserves the right to charge USR for the reasonable costs of such changes. These engineering fees will

not be charged for software updates that SMSI and USR mutually agree are required to accommodate the natural progression

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of hardware features in the industry. The fees for these design changes and other Engineering modifications requested of SMSI are outlined in Appendix B of this document. USR shall establish a registration procedure by which end users of its modems may register ownership. USR shall provide this registration information to SMSI every 8 weeks in ASCII or DBF, Machine readable format.

3.2 SMSI's Obligations.

SMSI shall use its commercially reasonable efforts to assure that the Licensed Products are compatible with the modems of USR. SMSI shall provide technical support in the operation of the Licensed Products to the customer service staffs of USR to assist the customer service staffs in supporting the Licensed Products but SMSI shall not be otherwise obligated to provide technical support. USR agrees to reimburse SMSI for reasonable travel expenses incurred to provide such training. These travel expenses shall not be charged for new product introductions or sales efforts of any kind by the SMSI staff. At SMSI's request, USR shall place the SMSI retail products and commercials for such products on the USR Compact Disk ("CD"), (commercials for the retail products shall not exceed 10 Megabytes) for the purpose of upgrading customers to the SMSI retail products. SMSI will pay USR *** of the gross sales revenues attributable to upgrades directly generated by sales off the USR CD.

4. Delivery.

SMSI shall deliver Licensed Products to USR on acceptance of purchase orders, subject to the normal processing schedules of SMSI. USR shall include a copy of SMSI's End-User License Agreement with the Licensed Products. SMSI shall maintain the capability to produce the Licensed Products outside California in the event it is unable to produce the Licensed Products in California as a result of a natural disaster.

5. Payment Schedule, Fees and Charges.

5.1 Price. USR shall pay royalties for the Licensed Products according to the prices specified in Appendix A hereto. USR may order all or any of the Licensed Products in its sole discretion. Appendix A also includes a list of Licensed Products Components. USR has the right to purchase all or any of the Licensed Products Components in Appendix A, in its sole discretion, for which USR shall pay the prices set forth in Appendix A.

6. Copies of Licensed Products.

Except as provided herein solely for technical support purposes, USR shall not have the right to copy, duplicate or otherwise reproduce the Licensed Products or any component part of the Licensed Products.

7. Termination.

7.1 Default. Each party has the right to terminate this Agreement on forty-five (45) days prior notice in writing to the other party for the following reasons or causes:

7.1.1 If such other party materially breaches or is in material default of any obligation hereunder, which breach or default is incapable of cure or, which, being capable of cure, has not been cured within forty-five (45) days (or ten (10) days in case of non-payment), after service of written notice of default of the non-breaching party;

7.1.2 If such other party becomes insolvent, is adjudicated bankrupt or if a receiver or trustee is appointed for such party for a substantial portion of its assets, or if such party institutes or becomes a party to any proceeding for the settlement of debts or an assignment for the benefit of creditors of such party, and the situation is not corrected within thirty (30) days after it received written notice from the non-breaching party. If this situation occurs, USR has the right to continue shipping the Licensed Products.

7.2 Force Majeure, Suspension and Termination. In the event that either USR or SMSI is unable to perform any of its obligations under this

Agreement or to enjoy any of its benefits because of natural disaster, actions or decrees of governmental

*** Confidential portion has been filed separately with the Securities and Exchange Commission

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bodies or communications line failure not the fault of such party (hereinafter referred to as a "Force Majeure Event"), such party immediately shall give notice to the other and shall do everything possible to resume performance. Upon receipt of such notice, this Agreement shall immediately be suspended. If the period of nonperformance exceeds sixty (60) days from the receipt of notice of the Force Majeure Event, the other party may, by giving written notice, terminate this Agreement. However, delays in delivery due to Force Majeure Events shall automatically extend the delivery date for a period equal to the duration of such events; any warranty period affected by a Force Majeure Event shall likewise be extended for a period equal to the duration of such event.

7.3 Conditions Upon Termination. The following conditions shall apply upon termination:

7.3.1 USR shall erase or destroy all master copies or copies or portions thereof contained or stored in any form or media, including the memory of a computer or computer system in its possession or under its control, provided however USR may sublicense all Licensed Products then existing in OEM's inventory subject to the terms and conditions of this Agreement.

7.3.2 USR shall certify to SMSI that the requirements of Section 7.3.1 have been completed within fifteen (15) days of termination.

7.4 Addition to Other Rights. The termination rights set forth above shall be in addition to, and not in substitution for, any other remedies that may be available to the party serving notice upon the other party, and any termination and any exercise of any such right shall not relieve the party receiving notice from any obligations accrued to the date of such termination or relieve such from liability and damage to the other for breach of this Agreement. No termination hereunder shall terminate any end user license.

7.5 Survival. The obligations of the parties under Sections 7, 8, 9, and 10 shall survive termination of any license hereunder.

7.6 Notwithstanding any other provision of this Section 7 to the contrary, USR shall be entitled to retain, for a period of five (5) years following the termination of this Agreement, such copies of the Licensed Products as may be reasonably required for the use of USR's customer support personnel in connection with providing ongoing support to USR's customers who are end users of the Licensed Products. Further, the termination of this Agreement shall not in any way affect USR's rights under end-user licenses for the Licensed Products heretofore or hereafter acquired by USR otherwise than pursuant to this Agreement.

8. Warranties.

8.1 SMSI's Warranties. SMSI warrants that during the Warranty Period (as defined below), the Licensed Products furnished hereunder shall be free from significant programming errors and from any defect in workmanship and materials which would cause such Licensed Products to be not merchantable. This warranty shall be of no effect should USR cause the Licensed Products to be modified without the written consent of SMSI.

8.2 SMSI's Fulfillment of Warranty Obligations. If at any time during the 90-day period immediately following the date on which any Licensed Product is first shipped to USR (the "Warranty Period") SMSI or USR shall discover one or more defects or errors in the Licensed Products or any other respect in which the Licensed Products fails to conform to the provisions of any warranty contained in this Agreement, SMSI shall, entirely at its own expense, promptly correct such defect, error or nonconformity by, among other things, supplying USR with corrected versions of the Licensed Products.

8.3 No Warranty Pass-Through. USR shall not pass through to its customers, end users or any other third party the warranties made by SMSI under this Agreement. USR shall make no representations to its customers, end users or

any other third party on behalf of SMSI. No warranty, representation or agreement herein shall be deemed to be made for the benefit of any customer, end user, or licensee of USR or any other third party.

8.4 LIMITATION OF LIABILITY. THE FOREGOING WARRANTIES ARE IN LIEU OF ALL OTHER WARRANTIES, EXPRESS OR IMPLIED, INCLUDING, BUT NOT LIMITED TO, THE IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE.

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CONSEQUENTIAL DAMAGES. IN NO EVENT SHALL EITHER OF THE PARTIES HERETO BE LIABLE TO THE OTHER FOR THE PAYMENT OF ANY INDIRECT, SPECIAL OR CONSEQUENTIAL DAMAGES, INCLUDING LOSS OF PROFITS, REVENUE, DATA, OR USE, INCURRED BY EITHER PARTY OR ANY THIRD PARTY, WHETHER IN AN ACTION IN CONTRACT OR TORT OR BASED ON A WARRANTY, EVEN IF THE OTHER PARTY OR ANY OTHER PERSON HAS BEEN ADVISED OF THE POSSIBILITY OF SUCH DAMAGES. THE REMEDIES PROVIDED FOR HEREIN EMBODY THE ESSENTIAL PURPOSE OF THE PARTIES HERETO WITH RESPECT TO REMEDIAL ACTION IN THE EVENT OF BREACH OF THIS AGREEMENT.

8.5 USR's Warranties with respect to software provided for inclusion in Compact Disc products. USR warrants that it owns or has the right to use, as contemplated herein, all items delivered to SMSI by or for USR for use in connection with the production, printing, and/or packaging of Compact Discs hereunder, including without limitation, Third Party Software, master media, art work and packaging (hereinafter referred to as the "Materials") and has the right to deliver all materials to SMSI and to have the Materials reproduced as provided herein. USR also warrants that it owns or has the right to use all copyrights in the contents of materials (including without limitation any computer code embedded therein) and has the unrestricted right to permit SMSI to perform the services hereunder. USR further warrants that the text, images, audio and other data or in the Materials will not infringe any intellectual property or personal right held by any party.

8.6 Indemnification

8.6.1 SMSI agrees to defend USR from any claims, suit or proceeding alleging that the Licensed Products infringe any third party United States or foreign patent, trademark, trade name or copyright or claimed infringement or misappropriation of intellectual rights, and to pay any liabilities, damages, costs and expenses (including the actual fees of attorneys and other professionals and all related costs and expenses) finally awarded in any such claim, suit or proceeding.

8.6.2 The indemnifying party shall be relieved of the foregoing obligation unless (i) the other party promptly notifies the indemnifying party of any such claim, (ii) the indemnifying party shall have sole control of the defense and all related settlement negotiations, and (iii) the other party provides the indemnifying party with the assistance, information and authority necessary to perform the above. However, if the other party desires to have separate legal representation in any such action, it shall be responsible for the costs and fees related to its separate counsel. In the event the Licensed Products or software provided by USR are finally held or believed by the indemnifying party to infringe a third party's rights, the indemnifying party shall use reasonable efforts to obtain a license under the rights that have been infringed, to modify the infringing product so they are noninfringing or to provide to the other party substitute products that are noninfringing; provided that if in the indemnifying party's judgment such options are not commercially reasonable, the indemnifying party may terminate the licenses granted hereunder upon written notice to the other party. SMSI shall have no liability for infringement based on (a) use of other than the current release of the Licensed Products, (b) modification of the Licensed Products by any party other than SMSI, or (c) the combination or use of the Licensed Products with any other software, equipment, product, device, item or process not furnished by SMSI or not contemplated under this Agreement, if such infringement would have been avoided by the use of the Licensed Products as contemplated herein or alone and in their current unmodified form. THE INDEMNIFICATION OBLIGATIONS HEREUNDER ARE IN LIEU OF ANY EXPRESS OR IMPLIED WARRANTIES OF NON-INFRINGEMENT WHICH ARE HEREBY DISCLAIMED.

9. Proprietary Information, Publicity.

9.1 USR agrees that the Licensed Products provided hereunder, and any copies thereof, in whole or in part, and all intellectual property rights, including without limitation, patent, copyrights, trademark, trade secret, and

any other intellectual or industrial property rights, are and shall remain the sole property of SMSI, and that all rights thereto are reserved by SMSI. USR agrees that it will not create derivatives of such Licensed Products, nor use, copy, disclose, sell, assign, sublicense, or otherwise transfer the Licensed Products except as expressly provided in this Agreement. USR is prohibited from the disassembly or decompilation of the object code without the written consent of SMSI. the copyright to the Licensed Products shall remain the sole property of SMSI, which reserves all rights thereto, and nothing contained herein, shall be construed to compromise such ownership right. USR shall not remove any copyright notices on Licensed Products' diskette labels or end user documentation. USR shall only refer to the Licensed Products using the names set forth in Appendix A attached hereto, and by no other name. USR shall restrict its sub-licensees of the Licensed Products similarly.

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9.2 Each party acknowledges that all information (a) concerning the existence of or terms and conditions of this Agreement, or (b) disclosed by the other party and designated as confidential is "Confidential and Proprietary Information." Each party agrees that it will not permit the duplication, use or disclosure of any such Confidential and Proprietary information to any person (other than its own employees and representatives who are informed of the confidential nature of the information and who have executed appropriate non disclosure agreements), unless authorized in writing by the other party. "Confidential and Proprietary Information" is not meant to include any information which, at the time of disclosure, is generally known by the public and any competitors of either party.

9.3 SMSI shall not issue any press release or other public notice relating to this Agreement without the written consent of USR, which shall not be unreasonably withheld. Each party hereby grants to the other party the right to use the granting party's trademark(s), trade name(s) and product name(s) in conjunction with authorized advertising, press releases or other marketing-related activities.

10. Miscellaneous.

10.1 Applicable Law. This Agreement shall be governed by the laws of the State of California applicable to agreements made and to be performed in California including such state's Uniform Commercial Code, except that if any provision of the Agreement shall be inconsistent therewith, the terms of this Agreement shall prevail. Venue for any such action shall be in Cook County, Illinois.

10.2 Notices. Any notice or other communication hereunder shall be in writing and deemed given if personally delivered or sent to a party by commercial overnight delivery or registered or certified mail, return receipt requested or, first class mail to the following addresses:

To SMSI:
Smith Micro Software, Inc.
51 Columbia
Aliso Viejo, CA 92656
Attn: Mr. Robert Caggiano
Telephone (714) 362-5800
Fax (714) 362-2300

To USR:
U.S. Robotics Access Corp.
7770 North Frontage Rd.
Skokie, IL 60077
Attn: Mr. Rob Thomsen
Telephone (708) 676-7010
Fax (708) 676-7320

with a copy to:

U.S. Robotics Access Corp.
Legal Department
8100 N. McCormick Blvd.
Skokie, IL 60076
Telephone (708) 933-5830
Fax (708) 933-5149

Notices delivered personally, by overnight delivery or by registered or certified mail shall be deemed communicated as of actual receipt; notices sent by first class mail shall be deemed communicated as three (3) business days after mailing. Each party may change such party's address by written notice in accordance with this section.

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10.3 Independent Contractors. The parties are not employees or legal representatives of the other party for any purpose. Neither party shall have the authority to enter into any contracts in the name of or on behalf of the other party.

10.4 Waiver. No term or provision hereof shall be deemed waived and no breach excused unless such waiver or consent shall be in writing and signed by the party claimed to have waived or consented.

10.5 Assignment. Neither party shall assign or subcontract all or any part of this Agreement, or any interest therein, without the other party's prior written consent, except that USR may assign to any corporate affiliate without SMSI's consent.

10.6 Binding Effects; Benefits. This Agreement shall inure to the benefit of, and shall be binding upon, the parties hereto and their respective successors and assigns. Nothing herein is intended to confer on any person other than the parties hereto or their respective successors and assigns any rights, remedies, obligations or liabilities under, or by reason of, this Agreement.

10.7 Attorney's Fees. In the event of any controversy, claim or dispute between the parties hereto arising out of or relating to this Agreement, the prevailing party shall be entitled to recover from the non-prevailing party its reasonable expenses including, but not by way of limitation, attorney's fees.

10.8 Severability. If any of the provisions of this Agreement shall be declared void by a court of competent jurisdiction, such provisions shall be severable and independent from the other provisions of this Agreement, and the validity of the other provisions and of the entire Agreement shall not be affected thereby.

10.9 Captions; Headings. The headings of articles, sections and other subdivisions hereof are inserted only for the purpose of convenient reference and it is recognized that they may not adequately or accurately describe the contents of the sections which they head. Such headings shall not be deemed to govern, limit, modify, or in any other manner affect the scope, meaning or intent of the provisions of this Agreement or any part or portion thereof, nor shall they otherwise be given any legal effect.

10.10 Entire Agreement.

This Agreement, together with all appendices or other attachments referenced herein, constitutes the entire agreement between SMSI and OEM and supersedes all proposals, oral and written, between the parties on this subject.

10.11 Counterparts. This Agreement may be executed in counterparts, which together shall constitute the contract of the parties.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed and each hereby warrants and represents that the persons signing on its behalf has been and is on the date of this Agreement duly authorized by all necessary and appropriate corporate action to execute this Agreement.

SMITH MICRO SOFTWARE, INC.

By: /s/ WILLIAM W. SMITH, JR.

Title: President/CEO Date: 4/18/96

U.S. ROBOTICS ACCESS CORP.

By: /s/ MICHAEL SEEDMAN

Title: V.P., G.M Date: 6/19/96

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APPENDIX A

SMSI and U.S. Robotics Access Corp. Agreement

1. a. Domestic Licensed Products:

1. QuickLink II FAX and DATA for Windows/DOS or Windows
2. QuickLink MessageCenter FAX/DATA/Voice/Telephony for Windows
3. MacComCenter
4. Private Label OEM Software for FAX and DATA for Windows and/or Windows 95
5. Private Label OEM Software for FAX/DATA/VOICE/TELEPHONY for Windows and/or Windows 95
6. MacComCenter With Voice Module

NOTE: Private Label OEM Software name will be determined by USR. This software will be a derivative of the HotFax and HotFax MessageCenter code base. The feature is outlined in Appendix C, and is mutually agreed on by USR and SMSI in order to maximize upgrades to the HotFax and HotFax MessageCenter software on the CD and in order to reduce the number of disks for the OEM Kitted solution.

b. All Freight will be F.O.B. SMSI.

c. Payment terms: Net 30 from date of shipment to USR or acting agent.

PRICING FOR LICENSED PRODUCT COMPONENTS (PER UNIT BASIS):

PRODUCT COMPONENTS	PRICE
QuickStart Guide and Brochure for MacComCenter, MessageCenter, QuickLink II Win/DOS, Private Label OEM Software for FAX/DATA/VOICE/TELEPHONY and FAX/DATA	***
MacComCenter Manual	***
MessageCenter II Manual	***
QuickLink II Manual	***
Duplicated 3.5" Disk with label	***
Shrink Wrap	***

*** Confidential portion has been filed separately with the Securities and Exchange Commission

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ROYALTIES ON LICENSED PRODUCTS (PER UNIT BASIS):

LICENSED PRODUCTS ROYALTY	PRICE
QuickLink II Win/DOS Royalty	***
QuickLink MessageCenter Royalty	***
MacComCenter Royalty	***

Private Label OEM Software for FAX/DATA for ***
Windows and/or Windows 95

Private Label OEM Software for ***
FAX/DATA/VOICE/TELEPHONY Windows and/or
Windows 95

MacComCenter Voice module-Additional Royalty ***

*** Confidential portion has been filed separately with the Securities and
Exchange Commission

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APPENDIX B

ENGINEERING FEES

Reasonable engineering fees will be charged for custom projects requested by
USR. The format for creating the charge for these engineering fees will be as
follows:

1. USR creates statement of work.
2. SMSI responds to statement of work with outline of project including an
estimate of hours.
3. USR signs off on estimate of hours. Fees will not be less than *** of
hourly estimate or more than *** of hourly estimate. If USR requires
changes to the specifications after work has begun, these changes will
be priced separately according to the same method outlined above.
4. SMSI bills USR for project at *** per hour. 50% due at start of
project, 50% due upon sign off of Master Release Authorization Form
First Customer Ship of completed product.

*** Confidential portion has been filed separately with the Securities and
Exchange Commission

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APPENDIX C

The below specification is for the WIN/Win95 version of licensed product. This
fax/data and fax/data/voice/speakerphone product is based on HotFax and HotFax
Message Center code base. This list of features is only a starting point that
both parties agree upon. New features will be added to private label OEM
version as mutually agreed upon by both parties.

<TABLE>		OEM	RETAIL
<CAPTION>		<C>	<C>
GENERAL	<S>		
Location Setup	<C> Tells the program where you are in the world, based on install.	X	X
Advanced Location	Define Toll calling, Custom Area Code dialing etc.	X	X
Look and Feel	Makes Win 16 apps look like Win95 apps	X	X
Look and Feel Setup	Win 16 only	X	X
Auto-Bridge	Reads Quicklink setup information, imports HotLine and WinFax database	X	X
Mobile Features	(Retail and QL Mobile) simple Mobile vs. Land Line switch	X	X
Caller ID	Shows you who called and log it (tbd)	X	X
Distinctive Ring	Configure up to 4 different answer types for 1 phone line	X	X

Hot-Keys	Run specific features via user defined Hot-Key		X
Notification	Option to set notification of incoming fax, data, or voice call	X	X
MAPI	Supports MAPI when available	X	X
Un-Install	Un-Install Software	X	X
Wireless and Cellular	Wireless and Cellular Compatible	X	X
Install Software			
Auto Detect	Automatically detects the modem type, chipset identification, COM port	X	X
Manual Detect	Manually set modem type, COM port, and user definable modem and initialization strings	X	X
Win32-			
TAPI	Use registered TAPI modems	X	X
32 bit multithreading	Smooth multitasking for faxing, and downloading	X	X
NT support	Supports NT 3.51 (most features)	X	X
Long filenames	Filenames up to 256 characters	X	X
Plug and Play	Run HotFax when you insert your modem		X
Adds to Office Shortcut Bar	Installer adds HotFax to your Office 95 Taskbar	X	X
Use Exchange Phonebook	Open the exchange phonebook within HotFax for Data and Fax calls	X	X
OLE	Supports OLE	X	X
Attachments - on the fly (Fax Binder)	OLE Container allowing you to easily group documents together for faxing		X
OCR			
OCR to RTF or Text	OCR any Fax or image file		X
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11			
<TABLE>			
<S>	<C>	<C>	<C>
OCR Multiple files	Queue up a list of faxes to OCR		X
Auto OCR on receive	OCR to In-box upon fax receive		X
OCR Setup	Advanced features (Auto Page segmentation, etc.)		X
TERMINAL			
Scroll-back buffer	User definable size	X	X
Font Selection	Choose your own Terminal font for each connection	X	X
Terminal Emulstors	TTY ANSI VT52 VT100 VT102 VT220 3270	X	X
Function Bar	20 definable buttons/hot-keys for Macros, Script Launching and program execution	X	X
Printing	Print your screen or terminal buffer	X	X
Chat Mode	Easy chat with single click file transfer	X	X
Scripting	Basic like language with 113 verbs	X	X
Host Mode	Simple BBS like features	X	X
File Transfers	Xmodem (CRC/lk) Ymodem, Ymodem batch Zmodem Kermit SuperKermit ASCII	X	X
File Transfer Setup	General and ASCII	X	X
Adv. File Transfer Setup	Change setting for Xmodem-Zmodem & Kermit/ SuperKermit		X
Email support	Email (via MAPI) your screen or scroll-back buffer	X	X
Learn Mode	Automatically writes login scripts for you		X
LOG MANAGER			
In place editing	Reschedule faxes by in-place editing the time to send	X	X
Printing	Print the contents of your folder (receive log/send	X	X

	log)			
Column sorting	Sort your folder by clicking on the column heading	X		
Archiving Messages	Archive/Move your messages into any folder	X	X	
Nested Folders	Create as many folders for fax and voice messages as you want	X	X	
Archiving in ZIP format	Folders can ZIP your contents into a standard ZIP file	X	X	
Message Find	Find messages in any folder	X	X	
Auto Maintenance	Folders can automatically move and archive messages on particular days of the month	X	X	
Email support	Email your faxes and voice messages via MAPI	X	X	
Configure Fields	Configure which columns display on your folder		X	
Fax Host	Send and Retrieve your faxes from a remote location		X	
FAX				
Supports all popular fax cards	Class 1. Class 2. Class 2.0 and MWave	X	X	
PhoneBook	Name, Company, fax number, and voice number	X	X	
Import/Export	Import/Export phonebook information from ACII tab delimited text	X	X	
Group Fax	Send to a group list	X	X	
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12				
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	<C>		<C>	<C>
Print Faxes on receive (AutoPrint)	Simulates a plain paper fax machine	X	X	
Fax Preview	Preview a fax before you send it	X	X	
Attach any document	Attach feature allows you to pick any file in your system to fax	X	X	
Cover Pages Selection	Select for 3 different Cover Page designs Include an option to have up to 10 different cover pages at any time.	X	X	
Cover Page Import/Export	Import or export up to 10 different cover pages	X	X	
View faxes on receive	Option to load the new fax into viewer when you receive it	X	X	
More Cover Pages	40 Professional Cover Pages		X	
Fax Forwarding	Forward your faxes to a particular number	X	X	
Auto Fax Forward	Set auto fax forward from local or remote locations		X	
HotFax Menu	Integrated HotFax Menu allows one click faxing from any Windows application		X	
Header Setup	Enter customized fax header	X	X	
Drag and Drop Faxing	Easy shortcut to the fax driver on your Win95 desktop	X	X	
VIEWER				
Fax Preview	Preview your fax before you send it	X	X	
File Support	.QFX .REC .HFX .BMP .PCX .DCX .TIF	X	X	
Gray-scale support	Image enhancing to make your faxes more readable on-screen	X	X	

Scan New Faxes	With one click, view all your new faxes (Voice product only)	X	X
Show all pages	Show a thumbnail view of all the pages in a fax		X
Advanced Imaging Options	Rotate image any angle, Image Skew, and Dithering support		X
Annotation	Mark up and re-send a fax		X
Stamps	Makes it easy to lay in a signature block		X
Advanced File Support	.GIF .WPG .TGA .WMF PICT and JPEG		X
Cover Page Designer Design your own Cover Page	Choose from a pallet of tools to text and image design		X
Design your own Header	Create a header just like you create a cover page		X
VOICE			
Voice Answering Machine	Configure up to 10 mailboxes	X	X
Fax-On-Demand	Add up to 10 documents per mailbox	X	X
Fax-On-Demand	Add up to 100 documents per mailbox		X
Call Transfer	Transfer a call from a mailbox to another phone number	X	X
Urgent Paging	Page to numeric or Alpha numeric pager	X	X
Speakerphone	With supporting hardware	X	X
Sound Card Support	Play your voice messages through your sound card	X	X
Music On Hold	Play a MIDI file while the user is on hold	X	X
Redial Last	Redial last number dialed	X	X
10,000 Mailboxes	Almost unlimited number of voice mailboxes		X

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13

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COVER PAGE DESIGNER

Design your own Cover Page	Choose from a pallet of tools to text and image design		X
Design your own Header	Create a header just like you create a cover page		X

PAGING

Outbound Paging	Windows 95 support only		X
Page on Email receive	Win95 only		X

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