

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

## FORM 10-QSB

(Mark One)

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

For the quarterly period ended: March 31, 1998

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 000-21898

## INTERACTIVE INC.

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

South Dakota 46-0408024

(state of incorporation) (IRS Employer ID No)

204 N. Main, Humboldt, SD 57035

(Address of principal executive offices)

(605) 363-5117

Issuer's telephone number

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

Yes . . . No .X. .

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY  
PROCEEDINGS DURING THE PRECEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court. Yes . . . No . . .

## APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:

3,265,976 shares at March 31, 1998

Transitional Small Business Disclosure Format (Check one): Yes No x

## PART 1. FINANCIAL INFORMATION

## Item 1. Financial Statements (unaudited)

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INTERACTIVE INC.  
BALANCE SHEET  
March 31, 1998  
(Unaudited)

## ASSETS

## CURRENT ASSETS

		9/30/97
Cash	\$ 1,121	\$ 1,165
Accounts Receivable	5,422	10,418
Inventories	20,078	21,713
Prepaid expenses and other	4,192	800
	<hr/>	<hr/>
Total current assets	\$ 30,813	\$ 34,096

## PROPERTY AND EQUIPMENT, at cost

Land	\$ 1,962	\$ 1,962
Building and improvements	84,962	84,962
Computer and office equipment	54,246	54,246
	<hr/>	<hr/>
	\$ 141,170	\$ 141,170
Less accumulated depreciation	84,532	77,032
	<hr/>	<hr/>
	\$ 56,639	\$ 64,138

## OTHER ASSETS

Cost	\$ 253,971	\$ 253,971
Less accumulated amortization	246,183	244,526
	<hr/>	<hr/>
	\$ 7,788	\$ 9,445

## Total assets

	<hr/>	<hr/>
	\$ 95,240	\$ 107,679
	<hr/>	<hr/>

## LIABILITIES AND STOCKHOLDERS' EQUITY

## CURRENT LIABILITIES

Notes payable, bank	\$ 213,500	\$ 213,500
Notes payable, related party	545,000	545,000
Current maturities of long-term debt	265,436	265,436
Accounts payable, trade	1,129,365	1,119,092
Accounts payable, trade, Torrey Pines Research	296,297	296,297
Accrued expenses	248,009	244,526
	<hr/>	<hr/>
Total current liabilities	\$ 2,697,607	\$ 2,683,851

## LONG-TERM DEBT

	\$ 265,436	\$ 265,436
Less current maturities	(265,436)	(265,436)
	<hr/>	<hr/>
	\$ 0	\$ 0

## STOCKHOLDERS' EQUITY

Series A preferred stock, par value \$.001 per share; authorized 5,000,000 shares; issued 113,901 shares	\$ 114	\$ 114
Common stock, par value \$.001 per share; authorized 10,000,000 shares; issued 3,265,976	3,266	3,191
Additional paid-in capital	6,834,594	6,834,594
Accumulated deficit	(9,440,341)	(9,414,071)
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Total stockholders' equity	\$ (2,602,367)	\$(2,576,172)
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## Total liabilities and stockholders' equity

	<hr/>	<hr/>
	\$ 95,240	\$ 107,679
	<hr/>	<hr/>

INTERACTIVE INC.  
 STATEMENTS OF OPERATIONS  
 Six and Three Months Ended March 31, 1998 and 1997  
 (Unaudited)

	Six months ended March 31,		Three months ended March 31,	
	1998	1997	1998	1997
Net Sales	\$ 39,777	\$ 42,441	\$ 28,504	\$ 13,719
Cost of goods sold, exclusive of depreciation and amortization shown separately below	19,591	19,623	14,587	6,523
Gross profit	<u>\$ 20,186</u>	<u>\$ 22,818</u>	<u>\$ 13,916</u>	<u>\$ 7,196</u>
Operating expenses				
Marketing	\$ 27,811	\$ 40,365	\$ 16,616	\$ 20,950
Support and Production	1,564	2,841	1,183	1,134
General and administrative	5,884	7,380	4,264	3,404
Depreciation and amortization	9,156	51,909	4,578	25,954
	<u>\$ 44,415</u>	<u>\$ 102,495</u>	<u>\$ 26,641</u>	<u>\$ 51,442</u>
Operating Loss	<u>\$ (31,629)</u>	<u>\$ (79,677)</u>	<u>\$ (20,124)</u>	<u>\$ (44,246)</u>
Nonoperating income (expense):				
Rental income	\$ 468	\$ 2,725	\$ 239	\$ 625
Interest expense	(20,745)	(20,050)	(10,504)	(10,007)
Miscellaneous income	25,634	636	21,639	0
Nonoperating income (expense)	<u>\$ 5,357</u>	<u>\$ (16,689)</u>	<u>\$ 11,374</u>	<u>\$ (9,382)</u>
Net loss	<u>\$ (26,272)</u>	<u>\$ (96,366)</u>	<u>\$ (8,750)</u>	<u>\$ (53,628)</u>
Loss per common and common equivalent share	<u>\$ (0.01)</u>	<u>\$ (0.03)</u>	<u>\$ 0.00</u>	<u>\$ (0.02)</u>

See Notes to Financial Statements

INTERACTIVE INC.  
 STATEMENT OF STOCKHOLDERS' EQUITY  
 Six Months Ended March 31, 1998  
 (Unaudited)

	Capital Stock Issued		Additional Paid-in	Accumulated
	Preferred	Common	Capital	Deficit
Balance September 30, 1997	\$ 114	\$ 3,191	\$ 6,834,594	\$(9,414,070)
Issuance of common stock for services		75		
Net loss				(26,272)
Balance March 31, 1998	\$ 114	\$ 3,266	\$ 6,834,594	\$(9,440,342)

See Notes to Financial Statements.

INTERACTIVE INC.  
STATEMENTS OF CASH FLOWS  
Six Months Ended March 31, 1998 and 1997  
(Unaudited)

	Six months ended March 31,	
	1998	1997
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>		
Net loss	\$ (26,271)	\$ (96,365)
Adjustments to reconcile net loss to net cash (used in) operating activities:		
Depreciation and amortization	9,156	51,909
Issuance of common stock for services	75	5,528
Decrease in accounts receivable	4,996	13,331
Decrease in inventories	1,635	10,743
(Increase) in prepaid expenses and others	(3,392)	(341)
Increase (decrease) in accounts payable	10,273	(2,509)
Increase in accrued expenses	3,483	22,417
Net cash (used in) operating activities	\$ (45)	\$ 4,713
<b>CASH FLOW FROM FINANCING ACTIVITIES</b>		
Principal payments on long term debt	\$ 0	\$ (4,428)
Net cash provided by (used in) financing activities	\$ 0	\$ (4,428)
Net increase (decrease) in cash and cash equivalents	\$ (45)	\$ 285
<b>CASH AND CASH EQUIVALENTS</b>		
Beginning	\$ 1,165	\$ 1,034
Ending	\$ 1,120	\$ 1,319
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Cash payments for interest	\$ 0	\$ 105

See Notes to Financial Statements.

## INTERACTIVE INC.

NOTES TO FINANCIAL STATEMENTS  
(Unaudited)

## Note 1. Interim Financial Statements

The financial information presented has been prepared from the books and records without audit but, in the opinion of management, includes all adjustments, consisting of only normal recurring adjustments, necessary for a fair presentation of the financial information for the periods presented. The results of operations for the six months ended March 31, 1998, are not necessarily indicative of the results expected for the entire year.

## Note 2. Income Taxes

The Company adopted the Financial Accounting Standards Board Statement No. 109, Accounting for Income Taxes on October 1, 1993. Statement 109 requires that deferred taxes be recorded on a liability method and adjusted when new tax rates are enacted. There was no effect to the Company's financial statements as a result of adopting Statement 109.

At March 31, 1998, the Company had a net operating loss carryforward for tax purposes of approximately \$8,126,853. For financial reporting purposes, the operating loss carryforward is approximately \$9,440,791, which represents the amount of future tax deductions for which a tax benefit has not been recognized in the financial statements. No deferred asset has been recorded for the benefit of the net operating loss or any other temporary differences as the related valuation allowance would be equal to the net deferred tax asset.

## Note 3. Loss Per Common and Common Equivalent Share

The loss per common and common equivalent share has been computed using the weighted average of the number of shares outstanding for the six and three months ended March 31, 1998 and 1997. The weighted number of common and common equivalent shares outstanding for the six and three months ended March 31, 1998 and 1997 are 3,174,641, 3,117,131, 3,156,291 and 3,123,109 respectively. The loss per common and common equivalent share assuming full dilution is the same as the loss per common and common equivalent share since the convertible preferred stock, convertible notes and common stock options and warrants have not been included in the computation as their inclusion would be anti-dilutive.

## Note 4. Stock Options and Warrants

The Company has a plan to grant incentive stock options to employees and non-statutory stock options to other individuals who provide services to the Company. All options granted are at the discretion of the Board of Directors and vest with the option holder over a 36 or 48 month period of continuous service to the Company. The option price for all options granted to date is established by the board of Directors. The exercise price for options granted to an optionee who owns stock greater than 10% of the total voting power of all classes of stock of the company shall be 110% of the fair market value of the stock on the date the option is granted. The Company has 133,333 shares of common stock reserved for options as of March 31, 1998. The following details the stock options issued and outstanding as of March 31, 1998.

	Options Issued	Options Exercisable	Option Price	Expiration Year Ended
Incentive	9,334	9,334	\$0.25	2001
Incentive	3,000	3,000	0.25	2004
Incentive	4,500	2,256	0.32	2005
Non-statutory	3,000	3,000	0.25	2003
Non-statutory	18,000	18,000	0.25	2004
Non-statutory	36,000	30,000	0.25	2005
Non-statutory	10,000	4,992	0.32	2006

The Company has issued common stock warrants to purchase shares of common stock at a set price. The following details the common stock warrants issued and outstanding as of March 31, 1998.

	Warrants Issued	Warrant Price	Expiration Date
Underwriters' warrants	100,000	5.40	6-26-98
Warrants for refinancing note	1,000,000	.50	3-31-99

#### Note 5. Bank Line of Credit

The Company has a line-of-credit aggregating \$213,500 from a bank. At March 31, 1998 the agreement with the bank allowed up to a total of \$213,500 to be borrowed under this line-of-credit. The line is at a variable interest rate of .75% over the banks commercial base rate (10.43% at March 31, 1998), with interest on the outstanding balance due monthly. The Company has been unable to make the monthly interest payments, but is accruing the interest. The line is secured by substantially all of the assets of the Company.

#### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

##### Liquidity and Capital Resources

The Company is delinquent on its interest payments on its bank line of credit, its subordinated long term notes, most of its leases and most of its trade accounts payable. The Company has several judgments against it and several more threatened as a result of its inability to pay its obligations to its unsecured trade creditors. The judgments are all from unsecured creditors which the Company is no longer using for ongoing operations and the Company does not intend to pay these unsecured debts until its obligations to its secured creditors are satisfied. The Company currently feels that the best possibility it has available to repay its secured and unsecured creditors and to return value to its stockholders is to continue to operate the Company and to work out long term payment plans if it is able to do so in the future. While the Company does not expect that it will be forced into bankruptcy by its secured or unsecured creditors, there can be no assurance that this will not happen because of the Company's inability to meet its obligations to its creditors. The Company believes that a liquidation of its assets would only satisfy a small portion of the Company's obligations to its secured creditors and provide nothing for the Company's unsecured creditors or its stockholders.

The Company's inventory of SoundXchange hardware, which, as of March 31, 1998, accounted for approximately 65.1% of the Company's current assets, is liquid only to the extent of the Company's sales of such product. The Company has made minor engineering changes in the product in order to be able to utilize the inventory for newly developing markets and the Company hopes to continue to be able to do so in the future. Although there can be no guarantee that this will increase sales of the SoundXchange hardware, the Company believes that an increase in sales will occur allowing the Company to reduce its inventory of SoundXchange hardware at a profit.



The Company was also unable to pay its auditors in order to have audited financial statements for the years ended September 30, 1994, 1995, 1996 and 1997. The absence of audited financial statements may jeopardize the ability of the Company to continue as a reporting company and may jeopardize the ability for the Company's stock to continue to trade on the OTC Bulletin Board.

#### RESULTS OF OPERATIONS

**Revenue.** Net sales for the six months ended March 31, 1998 and 1997 were \$39,777 and \$42,441 respectively. The Company's decrease in sales is attributable mainly to less demand for its SoundXchange Models A, B and BX.

**Gross Profit.** The gross margin for the six months ended March 31, 1998 was approximately 51%, down from a gross margin of 54% for the six months ended March 31, 1997. The decrease from the previous year is due primarily to an increase in sales of the SoundXchange Model VC with its relatively lower profit margin.

**Sales and marketing expenses.** Sales and marketing expenses for the six months ended March 31, 1998 and 1997 were \$28,000 and \$40,000, respectively.

**Research and development.** There were no research and development expenses for the six months ended March 31, 1998. The Company does not have any employees currently engaged in research, product development and engineering, but the Company currently has access, through a temporary consulting arrangement with Torrey Pines Research (TPR), to former key research and development employees who are now employees of TPR. Although TPR is a stockholder of InterActive, and TPR has performed as a strategic partner in past development efforts of InterActive, there can be no assurance that TPR will continue to provide InterActive consulting services because of InterActive's current inability to pay for these consulting services. There were no amounts capitalized in connection with software development for the six months ended March 31, 1998 and 1997. Software development amortization expense for the six months ended March 31, 1998 and 1997 were \$0 and \$21,000, respectively. The Company believes that ongoing support of the Company's SoundXchange products is critical to the long term viability of such products and the future revenues of the Company.

**General and administrative.** General and administrative expenses for the six months ended March 31, 1998 and 1997 were \$6,000 and \$7,000, respectively.

**Depreciation and Amortization.** Depreciation and amortization expenses for the six months ended March 31, 1998 and 1997 were \$9,200 and \$51,900, respectively. The decrease in depreciation and amortization expense was due primarily to a one time write down of assets at fiscal year end 1997.

**Nonoperating Income (Expense).** Nonoperating income (expense) for the six months ended March 31, 1998 and 1997 were (\$2,000 and (\$16,700) respectively. The decrease in nonoperating expense was a result of income shown from recapture of inventory which was written down at September 30, 1997.

**Net Loss.** The Company suffered a net loss for the six months ended March 31, 1998 of \$26,300 or \$0.01 per share on 3,174,641 weighted average shares outstanding compared to a net loss for the six months ended March 31, 1997 of \$96,400 or \$0.03 per share on 3,117,131 weighted average shares outstanding.

Management believes that the largest challenges that the Company will continue to confront during 1998 are to obtain adequate financing and in achieving positive cash flow and profitability. While the Company is optimistic about the possibility of its overcoming these challenges and achieving its goals, the Company is a high technology company and there can be no assurance that it will be able to achieve any or all of its objectives.

PART II OTHER INFORMATION

Item 1. Legal Proceedings.

The Company has several judgments against it and several more threatened as a result of its inability to pay its obligations to its unsecured trade creditors. The judgments are all from unsecured creditors which the Company is no longer using for on going operations and the Company does not intend to pay these unsecured debts until its obligations to its secured creditors are satisfied.

The Company currently feels that the best possibility it has available to repay its secured and unsecured creditors and to return value to its stockholders is to continue to operate the Company and to work out long term payment plans if it is able to do so in the future. While the Company does not expect that it will be forced into bankruptcy by its secured or unsecured creditors, there can be no assurance that this will not happen because of the Company's inability to meet its obligations to its creditors. The Company believes that a liquidation of its assets would only satisfy a small portion of the Company's obligations to its secured creditors and provide nothing for the Company's unsecured creditors or its stockholders.

Item 2. Changes in Securities.

None

Item 3. Defaults Upon Senior Securities.

None

Item 4. Submission of Matters to a Vote of Security Holders.

None

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits.

None

(b) Reports on Form 8-K.

None

## SIGNATURES

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

Dated: May 8, 1998

INTERACTIVE INC.

/s/ Robert Stahl

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Robert Stahl  
President

/s/ Gerard L. Kappenman

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Gerard L. Kappenman  
Secretary

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