NETSMART TECHNOLOGIES INC
Form 10-K/A
August 22, 2003

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

Form 10-K/A

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2002

Commission File Number 0-21177

NETSMART TECHNOLOGIES, INC.
(Exact name of registrant as specified in its charter)

Delaware	13-3680154
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
146 Nassau Avenue, Islip, NY	11751
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (631) 968-2000

Securities registered pursuant to Section 12(b) of the Act: ____

Securities registered pursuant to Section 12(g) of the Act:

Title of Each Class	Outstanding shares as of February 11, 2003
Common Stock, par value $.01 per share	3,956,633

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__

Indicate by a check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S - K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act)

Yes [ ]   No [X]

As of June 30, 2002, the last day of our second quarter, the aggregate market value of the voting and non-voting common equity held by non affiliates was approximately $7,702,000.

DOCUMENTS INCORPORATED BY REFERENCE

None

PART I

Item 1. Business

Introduction

We develop market and support application software products to providers of services in the health and human services market, including mental health clinics, substance abuse clinics, psychiatric hospitals, public health agencies, managed care organizations and correctional facilities. Our software products perform patient management, billing, scheduling, and electronic medical records solutions for all modalities of care. These products are deployed utilizing current technologies. We sell our software products through our wholly owned subsidiary, Creative Socio-Medics Corporation, either on a license or a subscription basis to health care providers and we offer our clients software support under maintenance agreements. The maintenance contracts provide us with a recurring revenue stream.

We are a supplier of practice management systems to the behavioral health market, with over 500 contracts in place, representing approximately 50,000 clinicians, including 24 state agencies and installations in 43 states.

The cost of a new system to customers is typically in the range of $250,000 to $1 million. Governmental agencies such as mental health, mental retardation, child welfare, addiction, correction and public health facilities accounted for approximately 52% of revenue in 2002, with the remainder from private hospitals, smaller clinics, group and sole practitioners.

Business Strategy

Our systems provide comprehensive healthcare information technology solutions including billing, patient tracking and scheduling for inpatient and outpatient environments, as well as clinical documentation and medical record generation and management. We direct our marketing effort for these products towards providers of services in the health and human services market. Our branded suite of products has integrated point-of-services technologies which also include smart cards and personal digital assistants, which are commonly referred to as PDAs.

The health and human services market is always subject to changes in state and federal regulations as well as new demands required by the population. Some of the factors which we believe are affecting the market include the following.

HIPAA. As a supplier of practice management solutions to the behavioral health and substance abuse industry, we believe that we can benefit as a result of the Health Insurance Portability and Accountability Act, which is generally known as HIPAA. HIPAA essentially mandates the Health and Human Services department of the U.S. Government to enact standards regarding the standardization, privacy and security of health care information that will begin to take effect in the latter part of 2003.

We believe that this legislation will have the effect of requiring the under-automated health and human services industry to make the leap to install automated systems. We believe that our product suite, in conjunction with products offered by other companies with which we have a marketing arrangement, enables us to offer comprehensive enterprise-wide solutions for all human service providers.

Increased Demand. As a result of the recent acts of terrorism, the demand for services in the mental health and public health services has increased. Anxiety and fear have gripped many people who are now seeking mental health services. This increased demand puts more pressure on providers to improve the efficiency of care through the use of practice management and clinical systems. We believe

that the potential threat of bio terrorism will also put similar pressure on public health agencies to improve their delivery capabilities in much the same way.

Forward - Looking Statements

Statements in this Form 10-K annual report may be "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, but are not limited to, statements that express our intentions, beliefs, expectations, strategies, predictions or any other statements relating to our future activities or other future events or conditions. These statements are based on current expectations, estimates and projections about our business based, in part, on assumptions made by management. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may, and probably will, differ materially from what is expressed or forecasted in the forward-looking statements due to numerous factors, including those described above and those risks discussed from time to time in this Form 10-K annual report, including the risks described under "Risk Factors," and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in other documents which we file with the Securities and Exchange Commission. In addition, such statements could be affected by risks and uncertainties related to product demand, market and customer acceptance, competition, government regulations and requirements, pricing and development difficulties, as well as general industry and market conditions and growth rates, and general economic conditions. Any forward-looking statements speak only as of the date on which they are made, and we do not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date of this Form 10-K.

Organization of the Company

We are a Delaware corporation formed in September 1992 under the name Medical Services Corp. Our name was changed to Carte Medical Corporation in October 1993, CSMC Corporation in June 1995 and to Netsmart Technologies, Inc. in February 1996. Our executive offices are located at 146 Nassau Avenue, Islip, New York 11751, telephone (631) 968-2000. Reference to us and to Netsmart include our subsidiary, Creative Socio-Medics, unless the context indicates otherwise. Our website is located at www.csmcorp.com. Neither the Information contained in our website nor the information contained in any Internet website is a part of this Form 10-K annual report.

Risk Factors

Because we are particularly dependent upon government contracts, any decrease in funding for entitlement programs could result in decreased revenue.

We market our health information systems principally to behavioral health facilities, many of which are operated by government entities and include entitlement programs. During 2002, we generated 52% of our revenue from

contracts that are directly or indirectly with government agencies, as compared with 40% in 2001 and 51% in 2000. Government agencies generally have the right to cancel contracts at their convenience. Our ability to generate business from government agencies is affected by funding for entitlement programs, and our revenue would decline if state agencies reduce this funding.

Changes in government regulation of the health care industry may adversely affect our revenue, operating expenses and profitability.

Our business is based on providing systems for behavioral and public health organizations in both the public and private sectors. The federal and state governments have adopted numerous regulations relating to the health care

2

industry, including regulations relating to the payments to health care providers for various services, and our systems are designed to provide information based on these requirements. The adoption of new regulations can have a significant effect upon the operations of health care providers, particularly those operated by state agencies. Furthermore, changes in regulations in the health care field may force us to modify our health information systems to meet any new record-keeping or other requirements and may impose added costs on our business. If that happens, we may not be able to generate revenues sufficient to cover the costs of developing the modifications. In addition, any failure of our systems to comply with new or amended regulations could result in reductions in our revenue and profitability.

If we are not able to take advantage of technological advances, we may not be able to remain competitive and our revenue may decline.

Our customers require software which enables them to store, retrieve and process very large quantities of data and to provide them with instantaneous communications among the various data bases. Our business requires us to take advantage of recent advances in software, computer and communications technology. This technology has been developing at rapid rates in recent years, and our future may be dependent upon our ability to use and develop or obtain rights to products utilizing such technology. New technology may develop in a manner which may make our software obsolete. Our inability to use new technology would have a significant adverse effect upon our business.

Because of our size, we may have difficulty competing with larger companies that offer similar services, which may result in decreased revenue.

Our customers in the human services market include entitlement programs, managed care organizations and specialty care facilities which have a need for access to information over a distributed data network. The software industry in general, and the health information software business in particular, are highly competitive. Other companies have the staff and resources to develop competitive systems. We may not be able to compete successfully with such competitors. The health information systems business is served by a number of major companies and a larger number of smaller companies. We believe that price competition is a significant factor in our ability to market our health information systems and services, and our inability to offer competitive pricing may impair our ability to market our system.

Because we are dependent on our management, the loss of key executive officers could disrupt our business and our financial performance could suffer.

Our business is largely dependent upon our senior executive officers, Messrs. James L. Conway, our chief executive officer, Gerald O. Koop, our president, and Anthony F. Grisanti, our chief financial officer. Although we have employment agreements with these officers, the employment agreements do not guarantee that the officers will continue with us, and each of these officers has the right to terminate his employment with us on 90 days notice. Our agreements with Messrs. Conway and Grisanti are scheduled to expire on December 31, 2003, although each of Messrs. Conway and Grisanti has the right on ninety, days notice to extend his agreement for successive additional one year periods. In addition, Mr. Koop's employment agreement is scheduled to expire on December 31, 2003, following which he is expected to continue to work with us for a five-year period pursuant to a consulting agreement between us dated January 1, 2001. Our business may be adversely affected if any of our key management personnel or other key employees left our employ.

If we are unable to protect our intellectual property, our competitors may gain access to our technology, which could harm our ability to successfully compete in our market.

We have no patent protection for our proprietary software, and we rely on

non-disclosure agreements with our employees. In addition, this protection does not prevent our competitors from independently developing products similar or superior to our products and technologies. To further develop our services or products, we may need to acquire licenses for intellectual property. These licenses may not be available on commercially reasonable terms, if at all. Our failure to protect our proprietary technology or to obtain appropriate licenses could have a material adverse effect on our business, operating results or financial condition. Since our business is dependent upon our proprietary products, the unauthorized use or disclosure of this information could harm our business.

We also cannot guarantee that in the future, third parties will not claim that we infringed on their intellectual property. Asserting our rights or defending against third party claims could involve substantial costs and diversion of resources, which could materially and adversely affect us.

The covenants in our loan agreement restrict our financial and operational flexibility, including our ability to complete additional acquisitions, invest in new business opportunities, or pay down certain indebtedness.

Our revolving credit and term loan agreement contains covenants that restrict, among other things, our ability to borrow money, make particular types of investments, including investments in our subsidiaries, make other restricted payments, swap or sell assets, merge or consolidate, or make acquisitions. An event of default under our loan agreement could allow the lender to declare all amounts outstanding to be immediately due and payable. We have pledged substantially all of our consolidated assets to secure the debt under our loan

agreement. If the amounts outstanding under the loan agreement were accelerated, the lender could proceed against those consolidated assets. Any event of default, therefore, could have a material adverse effect on our business. Our loan agreement also requires us to maintain specified financial ratios. Our ability to meet these financial ratios can be affected by events beyond our control, and we cannot assure you that we will meet those ratios. We also may incur future debt obligations that might subject us to restrictive covenants that could affect our financial and operational flexibility or subject us to other events of default.

Our growth may be limited if we cannot make acquisitions.

A part of our growth strategy is to acquire other businesses that are related to our current business. Such acquisitions may be made with cash or our securities or a combination of cash and securities. To the extent that we require cash, we may have to borrow the funds or issue equity, which could dilute our earnings or the book value per share of our common stock. Our stock price may adversely affect our ability to make acquisitions for equity or to raise funds for acquisitions through the issuance of equity securities. If we fail to make any acquisitions, our future growth may be limited. As of the date of this prospectus, we do not have any agreement or understanding, either formal or informal, as to any acquisition.

If we make any acquisitions, they may disrupt or have a negative impact on our business.

If we make acquisitions, we could have difficulty integrating the acquired company's personnel and operations with our own. In addition, the key personnel of the acquired business may not be willing to work for us, and our officers may exercise their rights to terminate their employment with us. We cannot predict the affect expansion may have on our core business. Regardless of whether we are successful in making an acquisition, the negotiations could disrupt our ongoing business, distract our management and employees and increase our expenses.

We do not anticipate, and our loan agreement prohibits, the payment of dividends on our common stock, therefore, investors cannot rely on dividends to increase the value of their investment in Netsmart.

We have never paid a cash dividend and we do not anticipate paying cash dividends on our common stock in the foreseeable future. We presently intend to retain future earnings, if any, in order to provide funds for use in the

4

operation and expansion of our business. Consequently, investors cannot rely on the payment of dividends to increase the value of their investment on Netsmart. In addition, we are a party to a loan agreement which prohibits us from paying cash dividends without the prior consent of our lender.

The employment contracts with our executive officers and provisions of Delaware law may deter or prevent a takeover attempt and may reduce the price investors might be willing to pay for our common stock.

The employment contracts between us and each of James Conway, Gerald Koop and Anthony Grisanti provide that in the event there is a change in control of Netsmart, the employee has the option to terminate his employment agreement. Upon such termination, each of Messrs. Conway, Koop and Grisanti has the right to receive a lump sum payment equal to the sum of

* his compensation for a twelve-month period plus
* an amount equal to his monthly compensation multiplied by
    * the greater of 30 and
    * 1.5 times the number of years the employee has been employed by Netsmart, but not more than 36.

In addition, Delaware law restricts business combinations with stockholders who acquire 15% or more of a company's common stock without the consent of the company's board of directors.

These provisions could deter or prevent a takeover attempt and may also reduce the price that certain investors might be willing to pay in the future for shares of our common stock

Any issuance of preferred stock may adversely effect the voting power and equity interest of our common stock.

Our certificate of incorporation gives our board of directors the right to create new series of preferred stock. As a result, the board of directors may, without stockholder approval, issue preferred stock with voting, dividend, conversion, liquidation or other rights which could adversely affect the voting power and equity interest of the holders of common stock. The preferred stock, which could be issued with the right to more than one vote per share, could be utilized as a method of discouraging, delaying or preventing a change of control. The possible impact on takeover attempts could adversely affect the price of our common stock. Although we have no present intention to issue any additional shares of preferred stock or to create any series of preferred stock, we may issue such shares in the future. If we issue preferred stock in a manner which dilutes the voting rights of the holders of the common stock, our listing on The Nasdaq SmallCap Market may be impaired.

Shares may be issued pursuant to options and warrants which may adversely affect the market price of our common stock.

We may issue stock upon the exercise of options to purchase shares of our common stock pursuant to our long term incentive plans, of which options to purchase 664,702 shares were outstanding at December 31, 2002. The exercise of these options and the sale of the underlying shares of common stock may have an adverse effect upon the price of our stock.

In addition, we may issue stock upon the exercise of warrants to purchase an aggregate of 768,544 shares of our common stock pursuant to various agreements, of which warrants to purchase 708,544 shares were outstanding at December 31, 2002. The exercise of these warrants and the sale of the underlying shares of common stock may have an adverse effect upon the price of our stock.

Software and Related Systems and Services

We develop, market and support computer software which enables health and human services healthcare organizations to provide a full range of services in a network computing environment.

Users typically purchase one of several healthcare information systems, in the form of a perpetual license to use the system, as well as purchasing professional services, support, and maintenance. In addition, we resell third party hardware and software to our customers pursuant to value added resale arrangements with them. Since our products are designed to operate on hardware platforms that either support the Microsoft Windows operating system platform (Win_2000, NT, XP), or Unix operating system (IBM -AIX, Sun Microsystems-Solaris, Hewlett Packard-HPUX). We also offer these products. Due to the fact that our products operate on a variety of platforms, we are not dependent on any single hardware vendor or operating system. Since our products utilize the Cache database and development software provided by Intersystems Corporation, we resell this software. Due to the fact that our products are designed to operate solely with Cache products, we are dependent on Cache products for our operations. The professional services include project management, training, consulting and software development services, which are provided either on a time and material basis or pursuant to a fixed-price contract. The software development services may require the adaptation of health care information technology systems to meet the specific requirements of the customer.

Our typical license for a health information system ranges from $10,000 to $100,000 for a single facility healthcare organization to $250,000 to $1,000,000 for multi-unit care organizations such as those run by state agencies. Revenue from license fees were approximately $1,753,000, or 7.9% of revenue, for 2002, $747,000, or 4.1% of revenue, for 2001 and $2,603,000, or 12.9% of revenue, for 2000. A customer's purchase order may also include third party hardware or software. Revenue from hardware and third party software accounted for approximately $3,822,000, or 17.3% of revenue, for 2002, $2,390,000, or 13.2% of revenue, for 2001 and $4,158,000, or 20.6% of revenue, for 2000. Revenue from turnkey systems labor accounted for approximately $7,418,000, or 33.5% of revenue, for 2002, $6,568,000, or 36.3% of revenue, for 2001 and $6,502,000, or 32.2% of revenue in 2000.

Maintenance services have generated increasing revenue and have become a more significant portion of our business since most purchasers of health care information system licenses also purchase maintenance service. Maintenance revenue increases as existing customers purchase additional licenses and new customers purchase their initial software licenses. By agreement with our customers, we provide telephone help services and maintain and upgrade their software. Maintenance contracts may require us to make modifications to meet any new federal and state reporting requirements which become effective during the term of the maintenance contract. We do not maintain the hardware and third party software sold to our customers, but we provide a telephone help line service for certain third party software, which we license to our customers. Our maintenance revenue was approximately $6,247,000, or 28.2% of revenue, for 2002, $5,192,000, or 28.7% of revenue, for 2001 and $3,521,000, or 17.5% of revenue, for 2000. Our small systems revenue was approximately $929,000, or 4.2% of revenue, for 2002, $1,180,000, or 6.5% of revenue, for 2001 and $1,124,000, or 5.6% of revenue, for 2000.

We currently offer five product modules that provide a range of core application requirements for behavioral healthcare providers. These products consist of a suite of complete information technology applications developed by us, together with software provided by others which enables us to offer enterprise-wide solutions to the behavioral health industry. We offer the products in a variety

of delivery modes.

* Avatar - Practice Management: This system is a comprehensive solution providing patient management functions, billing, tracking, scheduling, and reporting for inpatient treatment facilities.

6

* Avatar - Clinician Workstation: This workstation provides a clinician with documentation and medical record management including assessment, care planning, progress notes and on-line medical records. The clinician workstation is our electronic medical record system for behavioral health, which integrates the clinical tools necessary for an interdisciplinary approach to the delivery of human services.

* Methadone Clinical System: Pursuant to a joint marketing agreement with Mallinckrodt Pharmaceutical Specialties, a division of Mallinckrodt Inc., we offer a solution for dispensing, admissions and medical records, counselor and reception/security specifically for methadone clinics. We can integrate Methadone Clinical System with our other behavioral health products.

* Avatar - Managed Care: The managed care and employee assistance program modules include such features as service request management, contact tracking (patients, providers, others), import of eligibility information by contract, provider search by location, specialty, contract, hospital privileges, claims adjudication and payment.

Markets and Marketing

The market for behavioral/public health information systems and related services consists of both private and publicly operated providers offering hospital or community-based outpatient behavioral/public healthcare services. These healthcare providers require a healthcare information system to administer their programs. We believe that there are at least 15,000 behavioral/public healthcare providers in the United States, including public and private hospitals, private and community-based residential facilities and federal, state and local governmental agencies.

Many long-term behavioral/public healthcare facilities are operated by government entities and include those operated as part of entitlement programs. During the years ended December 31, 2002, 2001 and 2000, approximately 52%, 40% and 51%, respectively, of revenue was generated from contracts with government agencies. Contracts with government agencies generally include provisions which permit the contracting agency to cancel the contract for its convenience, although we have not experienced a termination for convenience in the last five years.

In addition to these major behavioral/public healthcare providers, there are a larger number of sole practitioners, group practices and smaller clinics which may also require behavioral/public healthcare facilities. We intend to market our Internet-based systems to these potential customers.

We believe that the demand for information technology solutions is increasing as a result of new federal initiatives for data standards as well as continuous pressure from managed care providers to reduce healthcare delivery costs while expanding the availability of services.

In order to remain competitive, the health and human services health delivery networks need detailed clinical and management information systems that enable providers within the networks to maintain a broad scope of accurate medical and

financial information, manage costs and deliver quality care efficiently. In addition, the need to upgrade existing systems to meet the increased demand for data processing needs of managed care and regulatory oversight has also resulted in an increased demand for behavioral/public healthcare information technology. These data processing needs include analysis of patient assessments, maintenance of patient records, administration of patient treatment plans and the overall coordination of patient case management.

We coordinate our marketing effort with the state agencies and other major users of our systems. Our state agency clients formed a User Group Association, presently consisting of state organizations or agencies from 26 states. The association's members work with us to assess and determine future requirements in both patient managed care coordination and regulatory reporting.

No customer accounted for 10% or more of our revenue in 2002, 2001 and 2000.

We had a backlog of orders, including ongoing maintenance and data center contracts for our behavioral health information systems of $25.3 million at December 31, 2002 and $16.5 million at December 31, 2001. We expect to fill approximately $21.3 million of the 2002 backlog during 2003.

The major components of backlog is revenue of approximately $15 million from existing turnkey contracts. Maintenance of approximately $7 million that is comprised of both amounts expected to be filled under unexpired maintenance contracts and also amounts that are subject to automatic renewal, and unexpired Data Center contracts of approximately $2 million calculated using historical experience to determine future useage.

Data Center

Since our inception the Data Center has provided software which performs clinical and billing services for outpatient facilities, including mental health, alcohol and substance abuse facilities. Services include statistical reporting, data entry, electronic billing and submission.

All of our products and services are offered not only in a turnkey mode of operation but also in an Application Service Provider (ASP) mode in which the client uses our software products with part or all of the software's operation taking place on the computer facilities of our data centers. At present we have a data center service facility in Islip, New York and anticipate opening an additional facility in Ohio in 2003.

Revenue from our Data Center was approximately $1,957,000 or 8.9% of revenue for 2002, $2,042,000 or 11.3% of revenue for 2001 and $2,263,000 or 11.2% of revenue for 2000.

During 2002, two customers each accounted for more than 10% of the total Data Center revenue. One customer was a New York State agency, which accounted for $199,000, or 10.2% of total Data Center revenue. The other client was a hospital in New York City, which accounted for $225,000, or 11.5% of total Data Center revenue. During 2001, this same major hospital accounted for $351,000, or 17.2% of total Data Center revenue. During 2000, two customers each accounted for more than 10% of the total Data Center revenue. Both were hospitals in New York City, one of which accounted for $447,000 or 19.7% of total Data Center revenue and the other which accounted for $269,000, or 11.9% of total Data Center revenue. None of the above mentioned clients accounted for more than 10% of our consolidated revenue.

Our Data Center backlog at December 31, 2002 was $2,076,000. We anticipate that

all of this backlog will be earned in 2003. The Data Center backlog at December 31, 2001 was $1,974,000.

Product Development

We incurred product development costs relating to our health and human services information systems of approximately $1,318,000 in 2002, $1,335,000 in 2001 and $1,360,000 in 2000, all of which was company-sponsored. In 2001, we incurred capitalized software development costs of approximately $167,000 associated with our acquisition of software products from Advanced Institutional Management Software, Inc. In 2000, we incurred capitalized software development costs of

approximately $219,000 in connection with the development of our web portal services and application service provider solutions for healthcare providers. During 2000, we also incurred capitalized software development costs of $334,000 associated with our acquisition of the Connex suite of managed care and employee assistance program information systems. Included in these costs is $100,000 of valued assigned to the 15,528 shares of our common stock which we issued to acquire the Connex suite.

Competition

The healthcare software industry is highly competitive. Although we believe that we can provide a health care facility or managed care organization with software to enable it to perform its services more effectively, other software companies provide comparable systems and also have the staff and resources to develop competitive systems.

Healthcare information technology is an $18 billion industry served by numerous vendors. The dominant health care information technology vendors have achieved annual sales of more than $1 billion by focusing on solutions for large medical/surgical health care providers, such as large hospital systems and health maintenance organizations, and, have not focused on the behavioral/public healthcare industry. We believe that most of the presently available healthcare management software does not meet the specific needs of the behavioral/public healthcare industry, and that the functionality of our information systems are designed to meet the needs of this market. However, the behavioral health information systems business is serviced by a number of companies, some of which are better capitalized with larger infrastructure than we, and we may not be able to continue to compete effectively with such companies.

Additionally, we face significant competition in the Data Center medical systems ASP market. General ASP utilities offer clients use of computer facilities and operations staff to process either generalized medical software or software selected by the client from other software vendors. Large billing and clearing house computer service companies provide a broad area of billing for a diverse marketplace. Many organizations start with billing as their primary reason for automation spending. Several types of professional service firms offer departmental staff to operate a client's already in-house system when the client believes that such an approach will provide the needed expertise at a cost effective price. Our ASP service is focused on providing a complete and cost effective service to a specific set of sectors in the large health and human services marketplace. Behavioral health requires the ideal organization of software, systems and staff to enable a client to maximize service at a reasonable cost. Most important is that the service is based on the exclusive use of the Company's proprietary suite of Avatar products which enables a potential client to initiate the use of any part of a broad array of needed

clinical and financial systems for as long as these functions are needed knowing that these services are developed, operated, and updated by a professional IT staff which is on call as needed. In addition, our experience is that, once a client has contracted for services, it generally remains a client and is unaffected by competitive offerings. Some of our clients have been working with us for up to thirty years. We believe our specialized experience and investment in related software provides us with a competitive advantage.

We compete in the Health and Human Services Systems market with the following behavioral healthcare vendors:

Anasazi Software, Inc.
Askesis Development Group, Inc.
Civerex Systems, Inc.
CMHC Systems
Geneva Software
InfoMC, Inc.
IMPEL Strategic Solutions

Multi-Health Systems, Inc.
Qualifacts System inc.
Raintree Systems Inc.
SecureHEALTH Inc.
Sequest Technologies Inc.
The Echo Group
UNI/CARE Systems, Inc.
XAKTsoft, Inc.

As our business has expanded to the sale of larger integrated healthcare delivery systems, we have begun to compete with companies such as Siemens, HBOC, IDX, Meditech, Quadramed, and Misys. In the public health arena, We have competed against QS Technologies, MANTECH, and QS Inc.

Competitive Position:

Creative Socio-Medics has been in business since 1968. As a core part of its strategic business model, Creative bids on competitive procurements numerous times during the calendar year and has a very high win ratio, which is evidence of its leadership. This is especially evident in the statewide mental health/mental retardation field with Creative's dominance in that marketplace having for which it has 26 statewide systems.

We have an established customer base of more than 500 clients nationwide, including substantial private and government providers of healthcare services. These 500 contracts represent approximately 50,000 clinicians, including 26 state agencies and installations in 43 states.

Government Regulations and Contracts

The federal and state governments have adopted numerous regulations relating to the health care industry, including regulations relating to the payments to health care providers for various services. The adoption of new regulations can have a significant effect upon the operations of health care providers and insurance companies. Although our business is aimed at meeting certain of the problems resulting from government regulations and from efforts to reduce the cost of health care, we cannot predict the effect of future regulations by governments and payment practices by government agencies or health insurers, including reductions in the funding for or scope of entitlement programs. Any change in the structure of health care in the United States can have a material

effect on companies, such as us, that provide services to the health care industry, including those providing software. Although we believe that the likely direction which may result from the current study of the health care industry would be an increased trend to managed care programs, thereby increasing the importance of automation, our business may not benefit from any changes in the industry structure. Even if the industry does evolve toward more healthcare being provided by managed care organizations, it is possible that there will be substantial concentration in a few very large organizations, which may seek to develop their own software or obtain software from other sources. To the extent that the health care industry evolves with greater government-sponsored programs and less privately run organizations, our business may be adversely affected. Furthermore, to the extent that each state changes its own regulations in the health care field, it may be necessary for us to modify our behavioral health information systems to meet any new record-keeping or other requirements imposed by changes in regulations, and we may not be able to generate revenues sufficient to cover the costs of developing the modifications.

A significant amount of our business has been with government agencies, including specialized care facilities operated by, or under contract with, government agencies. The decision on the part of a government agency to enter into a contract is dependent upon a number of factors, including economic and budgetary problems affecting the local area, and government procurement regulations, which may include the need for approval by more than one agency

before a contract is signed. In addition, government agencies generally include provisions in their contracts which permit the contracting agency to cancel the contract at its convenience. We have not experienced a termination for convenience in the last five years.

Intellectual Property Rights

We have no patent rights for our behavioral health information system software, but we rely upon copyright protection for our software, as well as non-disclosure and secrecy agreements with our employees and third parties to whom we disclose information. We may not be able to protect our proprietary rights to our system and third parties may claim rights in the system. Disclosure of the codes used in any proprietary product, whether or not in violation of a non-disclosure agreement, could have a materially adverse affect upon us, even if we are successful in obtaining injunctive relief. We must continue to invest in product development, employee training, and client support.

Employees

As of December 31, 2002, we had 145 employees, including 4 executive, 11 sales and marketing, 121 technical and 9 clerical and administrative employees.

Executive Officers

Information concerning our executive officers is included in Item 11, Directors and Executive Officers for the Registrant.

Item 2. Property

We lease office space at the following locations:

Location	Purpose	Space	Annual Rental	Expiration

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146 Nassau Avenue Islip, New York	Executive offices	18,000 square feet	$327,000, plus 4% annual increases	12/31/03
1335 Dublin Road Columbus, Ohio	Offices	3,500 square feet	$56,000	11/30/03
5120 Shoreham Place San Diego, California	Offices	2,800 square feet	$72,000	07/31/05

We believe that our space is adequate for our immediate needs and that, if additional space is required, it would be readily available on commercially reasonable rates.

Item 3. Legal Proceedings

In October 2000, the Company's subsidiary, Creative Socio-Medics, commenced an action against the City of Richmond, in the Supreme Court of the State of New York, County of Suffolk, which action was subsequently removed to the United States District Court for the Eastern District of New York, for failure to pay more than $1 million pursuant to a contract between the Company and Richmond.

Richmond advised the court that it intended to move to dismiss the complaint for lack of personal jurisdiction in New York and improper venue. In November 2000, Richmond filed a complaint in the Circuit Court for the City of Richmond, Richmond, Virginia, alleging, among other things, that the contract with Creative Socio-Medics was procured through fraudulent misrepresentations concerning the nature of the work to be performed and the price for the services and that Creative Socio-Medics failed to perform its obligations under the agreement, seeking damages of $373,000 and a finding that it owes no additional amounts to Creative Socio-Medics. The parties entered into a stipulation staying the Richmond action until a determination of Richmond's jurisdictional challenges to the New York action. On August 21, 2002, the United States District Court for the Eastern District of New York denied Richmond's motion to dismiss the Company's complaint for lack of personal jurisdiction in New York on the basis of improper venue. The Company believes it has valid claims against Richmond and intends to vigorously pursue those claims. We also believe that the allegations contained in Richmond's complaint are without merit and we intend to vigorously defend against those claims.

The Company is involved in other litigation through the normal course of business. The Company believes that the resolution of these matters will not have a material adverse effect on the Company's consolidated financial position and results of operations.

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

On January 9, 2003, we held a special meeting of stockholders.

The following proposals were approved as follows:

	Votes For	Votes Against	Abstain	Broker Non-Votes
Amendment to the 2001 Long Term Incentive Plan	1,605,099	106,583	9,189	1,810,906

Approval of the selection of Marcum & Kliegman LLP as independent auditors for 2002	3,481,645	3,666	7,621	38,845

Part II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters

Our common stock is traded on The Nasdaq SmallCap Market under the symbol NTST. Set forth below is the reported high and low sales prices of our Common Stock for each quarterly period during 2002 and 2001.

Quarter Ended	High	Low
March 31, 2002	3.45	2.40
June 30, 2002	2.89	2.08
September 30, 2002	4.60	1.70
December 31, 2002	7.03	4.10
March 31, 2001	2.84	2.08
June 30, 2001	2.27	2.06
September 30, 2001	2.11	1.68
December 31, 2001	3.06	1.69

As of December 31, 2002, there were approximately 2,310 beneficial owners of our common stock. The closing price of our common stock was $4.68 per share on February 10, 2003. These quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not represent actual transactions.

We have not paid any cash dividends to the holders of our common stock since our organization and do not anticipate that we will pay any dividends in the foreseeable future. We currently intend to retain any future earnings for use in the operation and development of our business and for potential acquisitions. In addition, the terms of our revolving credit and term loan agreement prohibits us from paying cash dividends.

Sales of Unregistered Securities

On April 10, 2002, the Company issued to Newbridge Securities Corporation, Series E Common Stock Purchase Warrants to purchase 200,000 shares in connection with a financial advisory agreement whereby the Company will pay consulting fees in addition to the issuance of the warrants. These warrants, which expire over various times ranging from one to two years, were valued at $.24 per warrant, which represented the costs of the services based upon the contractual agreement. Either party may terminate the agreement. The warrants have the following exercise price, vesting dates and expiration date for the number of shares set forth below:

Shares	Exercise Price	Vesting Date	Expiration Date
50,000	$2.70	April 10, 2002	March 31, 2003
30,000	$4.00	June 1, 2002	May 31, 2003
30,000	$5.00	September 1, 2002	February 28, 2004
30,000	$6.00	November 1, 2002	April 30, 2004
30,000	$7.00	January 1, 2003	December 31, 2004

30,000	$8.00	February 28, 2003	January 31, 2005

The issuance of the foregoing securities was issued in reliance upon the exemption from registration provided by Section 4(2) of the Securities Act of 1933, as amended, as a transaction not involving a public placement.

13

Equity Compensation Plan Information

The following table sets forth information relating to our compensation plans as of December 31, 2002.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of secu remaining avai future issuanc equity compens plans (excludi securities ref column (a)
Equity compensation plans approved by security holders	1,038,246	$6.172	15,000
Equity compensation plans not approved by security holders	395,000	$5.446	--
Total	1,433,246	$5.97	15,000

The terms of the options and warrants to purchase 395,000 shares not approved by shareholders to be issued are as follows:

|*| warrants to purchase 100,000 shares of common stock at an exercise price of $5.45 per share were issued in 1999 in connection with a financial advisory agreement, whereby we paid consulting fees in addition to the issuance of the warrants. These warrants were valued at $.58 per warrant, which represented the cost of services based upon the contractual agreement. The exercise price of the warrants represented a 15% premium over the market value of the stock at the time of issuance. These warrants will expire in October 2004.

|*| warrants to purchase 20,000 shares of common stock at an exercise price of $4.20 per share were issued in 1999 for financial services rendered. These warrants were valued at $2.20 per warrant based upon the Black-Scholes calculation, which included an interest rate of 5.51%, and a volatility rate of .3. The exercise price of the warrants was the market value of the stock at the time of issuance. These warrants will expire in October 2004.

|*| options to purchase 75,000 shares at a price of $6.50 per shares were

issued as an inducement to a new employee. These options will expire in March 2005.

|*| warrants to purchase 200,000 shares at prices ranging from $2.70 to $8.00 per share were issued in 2002 in connection with a financial advisory agreement, whereby we paid consulting fees in addition to the issuance of the warrants. See "Sales of Unregistered Securities."

In addition to the options available for grant in equity compensation plans that were approved by the stockholders, in January 2003, at a special meeting of stockholders, the stockholders approved an increase of 370,000 in the number of shares of common stock issuable pursuant to our 2001 Long-Term Incentive Plan, of which options to purchase 217,500 shares were granted on January 27, 2003.

Item 6. Selected Financial Data

The selected consolidated financial data set forth below for the five years in the period ended December 31, 2002 has been derived from the company's audited consolidated financial statements. This information should be read in conjunction with the audited consolidated financial statements and notes thereto.

	Year Ended December 31,				
	2002	2001	2000	1999	1998
	(in thousands except per share data)				
Selected Statements of Operations Data:					
Revenue	$22,126	$ 18,119	$ 20,171	$ 21,252	$ 13,165
Income from Continuing Operations before interest and other financing costs	1,095	399	2,141	1,895	759
Income (Loss) from Discontinued Operations	--	--	70	180	(217)
Net Income	1,195(1)	315	2,386(2)	1,825	196
Per Share Data - Diluted:					
Continuing Operations	.29	.08	.61	.47	.12
Discontinued Operations	--	--	.02	.05	(.08)
Net Income (loss)	.29	.08	.63	.52	.04
Weighted average number of shares outstanding	4,153	3,872	3,771	3,516	2,865
Selected Balance Sheet Data:					
Working Capital	9,656	7,903	5,858	2,012	10

Total Assets	22,275	18,007	15,301	13,972	10,289
Long Term Debt Including Current Portion	1,750	2,250	--	--	--
Total Liabilities	10,968	8,060	5,997	8,617	7,005
Accumulated Deficit	(9,376)	(10,571)	(10,886)	(13,272)	(15,097)
Stockholders' Equity	11,306	9,948	9,303	5,355	3,284

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(1) Includes benefit of net operating loss in the amount of $400,000.

(2) Includes benefit of net operating loss in the amount of $494,000.

All per share information has been retroactively adjusted for the one-for-three reverse stock split which became effective September 1998.

15

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

Our operations are grouped into two segments:

|*| Software and Related Systems and Services
|*| Data Center (service bureau services)

Results of Operations

Fixed price software development contracts and licenses accounted for 44% and 38% of consolidated revenue for the years ended December 31, 2002 and 2001, respectively. We recognize revenue for fixed price contracts on the estimated percentage of completion basis. Since the billing schedules under the contracts differ from the recognition of revenue, at the end of any period, these contracts generally result in either costs and estimated profits in excess of billing or billing in excess of cost and estimated profits. Revenue from fixed price software development contracts is determined using the percentage of completion method which is based upon the time spent by our technical personnel on a project. As a result, during the third and fourth quarters, when many of our employees are on vacation and holidays, our revenue was affected. Our time spent on projects during the second half of the year generally ranges from 1% to 3% less than time spent on projects during the first half of the year.

Years Ended December 31, 2002 and 2001

Our total revenue for 2002 was $22,126,000, an increase of $4,007,000, or 22%, from our revenue for 2001, which was $18,119,000.

Revenue from contracts from government agencies represented 52% of revenue in 2002 and 40% of revenue in 2001. This reflects an increase in new government contracts.

Software and Related Systems and Services

Our Software and Related Systems and Services revenue for 2002 was $20,169,000, an increase of $4,092,000, or 25%, from our revenue for 2001, which was

$16,077,000. Software and related systems and services revenue is comprised of turnkey systems labor revenue, revenue from sales of third party hardware and software, license revenue, maintenance revenue and revenue from small turnkey systems.The largest component of revenue was turnkey systems labor revenue, which increased to $7,418,000 in 2002, from $6,568,000 in 2001, reflecting a 13% increase. Turnkey systems labor revenue refers to labor associated with turnkey installations and includes categories such as training, installation, project management and development.The increase in turnkey systmens labor revenue was substantially the result of an increase in spending for the information systems in the human services marketplace and our ability to provide the staff necessary to generate additional revenue. Labor rate price changes from 2002 to 2001 resulted in a 1% increase in the average daily billing rate and accounted for approximately $76,000, or 9%, of the total turnkey systems labor increase. Revenue from third party hardware and software increased to $3,822,000 in 2002, from $2,390,000 in 2001, which represents an increase of 60%. Sales of third party hardware and software are made in connection with the sales of turnkey systems. These sales are typically made at lower gross margins than our human services revenue. License revenue increased to $1,753,000 in 2002, from $747,000 in 2001, reflecting an increase of 135%. License revenue is generated as part of a sale of a human services information system pursuant to a contract or purchase order that includes delivery of the system and maintenance. The increase in

16

license revenue was the result of an increase in spending for information systems in the human services marketplace. Maintenance revenue increased to $6,247,000 in 2002, from $5,192,000 in 2001, reflecting an increase of 20%. As turnkey systems are completed, they are transitioned to the maintenance division, thereby increasing our installed base. Revenue from the sales of our small turnkey division decreased to $929,000 in 2002, from $1,180,000 in 2001, reflecting a decrease of 21%. Small turnkey division sales relate to turnkey contracts that are less than $50,000 and are usually completed within one month. We are experiencing a decline in small turnkey systems as a result of a redirection of our sales efforts to larger turnkey sales.

Gross profit increased to $6,636,000 in 2002 from $5,095,000 in 2001, reflecting an increase of 30.2%. Our gross margin percentage increased to 32.9% in 2002 from 31.7% in 2001. Although license and maintenance revenue, which are highly margined revenue components, increased in 2002, our gross margin percentage did not increase proportionately. This is because the mix of our revenue components for 2002 included a larger amount of third party hardware and software revenue than 2001. Our third party hardware and software revenue yields margins significantly less than our margins from human services revenue.

Data Center (Service Bureau Services)

Data center clients typically generate approximately the same amount of revenue each year. We bill on a transaction basis or on a fixed fee arrangement. Historically, each year we increase the transaction or fixed fees by an amount that approximates the New York urban consumer price index increase. The data center revenue decreased to $1,957,000 in 2002 from $2,042,000 in 2001, representing a decrease of $85,000, or 4%. In 2001, we provided additional services to a client for fees in the amount of $120,000. These services were not provided for in 2002.

Gross profit decreased to $946,000 in 2002 from $1,023,000 in 2001. Our gross margin percentage decreased from 50.1% in 2001 to 48.3% in 2002. This decrease was the result of the reduction in revenue with no corresponding decrease in costs.

Operating expenses

Selling, general and administrative expenses were $5,168,000 in 2002, reflecting an increase of $784,000 or 18% from the $4,384,000 in 2001. This increase was substantially in the area of provisions for bonuses, which increased by $190,000, investor relations, which increased by $97,000, consulting fees, which increased by $77,000, general insurance, which increased by $71,000, G&A salaries which increased by $46,000, non recurring costs related to the national users conference of $110,000 and settlement of a lawsuit for $69,000.

We incurred product development expenses of $1,318,000 in 2002, a decrease of 1% from the $1,335,000 in 2001. During 2002, we continued to invest in improved functionality and technology in our products, but at a lesser extent than in 2001.

Interest and other expenses was $262,000 in 2002, an increase of $75,000, or 40%, from the $187,000 in 2001. This increase was substantially the result of interest associated with the $2,500,000 term loan, which we received in June 2001 and an other than temporary decline in the value of a security.

Interest and other income consisted of interest income of $46,000 in 2002 which was generated from short term investments and interest income of $42,000 which was generated from short term investments, and other income of $30,000, which relates to a gain realized on stock investment in 2001.

We have a net operating loss tax carry forward of approximately $9 million. In 2002, we recorded current income tax expense of $84,000, which related to various state and local taxes. In addition, we recognized a partial deferred tax benefit in the amount of $400,000 principally due to a reduction in the valuation allowance of $400,000 related to our net operating loss carry forward. In 2001 we recorded an income tax benefit of $31,000. This benefit was based upon an overaccrual of state and federal taxes in 2000 as well as the recognition of an additional $6,000 benefit of our operating loss carry forward.

As a result of the foregoing factors, in 2002, we had a net income of $1,195,000, or $.32 per share (basic) and $.29 per share (diluted). For 2001, we had net income of $315,000, or $.09 per share (basic) and $.08 per share (diluted).

Years Ended December 31, 2001 and 2000

Our total revenue for 2001 was $18,119,000, a decrease of $2,052,000, or 10%, from our revenue for 2000, which was $20,171,000.

Revenue from contracts from government agencies represented 40% of revenue in 2001 and 51% of revenue in 2000. This decrease reflects a reduction in new government contracts.

Software and Related Systems and Services

Our Software and Related Systems and Services revenue for 2001 was $16,077,000, a decrease of $1,831,000, or 10%, from our revenue for 2000, which was $17,908,000. The largest component of revenue was turnkey systems labor revenue, which increased to $6,568,000 in 2001, from $6,502,000 in 2000, reflecting a 1% increase. Turnkey systems labor revenue refers to labor associated with turnkey installations and includes such categories as training, installation, project management and development. Although there was a general decline in the sales of turnkey systems due to an industry wide slowdown in information technology purchasing activity, we were able to generate additional labor revenue for

customization and enhancements services for our existing client base as well as increase our average daily billing rate by 7%. Revenue from third party hardware and software decreased to $2,390,000 in 2001, from $4,158,000 in 2000, which represents a decrease of 43%. Sales of third party hardware and software are made in connection with the sales of turnkey systems and were affected by the decline in the sales of turnkey systems. These sales are typically made at lower gross margins than our behavioral health systems and services revenue. License revenue decreased to $747,000 in 2001, from $2,603,000 in 2000, reflecting a decrease of 71%. License revenue is generated as part of a sale of a human services health information system pursuant to a contract or purchase order that includes delivery of the system and maintenance and is affected by the decline in revenue from turnkey systems. Maintenance revenue increased to $5,192,000 in 2001, from $3,521,000 in 2000, reflecting an increase of 48%. As turnkey systems are completed, they are transitioned to the maintenance division. Included in 2001 is $935,000 of maintenance revenue related to contracts for Advanced Institutional Management Systems ("AIMS") software. We acquired the rights to the AIMS software, including its installed customer base, in May 2001. Revenue from the sales of our small turnkey division increased to $1,180,000 in 2001, from $1,124,000 in 2000, reflecting an increase of 5%.%. Small turnkey division sales relate to turnkey contracts that are less than $50,000, in the methadone dispensing market and are usually completed within one month.

Gross profit decreased to $5,095,000 in 2001 from $6,977,000 in 2000, reflecting a decrease of 27%. Our gross margin percentage decreased to 32% in 2001 from 39% in 2000. This decrease was the result of a decrease in our license revenue mentioned above. In addition, the gross margin associated with the AIMS maintenance revenue is lower than the gross margin experienced with our other maintenance revenue.

18

Data Center

The data center (service bureau) revenue decreased to $2,042,000 in 2001, from $2,263,000 in 2000, reflecting a decrease of 10%, or $221,000. In 2000, we provided additional services to one client for fees in the amount of $226,000 as compared to $120,000 in 2001. This represented $106,000 of the decrease. The remaining $115,000 reduction was the result of a smaller client base.

Gross profit decreased to $1,023,000 in 2001 from $1,238,000 in 2000. Our gross margin percentage decreased from 54.7% in 2000 to 50.1% in 2001. This decrease was the result of the reduction in revenue with no corresponding decrease in costs.

Operating expenses

Selling, general and administrative expenses were $4,384,000 in 2001, reflecting a decrease of $331,000, or 7%, from the $4,715,000 in 2000. This decrease was substantially due to a reduction in employee bonus provisions, which decreased by $454,000 and costs which decreased by $181,000 related to issuance and extensions of warrants that were issued for financial consulting services. These decreases were partially offset by an increase in sales and marketing costs of $172,000 and an increase in legal fees of $157,000.

We incurred product development expenses of $1,335,000 in 2001, a decrease of 2% from the $1,360,000 in 2000. During 2001, we continued to invest in improved functionality and technology in our products, but at a lesser extent than in 2000.

Interest expense was $187,000 in 2001, an increase of $26,000, or 16%, from the $161,000 in 2000. This increase was substantially the result of interest

associated with the $2,500,000 term loan arrangement, which we entered into in June 2001.

Interest and other income consisted of interest income of $42,000, which was generated from short-term investments and other income of $30,000 which relates to a gain realized on stock investment.

We have a net operating loss tax carry forward of approximately $11 million. In 2001 we recorded an income tax benefit of $31,000. This benefit was based upon an overaccrual of state and federal taxes in 2000. In 2000, we provided for income taxes in the amount of $157,000. The 2000 provision was based upon federal alternative minimum tax calculations as well as for certain state taxes. In addition, we recognized a partial tax benefit in the amount of $494,000 principally related to our net operating loss carry forwards. We recognized an additional $6,000 benefit of our operating loss carry forwards in 2001.

As a result of the foregoing factors, in 2001, we had a net income of $315,000, or $.09 per share (basic) and $.08 per share (diluted). For 2000, we had net income of $2,386,000, or $.71 per share (basic) and $.63 per share (diluted).

Liquidity and Capital Resources

We had working capital of $9.7 million at December 31, 2002 as compared to working capital of $7.9 million at December 31, 2001. The increase in working capital was substantially the result of our net income after adding back depreciation and amortization and partially offset by the acquisition of equipment.

In June 2001, we entered into a revolving credit and term loan agreement with Fleet Bank ("Fleet"). This financing provides us with a five-year term loan of $2.5 million, as well as a two-year $1.5 million revolving line of credit. The term loan bears interest at LIBOR plus 2.5%. We have entered into an interest rate swap agreement with Fleet whereby we converted our variable interest rate on the term loan to a fixed rate of 7.95%. The revolving line of credit bears interest, at the Company's option, to be equal to either (i) LIBOR plus 2.0% or (ii) the prime rate and incur an annual facility fee of 0.5%. Under our revolving line of credit, we can borrow up to 75% of eligible receivables up to a maximum of $1.5 million.

The maximum available to us at December 31, 2002 under the borrowing base formula was $1.5 million. The proceeds of the term loan are designated for acquisitions as well as for product enhancements specific to California requirements. The revolving line of credit is available for general working capital needs. We did not use the revolving line of credit from inception through December 31, 2002. We have made principal payments on the $2.5 million term loan and the amount outstanding at December 31, 2002 is $1.75 million.

The terms of our revolving credit and term loan agreement require compliance with certain covenants, including maintaining a minimum net equity of $9 million, minimum cash reserves of $500,000, maintenance of certain financial ratios, limitations on capital expenditures and indebtedness and prohibition of the payment of cash dividends. As of December 31, 2002, we were in compliance with the financial covenants of this agreement.

During 2001, we acquired the intellectual property, customer contracts and certain other assets of AIMS. The acquisition was accounted for under the purchase method of accounting. The principal assets acquired were the AIMS' customer base and the rights to AIMS' Correctional and Public Health Systems

software. The purchase price consisted of $500,000 in cash and 180,000 shares of our stock, valued at $376,200, which was the market price on the date of acquisition. In addition, pursuant to the terms of the acquisition agreement, on or before April 27,2004, we may be required to issue up to 100,000 additional shares of common stock based upon revenue derived from new contracts for the AIMS systems. The value of such shares, if issued, will be charged to operations. We also assumed certain contract obligations. We allocated $194, 986 of assumed contract obligations to the purchase price. The total cost of the acquisition, which included legal and accounting fees associated with the acquisition, was $1,161,100, of which $167,000 was allocated to software development and $994,100 was allocated to customer lists.

A part of our growth strategy is to acquire other businesses that are related to our current business. Such acquisitions may be made with cash or our securities or a combination of cash and securities. If we fail to make any acquisitions our future growth may be limited to only internal growth. As of the date of this Form 10-K annual report, we did not have any agreements or understandings with respect to any material acquisitions, and we cannot give any assurance that we will be able to complete any material acquisitions.

20

The following table summarizes, as of December 31, 2002, our obligations and commitments to make future payments under debt, capital leases and operating leases:

Contractual Obligations	Payments Due by Period				
	Total	Less than 1 year	1-3 years	4-5 years	Over 5 years
Long Term Debt(1)	1,750,012	500,000	1,000,000	250,012	--
Capital Lease Obligations(2)	12,609	10,808	1,801	--	--
Operating Leases(3)	593,000	473,000	120,000	--	--
Total Contractual Cash Obligations	2,355,621	983,808	1,121,801	250,012	--

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(1) See Note 7 to Netsmart's Consolidated Financial Statements for the years ended December 31, 2002, 2001 and 2000, which describes the Company's financing agreement.
(2) See Note 10 to Netsmart's Consolidated Financial Statements for the years ended December 31, 2002, 2001 and 2000, which describes the Company's Capital Lease Obligation.
(3) See Note 12 to Netsmart's Consolidated Financial Statements for the years ended December 31, 2002, 2001 and 2000, which describes the Company's Operating Lease Obligations.

Based on our outstanding contracts and our continuing business, we believe that our cash flow from operations, the availability under our financing agreement

and our cash on hand will be sufficient to enable us to fund our operations for at least the next twelve months. It is possible that we may need additional funding if we go forward with certain acquisitions or if our business does not develop as we anticipate or if our expenses, including our software development costs relating to our expansion of our product line and our marketing costs for seeking to expand the market for our products and services to include smaller clinics and facilities and sole group practitioners exceed our expectation.

Critical Accounting Policies and Estimates

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. These accounting principles require us to make certain estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions upon which we rely are reasonable based upon information available to us at the time that these estimates, judgments and assumptions are made. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities as of the date of the financial statements, as well as the reported amounts of revenues and expenses during the periods presented. To the extent there are material differences between these estimates, judgments or assumptions and actual results, our financial statements will be affected. The significant accounting policies that we believe are the most critical to aid in fully understanding and evaluating our reported financial results include the following:

Revenue Recognition
Impairment of Capitalized Software Development Costs
Impairment of Customer Lists

21

Revenue Recognition: Revenue associated with fixed price turnkey sales consists of the following components; licensing of software, labor associated with the installation and implementation of the software and maintenance services rendered in connection with such licensing activities. Revenue from fixed price software development contracts and revenue under license agreements, which require significant modification of the software package to the customer's specifications, are recognized on the estimated percentage-of-completion method. Using the units-of-work-performed method to measure progress towards completion, revisions in cost estimates and recognition of losses on these contracts are reflected in the accounting period in which the facts become known. The complexity of the estimation process and issues related to the assumptions, risks and uncertainties inherent with the application of the percentage of completion method of accounting affect the amounts of revenue and related expenses reported in our Consolidated Financial Statements. A number of internal and external factors can affect our estimates, including labor rates, utilization and efficiency variances and specification and testing requirement changes. Maintenance contract revenue is recognized on a straight-line basis over the life of the respective contract. We also derive revenue from the sale of third party hardware and software which is recognized based upon the terms of each contract. Consulting revenue is recognized when the services are rendered. Data Center revenue is recognized in the period in which the service is provided. The above sources of revenue are recognized when, persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed and determinable an collectibility is probable.

Contract terms provide for billing schedules that differ from revenue recognition and give rise to costs and estimated profits in excess of billings, and billings in excess of costs and estimated profits.

Deferred revenue represents revenue billed and collected but not yet earned.

The cost of maintenance revenue, which consists solely of staff payroll and applicable overhead, is expensed as incurred.

Impairment of Capitalized Software Development Costs - Capitalization of computer software development costs begins upon the establishment of technological feasibility. Technological feasibility for our computer software products are generally based upon achievement of a detail program design free of high risk development issues. The establishment of technological feasibility and the ongoing assessment of recoverability of capitalized computer software development costs requires considerable judgment by management with respect to certain external factors, including, but not limited to, technological feasibility, anticipated future gross revenue, estimated economic life and changes in software and hardware technology. Prior to reaching technological feasibility these costs are expensed as incurred and included in research and development. Amortization of capitalized computer software development costs commences when the related products become available for general release to customers. Amortization is provided on a product by product basis. The annual amortization is the greater of the amount computed using (a) the ratio that current gross revenue for a product bear to the total of current and anticipated future gross revenue for that product or (b) the straight-line method over the remaining estimated economic life of the product. The estimated life of these products range from 3 to 5 years.

We periodically perform reviews of the recoverability of such capitalized software costs. At the time a determination is made that capitalized amounts are not recoverable based on the estimated cash flows to be generated from the applicable software, any remaining capitalized amounts are written off.

Impairment of Customer Lists - Pursuant to Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", we evaluate our long-lived assets for financial impairment, and continue to evaluate them as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. We evaluate the recoverability of long-lived assets by measuring the carrying amount of the assets against the estimated undiscounted future cash flows associated with them. At the time such evaluations indicate that the future undiscounted cash flows of certain long-lived assets are not sufficient to recover the carrying amount of such assets, the assets are adjusted to their fair values.

Forward-Looking Statements

Statements in this Form 10-K annual report may be "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, but are not limited to, statements that express our intentions, beliefs, expectations, strategies, predictions or any other statements relating to our future activities or other future events or conditions. These statements are based on current expectations, estimates and projections about our business based, in part, on assumptions made by management. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may, and probably will, differ materially from what is expressed or forecasted in the forward-looking statements due to numerous factors, including those described above and those risks discussed from time to time in this Form 10-K annual report, including the risks described under "Risk Factors" and in other documents which we file with the Securities

and Exchange Commission. In addition, such statements could be affected by risks and uncertainties related to product demand, market and customer acceptance, competition, government regulations and requirements, pricing and development difficulties, as well as general industry and market conditions and growth rates, and general economic conditions. Any forward-looking statements speak only as of the date on which they are made, and we do not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date of this Form 10-K.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk related to changes in interest rates. Most of our debt is at fixed rates of interest after completing an interest rate swap agreement, which effectively converted our variable rate debt into a fixed rate debt of 7.95%. Therefore if the LIBOR plus 2.5% rate increases above 7.95%, it may have a positive effect on our net income.

Netsmart Technologies, Inc.
Quarterly Summary
Unaudited

The following table sets forth certain unaudited quarterly results of operations for each of the quarters in the years ended December 31, 2002 and 2001. All quarterly information was obtained from unaudited financial statements not otherwise contained in this report. We believe that all necessary adjustments have been made to present fairly the quarterly information when read in conjunction with the consolidated financial statements and notes thereto included elsewhere in this report. The operating results for any quarter are not necessary indicative of the results for any future period.

In thousands, except per share data amounts

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
2002 (a)				
Total revenue	$ 4,830	$ 5,447	$ 6,044	$ 5,805
Gross profit	1,685	1,843	1,880	2,174
Net income	103	142	202	748
Per share amounts:				
Net earnings - Basic:	$ .03	$ .04	$ .05	$ .19
Net earnings - Diluted:	$ .03	$ .04	$ .05	$ .18
2001				
Total revenue	$ 4,575	$ 4,665	$ 4,575	$ 4,304
Gross profit	1,482	1,577	1,486	1,573
Net income	65	70	50	130
Per share amounts:				
Net earnings - Basic:	$ 0.02	$ 0.02	$ 0.01	$ 0.04

Net earnings - Diluted:	$ 0.02	$ 0.02	$ 0.01	$ 0.03
	=======	======	=======	=======

(a) Includes the benefit of a net operating loss in the amount of $400 in the fourth quarter of 2002.

Earnings per share for each quarter are computed using the weighted-average number of shares outstanding during that quarter, while earnings per share for the full year are computed using the weighted-average number of shares outstanding during the year. Thus, the sum of the earnings per share for the four quarters' earnings per share may not equal the full-year earnings per share.

Item 8. Financial Statements and Supplementary Data

The financial statements and supplementary data begin on page F-1 of this Form 10-K.

Item 9. Changes and Disagreements with Accountants on Accounting and Financial Disclosure

On May 7, 2002, the audit committee of the board of directors recommended, and the board of directors approved, the dismissal of Eisner LLP (formerly Richard A. Eisner & Company, LLP), as our independent public accountants and the selection of Marcum & Kliegman LLP to serve as our independent public accountant for the year ending December 31, 2002. The selection of Marcum & Kliegman LLP was approved by our stockholders.

At no time since its engagement has Marcum & Kliegman LLP had any direct or indirect financial interest in or any connection with the Registrant or any of its subsidiaries other than as independent accountants.

The Company's financial statements for the years ended December 31, 2001 and 2000 were audited by Eisner LLP, whose report on such financial statements did not include any qualification, disclaimer, modification or explanatory paragraph. There were no disagreements with Eisner LLP during the years ended December 31, 2001 or 2000 or during the period subsequent to December 31, 2001 on any matter of accounting principles or practices, financial statement disclosure or auditing scope or procedure.

Part III

Item 10. Directors and Executive Officers of the Registrant.

Our directors and executive officers are as follows:

Name	Age	Position
James L. Conway	55	Chief executive officer and director
Gerald O. Koop	64	President and director
Anthony F. Grisanti	53	Chief financial officer, treasurer and secretary
John F. Phillips	65	Vice president and director
Joseph G. Sicinski(1 & 2)	70	Director
Edward D. Bright	66	Chairman of the board and director
Francis J. Calcagno(1 & 2)	53	Director

John S.T. Gallagher(1 & 2)   72   Director

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(1)   Member of the compensation committee.
(2)   Member of the audit committee.

Mr. James L. Conway has been our chief executive office since April 1998, a director since January 1996 and president from January 1996 until January 2001. From 1993 until April 1998, he was president of a Long Island based manufacturer of specialty vending equipment for postal, telecommunication and other industries. He was previously vice president and treasurer of ITT Credit Corporation.

Mr. Gerald O. Koop has been one of our directors since June 1998 and president since January 2001. He has held management positions with Creative Socio-Medics for more than the past five years, most recently as its chief executive officer, a position he has held since 1996.

25

Mr. John F. Phillips has been one of our directors and president of Creative Socio-Medics since June 1994, when Creative Socio-Medics was acquired, and our vice president since June 1994.

Mr. Joseph G. Sicinski has been one of our directors since June 1998. He is president and a director of the Trans Global Services, Inc., a technical staffing company, a position he held with Trans Global and its predecessor since September 1992. From April 1998 until December 2001, he was also chief executive officer of Trans Global.

Mr. Edward D. Bright has been our chairman of the board and a director since April 1998. From April 1998 until 1999, Mr. Bright was chairman, secretary, treasurer and a director of Consolidated Technology Group Ltd., a public company now known as The Sagemark Companies, Ltd. In 2000, Mr. Bright was reelected chairman of the board and a director of Sagemark. From January 1996 until April 1998, Mr. Bright was an executive officer of or advisor to Creative Socio-Medics Corp., our wholly-owned subsidiary.

Mr. Francis J. Calcagno has been one of our directors since September 2001. He is a senior managing director of Dominick & Dominick LLC, a position he has held since 1997. From 1993 until 1997, he was a managing director of Deloitte and Touche, LLP.

Mr. John S.T. Gallagher has been one of our directors since March 2002. He is deputy county executive for health and human services in Nassau County, New York. He has been a senior executive officer of North Shore University Hospital and North Shore - Long Island Jewish Health System since 1982, having served as executive vice president of North Shore from 1982 until 1992, president from 1992 until 1997 and chief executive officer of the combined hospital system from 1997 until January 2002. In January 2002, he became co-chairman of the North Shore - Long Island Jewish Heath System Foundation. Mr. Gallagher is also a director of Perot Systems Corporation, a worldwide provider of information technology services.

Directors are elected for a term of one year.

None of our officers and directors are related.
Our board of directors has two committees - the audit committee and the compensation committee.

The audit committee consists of three independent directors, Messrs. Francis J. Calcagno, who is chairman of the committee, John S.T. Gallagher and Joseph G. Sicinski. The responsibilities of the audit committee is to oversee our financial reporting process, report the results of its activities to the board, approve the selection of the independent auditors, review our periodic filings with the independent auditors prior to filing, and review and respond to any matters raised by the independent auditors in their management letter. The board of directors has determined that at least one member of the audit committee, Mr. Calcagno, is an audit committee financial expert. Mr. Calcagno is an independent director as defined in the rule of the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934.

The compensation committee, which is composed of Messrs. Calcagno, Gallagher and Sicinski, serves as the stock option committee for our stock option plans and the employee stock purchase plan, and it reviews and approves any employment agreements with management and changes in compensation for our executive officers.

Excluding actions by unanimous written consent, during 2002, the board of directors held two meetings, the compensation committee held one meeting, and the audit committee held four meetings. The audit committee met with our independent accountants and chief financial officer prior to filing of this Form 10-K annual report to review the 2002 audited financial statements with the independent auditors. During 2002, all of our directors attended at least 80% of the meetings of the board and any committee of which they are members.

We pay a monthly fee of $1,250 to Mr. Calcagno, $750 to Mr. Sicinski and $2,000 to Mr. Gallagher and we pay the chairman of the board a monthly fee of $1,500.

Our certificate of incorporation includes certain provisions, permitted under Delaware law, which provide that a director shall not be personally liable to us or our stockholders for monetary damages for breach of fiduciary duty as a director except for liability (i) for any breach of the director's duty of loyalty to us or our stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) for any transaction from which the director derived an improper personal benefit, or (iv) for certain conduct prohibited by law. The Certificate of Incorporation also contains broad indemnification provisions. These provisions do not affect the liability of any director under federal or applicable state securities laws.

Compliance with Section 16(a) of the Securities Exchange Act

Section 16(a) of the Securities Exchange Act of 1934 requires our executive officers, directors and persons who own more than ten percent of a registered class of our equity securities ("Reporting Persons") to file reports of ownership and changes in ownership on Forms 3, 4 and 5 with the Securities and Exchange Commission and the Nasdaq Stock Exchange. These Reporting Persons are required by SEC regulation to furnish us with copies of all Forms 3, 4 and 5 they file with the SEC and Nasdaq. Based solely upon our review of the copies of the forms we have received, we believe that all Reporting Persons complied on a timely basis with all filing requirements applicable to them with respect to transactions during fiscal 2002, except that John Phillips filed 38 days late for a filing due December 10, 2002 and 36 days late for a filing due December 12, 2002.

Item 11. Executive Compensation.

Set forth below is information with respect to compensation paid or accrued by us for 2002, 2001 and 2000 to our chief executive officer and to each of our other officers whose salary and bonus for 2002 exceeded $100,000.

SUMMARY COMPENSATION TABLE

		Annual Compensation		Long-Term Compensation (Awards)
Name and Principal Position	Year	Salary	Bonus	Options, SARs (Number)
James L. Conway, CEO	2002	$193,151	$120,000	20,000
	2001	182,239	61,261	--
	2000	177,120	102,515	21,000
Gerald O. Koop, president	2002	170,807	170,408	20,000
	2001	160,959	97,874	--
	2000	156,480	139,269	21,000
John F. Phillips, vice president	2002	170,807	60,000	15,000
	2001	160,959	41,041	--
	2000	156,480	83,973	18,750
Anthony F. Grisanti, chief financial officer	2002	148,463	106,000	16,000
	2001	139,679	65,821	--
	2000	135,840	104,656	18,750

The bonuses for Mr. Koop includes accrued commissions of $165,408 for 2002, $82,874 for 2001 and $94,568 for 2000. These commissions will be paid in installments through 2003.

In January 2001, we entered into employment agreements with Messrs. James L. Conway, John F. Phillips, Gerald O. Koop and Anthony F. Grisanti for a term of three years for Messrs. Conway and Grisanti and two years for Messrs. Koop and Phillips. We believe that these officers are vital to our business. Each of the officers has the right to extend the term for an additional year. Following termination of the employment term, or earlier at the discretion of the officer, each of the officers has the right to continue as a part-time consultant for a term of five years for annual compensation of $75,000. Pursuant to these employment agreements, these officers received the following salaries in 2002: Mr. Conway - $178,751, Mr. Koop - $156,407, Mr. Phillips - $156,407, and Mr. Grisanti - $134,063. The agreements provide for annual increases associated with cost of living indexes. The agreements provide that the executives are eligible to participate in a bonus pool to be determined annually by the board, based on the executive's performance. The agreements also provide each of these officers with an automobile allowance, which is included under "Salary", and insurance benefits. In the event of the officer's dismissal or resignation or a material change in his duties or in the event of a termination of employment by the executive or by us as a result of a change of control, the officer may receive severance payments of between 30 and 36 months' compensation. In January 2001, we entered into a consulting agreement with Mr. Bright - see Item 13, Certain Relationships and Related Transactions.

Compensation Committee Interlocks and Insider Participation

During fiscal 2002, our compensation committee consisted of Messrs. Clacagno, Gallagher and Sincinski. None of them were our officers or employees during fiscal 2002 nor did any of them have any relationship with us that is required to be disclosed under this heading.

Option Exercises and Outstanding Options

The following table sets forth information concerning the grants of options made during the year.

Options / SAR Grants in Last Fiscal Year

	Individual Grants			
Name	Number of Securities Underlying Options / SARS Granted # (1)	% of Total Options / SARS Granted to Employees in Fiscal Year (2)	Exercise or Base Price ($/Sh) (3)	Expiration Da
James L. Conway, CEO	20,000	11.2%	$2.50	3/11/08
Gerald O. Koop, President	20,000	11.2%	$2.50	3/11/08
John F. Phillips, Vice President	15,000	8.4%	$2.50	3/11/08
Anthony F. Grisanti, CFO	16,000	9.0%	$2.50	3/11/08

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(1) Includes options granted during fiscal 2002.

(2) Based on a total of 178,500 shares subject to options granted to employees under Netsmart's option plans in 2002.

(3) Under all stock option plans, the option purchase price is equal to the fair market value at the date of the grant. Options were granted to executives on March 11, 2002.

(4) In accordance with U.S. Securities and Exchange Commission rules, these columns show gain that could accrue for the respective options, assuming that the market price of Netsmart common stock appreciates from the date of grant over a period of 6 years at an annualized rate of 5% and 10%, respectively. If the stock price does not increase above the exercise price at the time of exercise, realized value to the named executives from these options will be zero.

The following table sets forth information concerning the exercise of options during the year ended December 31, 2002 and the year-end value of options held by our officers named in the Summary Compensation Table. No stock appreciation rights have been granted.

Aggregate Option Exercises in Last Fiscal Year and Fiscal Year-End Option Value
(All options were fully exercisable at year end)

Name	Shares Acquired Upon Exercise	Value Realized	Number of Securities Underlying Unexercised Options at Fiscal Year End	Value of Unexercised In-the-Money Options at Fiscal Year End
James L. Conway	21,000	$62,769	68,250	$ 43,380
Gerald O. Koop	21,000	$62,769	100,000	321,900
John F. Phillips	30,000	$140,100	83,750	269,591
Anthony F. Grisanti	5,052	$18,339	34,750	88,310

The determination of "in the money" options at December 31, 2002, is based on the closing price of the common stock on the Nasdaq SmallCap Market on December 31, 2002, which was $4.67 per share.

The options held by Mr. Conway include warrants, exercisable at $12.00 per share, held by Mr. Conway (34,000 shares) and Mr. Conway's wife (14,250 shares). Mr. Conway disclaims beneficial interest in securities held by his wife. These warrants are scheduled to expire on April 30, 2003, unless they are extended by the Company.

Information relating to securities issued under equity compensation plans is disclosed in response to "Item 5. Market for Registrant's Common Equity and Related Stockholder Matters".

29

Item 12. Security Ownership of Certain Beneficial Owners and Management.

Set forth below is information as of January 1, 2003, as to each person owning of record or known by us, based on information provided to us by the persons named below and filings with the Securities and Exchange Commission, to own beneficially at least 5% of our common stock, each director, each officer listed in the Summary Compensation Table and all officers and directors as a group.

Name and Address	Shares	Percent of Outstanding Common Stock

John F. Phillips 146 Nassau Avenue Islip, New York 11751	221,427	5.5%
Edward D. Bright	198,172	4.9%
Gerald O. Koop	179,665	4.4%
James L. Conway	178,717	4.4%
Anthony F. Grisanti	134,815	3.4%
Joseph G. Sicinski	25,000	*
Francis J. Calcagno	5,000	*
John S.T. Gallagher	20,000	*
All directors and officers as a group (seven individuals)	962,796	22.0%

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* Less than 1%.

Except as set forth in the following paragraphs, each person has the sole voting and sole investment power and direct beneficial ownership of the shares. Each person is deemed to beneficially own shares of common stock issuable upon exercise of options or warrants which are exercisable on or within 60 days after the date as of which the information is provided.

The number of shares owned by our directors and officers shown in the table includes shares of common stock which are issuable upon exercise of options and warrants that are exercisable at December 31, 2002 or will become exercisable within 60 days after that date. Set forth below is the number of shares issuable upon exercise of those options and warrants for each of our directors and the officers named in the Summary Compensation Table.

Name	Number
John F. Phillips	83,750
Edward D. Bright	96,250
Gerald O. Koop	100,000
James L. Conway	68,250
Anthony F. Grisanti	34,750
All officers and directors as a group	413,000

The options and warrants held by Mr. Conway include warrants, exercisable at $12.00 per share, to purchase 34,000 held by Mr. Conway and 14,250 shares held by Mr. Conway's wife, as to which he disclaims beneficial ownership. These warrants are scheduled to expire on April 30, 2003.

Item 13. Certain Relationships and Related Transactions.

In August 2001, we entered into an non exclusive investment banking agreement Dominick & Dominick, Inc., of which Mr. Francis J. Calcagno, one of our directors, is a senior managing director. Mr. Calcagno was not a director at the time we entered into this agreement with Dominick & Dominick. Dominick & Dominick holds warrants to purchase 100,000 shares of common stock at an exercise price of $5.45 per share. These warrants were issued pursuant to a nonexclusive investment banking agreement dated September 8, 1999. During 2002, this non exclusive investment banking agreement was terminated.

We entered into a consulting agreement with Mr. Bright dated January 1, 2001, pursuant to which Mr. Bright is to devote 50% of his time to our business

for a period of two years, with Mr. Bright having the right to extend the term for an additional year. Following the completion of the term, or earlier at the discretion of Mr. Bright, Mr. Bright continues as a consultant for an additional five years. Mr. Bright receives compensation at the annual rate of $75,000 during the consulting term, and we provide him with an automobile allowance and insurance benefits. Mr. Bright is eligible, at the discretion of the board, to participate in a bonus pool which may be established by the board. In the event that Mr. Bright's consultant relationship is terminated as a result of a change of control, we are to pay him as severance pay between 30 and 36 months compensation. We paid Mr. Bright total compensation of $87,000 for 2002, in addition to a bonus of $5,000.

Item 14. Controls and Procedures

Within the 90-day period prior to the filing of this annual report, an evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures to Exchange Act Rule 13a-14. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation.

31

Part IV

Item 15. Exhibits, Financial Statements Schedules and Reports on Form 8-K.

32

1. Financial Statements
   Report of Marcum & Kliegman LLP
   Report of Eisner LLP
   Consolidated Balance Sheets as of December 31, 2002 and 2001
   Consolidated Statements of Income for the Years Ended December 31, 2002, 2001 and 2000 Consolidated Statements of Stockholders' Equity for the Years Ended December 31, 2002, 2001 and 2000
   Consolidated Statements of Cash Flows for the Years Ended December 31, 2002, 2001 and 2000
   Notes to Consolidated Financial Statements

2. Financial Statement Schedules
   None

3. Reports on Form 8-K
   None

4. Exhibits
   3.1(1) Restated Certificate of Incorporation, as amended
   3.2(1) By-Laws
   10.1(2) Employment Agreement dated January 1, 2001, between the Registrant and James L. Conway.

10.2(2)	Employment Agreement dated January 1, 2001, between the Registrant and John F. Phillips.
10.3(2)	Employment Agreement dated January 1, 2001, between the Registrant and Gerald O. Koop.
10.4(2)	Employment Agreement dated January 1, 2001, between the Registrant and Anthony F. Grisanti.
10.5(2)	Consulting Agreement dated January 1, 2001, between the Registrant and Edward D. Bright
10.6(1)	1993 Long-Term Incentive Plan.
10.7(3)	1998 Long-Term Incentive Plan.
10.8(4)	1999 Long-Term Incentive Plan.
10.9(5)	2001 Long-Term Incentive Plan.
10.10(4)	1999 Employee Stock Purchase Plan
10.11(2)	Agreement dated June 1, 2001, between the Registrant and Fleet Bank.
10.12(6)	AIMS Acquisition Agreement
21.1	Subsidiaries of the Registrant.
23.1	Independent Auditors' Consent
25.1	Powers of attorney (See Signature Page)

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(1) Filed as an exhibit to the Registrant's registration statement on Form S-1, File No. 333-2550, which was declared effective by the Commission on August 13, 1996, and incorporated herein by reference.

(2) Filed herewith.

(3) Filed as an appendix to the Registrant's proxy statement dated September 30, 1999, relating to its 1999 Annual Meeting of Stockholders and incorporated herein by reference.

(4) Filed as an appendix to the Registrant's proxy statement dated November 9, 2000, relating to its 2000 Annual Meeting of Stockholders and incorporated herein by reference.

(5) Filed as an appendix to the Registrant's proxy statement dated November 14, 2002, relating to its 2002 Special Meeting of Stockholders held on January 9, 2003 and incorporated herein by reference.

(6) Filed as an exhibit to the Registrant's 8-K dated May 10, 2001.

NETSMART TECHNOLOGIES, INC.
AND SUBSIDIARIES

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

INDEX

Page to Page

Independent Auditors' Report - Marcum & Kliegman LLP..............F-3

Independent Auditors' Report - Eisner, LLP........................F-4

Consolidated Balance Sheets.......................................F-5......F-6

Consolidated Statements of Income.................................F-7......F-8

Consolidated Statements of Stockholders' Equity...................F-9

Consolidated Statements of Cash Flows.............................F-10.....F-12

Notes to Consolidated Financial Statements ....F-13.....F-30

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INDEPENDENT AUDITORS' REPORT

Board of Directors and Stockholders of
Netsmart Technologies, Inc.

We have audited the accompanying consolidated balance sheet of Netsmart Technologies, Inc. and subsidiaries as of December 31, 2002 and the related consolidated statements of income, stockholders' equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Netsmart Technologies, Inc. and its subsidiaries as of December 31, 2002, and the consolidated results of their operations and their consolidated cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/*

Marcum & Kliegman LLP

Woodbury, New York
February 3, 2003

INDEPENDENT AUDITORS' REPORT

Board of Directors and Stockholders of
Netsmart Technologies, Inc.

We have audited the accompanying consolidated balance sheet of Netsmart Technologies, Inc. and subsidiaries as of December 31, 2001 and the related consolidated statements of income, stockholders' equity and cash flows for each of the years in the two year period ended December 31, 2001. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements enumerated above present fairly, in all material respects, the consolidated financial position of Netsmart Technologies, Inc. and its subsidiaries as of December 31, 2001, and the consolidated results of their operations and their consolidated cash flows for each of the years in the two year period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States of America.

/s/*

Eisner LLP
(formerly Richard A. Eisner & Company LLP)

New York, New York
February 15, 2002

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	December 31, 2002	December 31, 2001
Assets:		
Current Assets:		
Cash and Cash Equivalents	$ 7,251,740	$ 3,837,226
Accounts Receivable - Net	7,058,855	5,876,970
Costs and Estimated Profits in Excess of Interim Billings	3,857,522	3,783,356
Deferred taxes	900,000	500,000
Other Current Assets	196,577	128,232

Total Current Assets	19,264,694	14,125,784
Property and Equipment - Net	364,306	366,356
Other Assets:		
Software Development Costs - Net	382,387	686,301
Customer Lists - Net	2,141,855	2,618,145
Other Assets	121,419	210,787
Total Other Assets	2,645,661	3,515,233
Total Assets	$22,274,661	$18,007,373

See Notes to Consolidated Financial Statements.

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	December 31,	
	2002	2001
Liabilities and Stockholders' Equity:		
Current Liabilities:		
Current Portion - Long Term Debt	$ 500,000	$ 500,000
Current Portion Capital Lease Obligations	9,886	28,905
Accounts Payable	1,166,145	688,682
Accrued Expenses	922,417	359,908
Interim Billings in Excess of Costs and Estimated Profits	5,914,970	3,959,230
Deferred Revenue	1,095,412	685,569
Total Current Liabilities	9,608,830	6,222,294
Capital Lease Obligations - Less current portion	1,864	12,519
Long Term Debt - Less current portion	1,250,012	1,750,004
Interest Rate Swap at Fair Value	107,713	74,875
Total Non Current Liabilities	1,359,589	1,837,398
Commitments and Contingencies		
Stockholders' Equity:		

Preferred Stock - $.01 Par Value, 3,000,000 Shares Authorized; None issued and outstanding	--	--
Common Stock - $.01 Par Value; Authorized 15,000,000 Shares; Issued 4,046,430 shares at December 31, 2002, 3,719,247 shares at December 31, 2001	40,464	37,192
Additional Paid in Capital	21,411,777	20,856,166
Unearned Compensation	(14,400)	--
Accumulated Comprehensive loss - Interest Rate Swap	(107,713)	(74,875)
Accumulated Deficit	(9,375,774)	(10,570,992)
	11,954,354	10,247,491
Less: cost of shares of Common Stock held in treasury - 89,797 at December 31, 2002 and 28,038 shares at December 31, 2001	648,112	299,810
Total Stockholders' Equity	11,306,242	9,947,681
Total Liabilities and Stockholders' Equity	$22,274,661	$ 18,007,373

See Notes to Consolidated Financial Statements.

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

	Year ended December 31,		
	2002	2001	2000
Revenues:			
Software and Related Systems and Services:			
General	$13,921,449	$10,885,337	$14,387,256
Maintenance Contract Services	6,247,336	5,191,986	3,520,717
Total Software and Related Systems and Services	20,168,785	16,077,323	17,907,973
Data Center Services	1,957,392	2,042,098	2,262,676
Total Revenues	22,126,177	18,119,421	20,170,649
Cost of Revenues:			
Software and Related			

Systems and Services:			
General	10,184,637	7,367,949	8,645,275
Maintenance Contract Services	3,348,217	3,614,336	2,285,663
Total Software and Related Systems and Services	13,532,854	10,982,285	10,930,938
Data Center Services	1,011,602	1,018,950	1,024,523
Total Cost of Revenues	14,544,456	12,001,235	11,955,461
Gross Profit	7,581,721	6,118,186	8,215,188
Selling, General and Administrative Expenses	5,168,184	4,384,291	4,714,829
Research and Development	1,318,124	1,334,577	1,359,781
Total	6,486,308	5,718,868	6,074,610
Income from Continuing Operations before Interest Expense	1,095,413	399,318	2,140,578
Interest and Other Income	46,115	71,742	--
Interest and Other Expense	262,310	186,638	161,386
Income from Continuing Operations before Income Tax (Benefit)	879,218	284,422	1,979,192
Income Tax (Benefit)	(316,000)	(31,000)	(336,827)
Income from Continuing Operations	1,195,218	315,422	2,316,019

See Notes to Consolidated Financial Statements.

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

	Year ended December 31,		
	2002	2001	2000
Discontinued Operations:			
Gain on Sale of Discontinued Operations	--	--	70,000

Net Income	$1,195,218	$ 315,422	$2,386,019
Earnings Per Share of Common Stock:			
Basic:			
Income from Continuing Operations	$ .32	$ .09	.69
Income from Discontinued Operations	--	--	.02
Net Income	$ .32	$ .09	$ .71
Weighted Average Number of Shares of Common Stock Outstanding	3,748,537	3,618,260	3,367,005
Diluted:			
Income from Continuing Operations	$ .29	$ .08	$ .61
Income from Discontinued Operations	--	--	.02
Net Income	$ .29	$ .08	$ .63
Weighted Average Number of Shares of Common Stock and Common Stock Equivalents Outstanding	4,153,484	3,871,876	3,770,992

See Notes to Consolidated Financial Statements.

F-8

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Common Stock		Additional Paid-in Capital			Accumulated Comprehensive Loss	
	Shares	Amount	Common Stock	Unearned Compensation	Accumulated Deficit	Interest Rate Swap	Comprehensi Income
Balance - January 1, 2000	2,988,738	$29,887	$18,657,579	$ --	$(13,272,433)	$ --	$ --
Common Stock							

Issued - Exercise of Options	328,321	3,283	378,258	--	--	--	--
Common Stock Issued - Exercise of Warrants	192,105	1,921	1,137,709	--	--	--	--
Common Stock Issued - Acquisition	15,528	155	99,845	--	--	--	--
Issuance and Extension of Warrants	--	--	181,000	--	--	--	--
Net Income	--	--	--	--	2,386,019	--	2,386,019
							$2,386,019
Balance - December 31, 2000	3,524,692	35,246	20,454,391	--	(10,886,414)	--	$ --
Common Stock Issued - Exercise of Options	14,555	146	21,688	--	--	--	--
Common Stock Issued - Acquisition	180,000	1,800	374,400	--	--	--	--
Issuance and Extension of Warrants	--	--	5,687	--	--	--	--
Change in Fair Value of Interest Rate Swap	--	--	--	--	--	(74,875)	(74,875)
Net Income	--	--	--	--	315,422	--	315,422
							$ 240,547
Balance - December 31, 2001	3,719,247	37,192	20,856,166	--	(10,570,992)	(74,875)	
Common Stock Issued - Exercise of Options	327,183	3,272	501,938	--	--	--$	--
Issuance of Warrants and Options	--	--	53,673	(14,400)	--	--	--
Change in Fair Value of Interest Rate Swap	--	--	--	--	--	(32,838)	(32,838)

Net Income	--	--	--	--	1,195,218	--	1,195,218
							$1,162,380
Balance - December 31, 2002	4,046,430	$40,464	$21,411,777	$(14,400)	$(9,375,774)	$(107,713)	

See Notes to Consolidated Financial Statements.

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
	2002	2001	2000
Operating Activities:			
Income from Continuing Operations	$ 1,195,218	$ 315,422	$ 2,316,019
Adjustments to Reconcile Income from Continuing Operations to Net Cash Provided by Operating Activities:			
Depreciation and Amortization	1,036,721	1,010,821	717,776
Costs Related to Issuance of warrants and options for services	39,273	5,687	181,000
Provision for Doubtful Accounts	370,000	340,000	330,000
Changes in Assets and Liabilities:			
[Increase] Decrease in:			
Accounts Receivable	(1,551,885)	(1,528,372)	771,136
Costs and Estimated Profits in Excess of Interim Billings	(74,166)	284,899	184,817
Deferred Taxes	(400,000)	(6,000)	(494,000)
Other Current Assets	(68,345)	16,710	22,574
Other Assets	89,368	(124,574)	76,259
Increase [Decrease] in:			
Accounts Payable	477,463	(118,616)	(1,754,789)
Accrued Expenses	562,509	(794,739)	(88,901)
Interim Billings in Excess of Costs and Estimated Profits	1,955,740	413,547	(400,150)
Deferred Revenue	409,843	77,125	519,898
Total Adjustments	2,846,521	(423,512)	65,620
Net Cash Provided (Used In) by Operating Activities	4,041,739	(108,090)	2,381,639

Investing Activities:			
Acquisition of Property and Equipment	(254,467)	(120,765)	(223,491)
Net Cost of AIMS Acquisition	--	(589,914)	--
Software Development Costs	--	--	(536,100)
Cash Provided by Discontinued Operations	--	--	220,000
Net Cash Used In Investing Activities	(254,467)	(710,679)	(539,591)

See Notes to Consolidated Financial Statements.

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
	2002	2001	2000
Financing Activities:			
Payment of Short-Term Notes	--	--	(882,404)
Proceeds from Term Loan	--	2,500,000	
Payment of Capitalized Lease Obligations	(29,674)	(34,790)	(27,047)
Net Proceeds from Warrant Exercise	--	--	1,139,630
Net Proceeds from Stock Option Exercise	156,908	21,834	141,731
Payments of Term Loan	(499,992)	(249,996)	--
Net Cash (Used in) Provided by Financing Activities	(372,758)	2,237,048	371,910
Net Increase in Cash and Cash Equivalents	3,414,514	1,418,279	2,213,958
Cash and Cash Equivalents - Beginning of Year	3,837,226	2,418,947	204,989
Cash and Cash Equivalents - End of Year	$7,251,740	$3,837,226	$2,418,947
Supplemental Disclosure of Cash Flow Information:			
Cash paid during the years for:			
Interest	$ 167,542	$ 135,566	$ 172,556
Income Taxes	$ 41,517	$ 87,859	$ 157,173

Supplemental Disclosures of Non-Cash Investing and Financing Activities:

Year ended December 31, 2002:

During 2002, stock options to purchase 327,183 shares of common stock were

exercised and proceeds of $505,210 includes $348,302, representing the market value of the Company's common stock which was received for the exercise price of certain of these options.

The fair value of the interest rate swap calculated at December 31, 2002 was $107,713.

Year ended December 31, 2001:

The Company issued 180,000 shares of common stock related to the AIMS acquisition. These shares were valued at $376,200 which was the market value at the date of grant. The Company also recorded a liability of $194,986 for contract obligations assumed.

The fair value of the interest rate swap calculated at December 31, 2001 was $74,875.

Year ended December 31, 2000:

The Company issued 15,528 shares of common stock to acquire the Connex suite of managed care and employee assistance program information systems software. These shares were valued at $100,000 which was the market value on date of issuance.

During 2000, stock options to purchase 328,321 shares of common stock were exercised and proceeds of $381,541 includes $239,810, representing the market value of 22,705 shares of the Company's common stock which was received for the exercise price of certain of these options.

During 2000, the Company entered into a capitalized lease obligation to purchase equipment in the amount of $13,249.

See Notes to Consolidated Financial Statements

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, Sheet #1

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[1] The Company

Netsmart Technologies, Inc. and subsidiaries (the "Company") licenses and installs its proprietary software products, operates an established service bureau and enters into long term maintenance agreements with behavioral health and public health organizations, methadone clinics and other substance abuse facilities throughout the United States.

During 2001, the Company acquired the intellectual property, customer contracts and certain other assets of Advanced Institutional Management Systems ("AIMS"). The acquisition was accounted for under the purchase method of accounting. The principal assets acquired were the AIMS customer base and the rights to AIMS Correctional and Public Health Systems software. The purchase price consisted of 180,000 shares of the Company's common stock, valued at $376,200 and $500,000 cash. In addition, the Company may issue up to 100,000 additional shares of common stock, based on revenue derived through April 2004 from new contracts for the AIMS systems. The value of such shares, if issued, will be charged to

operations. The Company also assumed certain contract obligations. The Company has allocated $194,986 of assumed contract obligations to the purchase price. The cost of the acquisition was $1,161,100, of which $167,000 was allocated to software development and $994,100 to customer lists. The Company is amortizing the purchased software over a three-year life and the customer lists over a seven-year life.

[2] Summary of Significant Accounting Policies

Principles of Consolidation - The consolidated financial statements include Netsmart Technologies, Inc. ("Netsmart"), and its wholly-owned subsidiary, Creative Socio-Medics Corp. ("CSM"). In addition, the results of operations from the AIMS acquisition is included from May 2001. All intercompany transactions are eliminated in consolidation. Netsmart owned an 80% interest in a joint venture, PsyMedX. No minority interest related to the joint venture has been recorded, since the joint venture partner was in breach of the joint venture agreement and in 2001 ceased to exist.

Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents - The Company considers all highly liquid instruments purchased with a maturity of three months or less to be cash equivalents. Cash equivalents totaled approximately $2,064,000 and $2,035,000 at December 31, 2002 and 2001 respectively.

Concentration of Credit Risk - The Company extends credit to customers which results in accounts receivable arising from its normal business activities. The Company does not require collateral or other security to support financial instruments subject to credit risk. The Company routinely assesses the financial strength of its customers and based upon factors surrounding the credit risk of the customers believes that its accounts receivable credit risk exposure is limited.

The Company's behavioral health information systems are marketed to specialized care facilities, many of which are operated by government entities and include entitlement programs. During the years ended December 31, 2002, 2001 and 2000, approximately 52%, 40% and 51% respectively, of the Company's revenue were generated from contracts directly or indirectly with government agencies.

During the years ended December 31, 2002, 2001 and 2000, no one customer accounted for more than 10% of revenue.

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[2] Summary of Significant Accounting Policies - [Continued]

The Company places its cash and cash equivalents with high credit quality financial institutions. The amount on deposit in any one institution that exceeds federally insured limits is subject to credit risk. At December 31, 2002 and 2001, cash and cash equivalent balances of $7.1 million and $3.6 million respectively, were held at a financial institution in excess of federally

insured limits.

Revenue Recognition - The Company recognizes revenue principally from the licensing of its software and maintenance services rendered in connection with such licensing activities. Information processing revenue is recognized in the period in which the service is provided. Maintenance contract revenue is recognized on a straight-line basis over the life of the respective contract. The Company also derives revenue from the sale of third party hardware and software which is recognized based upon the terms of each contract. The above sources of revenue which do not require significant customization or modification are recognized when, persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed and determinable and collectibility is probable. In addition, consulting revenue is recognized when the services are rendered.

Software development revenue from time-and-materials contracts, which require customization and modification, are recognized as services are performed. Revenue from fixed price software development contracts and revenue under license agreements which require significant modification of the software package to the customer's specifications, are recognized on the estimated percentage-of-completion method. Progress towards completion on a contract is measured using the units of work performed method. Revisions in cost estimates and recognition of losses on these contracts are reflected in the accounting period in which the facts become known. Contract terms provide for billing schedules that differ from revenue recognition and give rise to costs and estimated profits in excess of billings, and billings in excess of costs and estimated profits.

Deferred revenue represents revenue billed and collected but not yet earned.

The cost of maintenance revenue, which consists solely of staff payroll and applicable overhead, is expensed as incurred.

Property and Equipment and Depreciation - Property and equipment is stated at cost less accumulated depreciation. Depreciation of property and equipment is computed using the straight-line method at rates adequate to allocate the cost of applicable assets over their expected useful lives. Amortization of leasehold improvements is computed using the shorter of the lease term or the expected useful life of these assets.

Estimated useful lives are as follows:

Equipment	3-5 Years
Furniture and Fixtures	5 Years
Leasehold Improvements	2-5 Years

Capitalized Software Development Costs - Capitalization of computer software development costs begins upon the establishment of technological feasibility. Technological feasibility for the Company's computer software products is generally based upon achievement of a detail program design free of high risk development issues. The establishment of technological feasibility and the ongoing assessment of recoverability of capitalized computer software development costs requires considerable judgment by management with respect to certain external factors, including, but not limited to, technological feasibility, anticipated future gross revenue, estimated economic life and changes in software and hardware technology. Prior to reaching technological feasibility these costs are expensed as incurred and included in research and development. Amortization of capitalized computer software development costs commences when the related products become available for general release to customers. Amortization is provided on a product by product basis. The annual

amortization is the greater of the amount computed using (a) the ratio that current gross revenue

[2] Summary of Significant Accounting Policies - [Continued]

for a product bear to the total of current and anticipated future gross revenue for that product or (b) the straight-line method over the remaining estimated economic life of the product. The estimated life of these products range from 3 to 5 years.

The Company periodically performs reviews of the recoverability of such capitalized software costs. At the time a determination is made that capitalized amounts are not recoverable based on the estimated cash flows to be generated from the applicable software, any remaining capitalized amounts are written off.

During 2000, the Company acquired the Connex suite of managed care and employee assistance program information systems. The acquisition price consisted of approximately $47,000 in cash and 15,528 shares of Netsmart's common stock valued at $100,000. The purchase price was allocated to computer software in the amount of $147,000. During 2000, the Company made additional enhancements to the purchased software in the amount of $270,000. As of December 31, 2002, the Company has invested approximately $417,000 on this effort of which $170,000 was unamortized.

Information related to capitalized software costs applicable to continuing operations is as follows:

Year ended December 31,	2002	2001	2000
Beginning of Year	$ 686,301	$ 822,645	$ 310,722
Capitalized	--	167,000	636,100
Amortization	(303,914)	(303,344)	(124,177)
Net	$ 382,387	$ 686,301	$ 822,645

Customer Lists - Customer lists represent a listing of customers obtained through the acquisitions of CSM, Johnson and AIMS to which the Company can market its products. Customer lists are being amortized on the straight-line method over an estimated useful life of 12 years for the CSM and Johnson lists and 7 years for the AIMS list.

Customer lists at December 31, 2002 and 2001 are as follows:

	December 31,	
	2002	2001
Customer Lists	$5,100,323	$5,100,323
Less: Accumulated Amortization	2,958,468	2,482,178
Net	$2,141,855	$2,618,145

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Amortization expense amounted to $476,290, $440,787 and $334,276, respectively, for the years ended December 31, 2002, 2001 and 2000.

Pursuant to Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of", the Company evaluates its long-lived assets for financial impairment, and continues to evaluate them as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable.

The Company evaluates the recoverability of long-lived assets by measuring the carrying amount of the assets against the estimated undiscounted future cash flows associated with them. At the time such evaluations indicate that the future undiscounted cash flows of certain long-lived assets are not sufficient to recover the carrying value of such assets, the assets are adjusted to their fair values. The

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[2] Summary of Significant Accounting Policies - [Continued]

provisions of these interpretations that are applicable to the Company were implemented on a prospective basis as of January 1, 2002, which had no material effect on the Company's consolidated financial position or results of operations.

Stock Options and Similar Equity Instruments - At December 31, 2002, the Company had three stock-based employee compensation plans, which are described more fully in Note 13. As permitted under SFAS No. 148, "Accounting for Stock-Based Compensation--Transition and Disclosure", which amended SFAS No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation", the Company has elected to continue to follow the intrinsic value method in accounting for its stock-based employee compensation arrangements as defined by Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees", and related interpretations including "Financial Accounting Standards Board Interpretation No. 44, Accounting for Certain Transactions Involving Stock Compensation", an interpretation of APB No. 25. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation:

	Year ended December 31,		
	2002	2001	2000
Net Income as Reported	$1,195,218	$ 315,422	$2,386,019
Deduct: Total stock-based employee compensation			

expense determined under fair value-based method for all awards, net of related tax effect	123,952	473,749	94,022
Pro Forma Net Income (Loss)	$1,071,266	$ (158,327)	$2,291,997
Basic Net Income Per Share as Reported	$ .32	$ .09	$ .71
Basic Pro Forma Net Income (Loss) Per Share	$ .29	$ (.04)	$ .68
Diluted Net Income Per Share as Reported	$ .29	$ .08	$ .63
Diluted Pro Forma Net Income (Loss) Per Share	$ .26	$ (.04)	$ .61

The fair value of options at date of grant was estimated using the Black-Scholes fair value based method with the following weighted average assumptions:

	2002	2001	2000
Expected Life (Years)	5	5	5
Interest Rate	4.00%	4.00%	5.50%
Annual Rate of Dividends	0%	0%	0%
Volatility	63%	60%	57%

[2] Summary of Significant Accounting Policies - [Continued]

The weighted average fair value of options at date of grant using the fair value based method during 2002, 2001 and 2000 is estimated at $1.42, $1.45 and $1.50 respectively

Earnings Per Share - Basic earnings per share of common stock is computed by dividing income from continuing operations and net income by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share reflects the amount of earnings for the period available to each share of common stock outstanding during the reporting period, giving effect to all potentially dilutive shares of common stock from the potential exercise of stock options and warrants.

The computation of diluted earnings per share does not assume conversion, exercise or contingent issuance of securities that would have an antidilutive effect on earnings per share (i.e. improving earnings per share). The dilutive effect of outstanding options and warrants and their equivalents are reflected in dilutive earnings per share by the application of the treasury stock method. Options and warrants will have a dilutive effect only when the average market price of the common stock during the period exceeds the exercise price of the options or warrants. The Company had potentially dilutive options and warrants

outstanding of 729,702, 723,385 and 974,275 during the years ended December 31, 2002, 2001 and 2000, respectively.

The following table sets forth the computation of basic and diluted earnings per share:

	Year ended December 31,		
	2002	2001	2000
Numerator:			
Income from continuing operations	$1,195,218	$ 315,422	$2,316,019
Discontinued operations:			
Gain on sale of discontinued operations	--	--	70,000
Net income available to common stockholders	$1,195,218	$ 315,422	$2,386,019
Denominator:			
Weighted average shares	3,748,537	3,618,260	3,367,005
Effect of dilutive securities:			
Employee stock options	395,668	253,616	403,987
Stock warrants	9,279	--	--
Dilutive potential common shares	404,947	253,616	403,987
Denominator for diluted earnings per share-adjusted weighted average shares after assumed conversions	4,153,484	3,871,876	3,770,992

Advertising - Advertising costs are expensed as incurred. Advertising expense amounted to $139,110, $290,146 and $226,024 for the years ended December 31, 2002, 2001 and 2000, respectively.

Reclassification - Certain prior years' amounts have been reclassified to conform to the current year's presentation.

[2] Summary of Significant Accounting Policies - [Continued]

Financial Instruments - Effective June 2001 the Company adopted SFAS No. 133, "Accounting for Derivative instruments and Hedging Activities" as amended. SFAS No. 133 requires the recognition of all derivative instruments as either assets or liabilities on the balance sheet measured at fair value. Generally, increases or decreases in the fair value of derivative instrument will be recognized as gains or losses in earnings in the period of change. If the derivative instrument is designated and qualifies as a cash flow hedge, the change in fair

value of the derivative instrument will be recorded as a separate component of stockholders' equity.

The Company entered into an interest rate swap to hedge exposure related to changes in the LIBOR rate. Before entering into a derivative transaction for hedging purposes, it is determined that a high degree of initial effectiveness exists between the change in value of the hedged item and the change in the value of the determinative instrument from movement in interest rates. High effectiveness means that the change in the value of the derivative instrument will effectively offset the change in the fair value of the hedged item. The effectiveness of each hedged item is measured throughout the hedged period. Any hedge ineffectiveness as defined by SFAS No. 133 is recognized in the income statement.

New Accounting Pronouncements - In June 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets". The provisions of these interpretations that are applicable to the Company were implemented on a prospective basis as of January 1, 2002, which had no material effect on the Company's consolidated financial position or results of operations.

In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections". SFAS No. 145 requires that gains and losses from extinguishment of debt be classified as extraordinary items only if they meet the criteria in Accounting Principles Board Opinion No. 30 ("Opinion No. 30"). Applying the provisions of Opinion No. 30 will distinguish transactions that are part of an entity's recurring operations from those that are unusual and infrequent that meets the criteria for classification as an extraordinary item. The Company is required to adopt SFAS No. 145 no later than the first quarter of fiscal 2003, although early adoption is allowed. The adoption of this standard is not expected to have a material effect on the Company's consolidated financial position and results of operations.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 addresses accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)". SFAS No. 146 requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value when the liability is incurred. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002, with early application encouraged. The adoption of this standard is not expected to have a material effect on the Company's consolidated financial position or results of operations.

In November 2002, the FASB issued Interpretation No. 45, ("FIN 45") "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 requires a company, at the time it issues a guarantee, to recognize an initial liability for the fair value of obligations assumed under the guarantee and elaborates on existing disclosure requirements related to guarantees and warranties. The initial recognition requirements of FIN 45 are

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[2] Summary of Significant Accounting Policies - [Continued]

effective for guarantees issued or modified after December 31, 2002 and adoption of the disclosure requirements are effective for the Company as of December 31, 2002. The Company does not expect that the adoption of the recognition requirements of FIN 45 will have a material effect on its consolidated financial position or results of operations.

In January 2003, the FASB issued Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional financial support from other parties. FIN 46 is effective for all new variable interest entities created or acquired after January 31, 2003. For variable interest entities created or acquired prior to February 1, 2003, the provisions of FIN 46 must be applied for the first interim or annual period beginning after June 15, 2003. The Company does not expect the adoption of FIN 46 will have a material effect on its consolidated financial position or results of operations.

[3] Accounts Receivable

Accounts receivable is shown net of allowance for doubtful accounts of $530,640 and $357,994 at December 31, 2002 and 2001 respectively. The changes in the allowance for doubtful accounts are summarized as follows:

	Year Ended December 31,		
	2002	2001	2000
Beginning Balance	$ 357,994	$ 370,222	$ 305,226
Provision for Doubtful Accounts	370,000	340,000	330,000
Charge-offs	(197,354)	(352,228)	(265,004)
Ending Balance	$ 530,640	$ 357,994	$ 370,222

[4] Costs, estimated profits, and billings on uncompleted contracts are summarized as follows:

	December 31,	
	2002	2001
Costs Incurred on Uncompleted Contracts	$ 18,599,730	$ 16,065,533
Estimated Profits	10,501,200	8,803,818
Total	29,100,930	24,869,351
Billings to Date	31,158,378	25,045,225
Net	$ (2,057,448)	$ (175,874)

Included in the accompanying consolidated balance sheet under the following

captions:

Costs and estimated profits in excess of interim billings	$ 3,857,522	$ 3,783,356
Interim billings in excess of costs and estimated profits	(5,914,970)	(3,959,230)
Net	$ (2,057,448)	$ (175,874)

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, Sheet #8

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[5] Discontinued Operations

During 1998 the Company discontinued its CarteSmart division which included its interest in a joint venture. On June 30, 1998, the Company sold this division, with an option to purchase the Company's interest in the joint venture if the other party to the venture did not elect to acquire the Company's interest, to Granite Technologies, Inc. ("Granite"), a corporation formed by the former management of the division. Granite issued to the Company its $500,000 promissory note and an equity interest in Granite equal to 20% at the time of transaction. Granite also agreed to pay certain royalties to the Company. The note was subject to cancellation if the other party to the joint venture elected to purchase the Company's interest. As the Company had virtually no influence over the financing and operating policies of Granite, the interest in Granite was accounted for using the cost method. During 2000, the Company's 20% interest in Granite was diluted to 13% as a result of additional equity issued by Granite to third parties.

During 2001, Granite was purchased by The Finx Group, Inc. ("Finx") and the Company received 496,124 restricted shares of Finx for its 13% interest in Granite. The Finx shares are traded on the OTC Bulletin Board. During 2001, the Company advanced Granite $39,490 for working capital purposes. In December 2001, Finx repaid the advance with 79,661 shares of its common stock. At December 31, 2001, the Company valued its aggregate holding in Finx, consisting of 575,785 shares at $69,490. At December 31, 2002, the Company reassessed its value in the Finx stock and reduced it by $57,974 to $11,516. The adjustment was charged as an other-than-temporary decline to interest and other expenses. The Finx shares are included in other assets.

In October 1998, the other party to the joint venture exercised its right to purchase the Company's interest in the joint venture for a $500,000 note. The Company has been paid in full from installment payments on this note over a period ranging from November 1998 through December 2000. The Company recognized gain on the sale of discontinued operations as it continually revalued this note throughout the payment period.

[6] Property and Equipment

Property and equipment consist of the following:

	December 31,	
	2002	2001

Equipment, Furniture and Fixtures	$1,417,042	$1,191,975
Leasehold Improvements	305,862	294,152
Totals - At Cost	1,722,904	1,486,127
Less: Accumulated Depreciation and Amortization	1,358,598	1,119,771
Net	$ 364,306	$ 366,356

Depreciation and amortization expense amounted to $256,517, $266,690, and $259,323, respectively for the years ended December 31, 2002, 2001 and 2000.

[7] Bank Financing

Bank Financing - In June 2001, the Company entered into a financing agreement with a bank. This improved credit facility and medium term financing replaces the Company's asset based borrowing facility. The new financing provides the Company with a five-year term loan of $2.5 million and a two year $1.5 million revolving line of credit. The term loan is paid in equal monthly installments during the term of the loan plus interest. Proceeds from the term loan are available for acquisitions and to upgrade certain software systems to meet requirements in California. Funds drawn down from the revolving line of credit are to be used for working capital purposes. The term loan bears

[7] Bank Financing - [Continued]

interest at LIBOR plus 2.5%. The revolving line of credit will bear interest, at the Company's option, to be equal to either (i) LIBOR plus 2.0% or (ii) the Prime Rate, and incur an annual facility fee of 0.5%. On July 12, 2001, the Company entered into an interest rate swap agreement on the term loan at 7.95% for five years (Note 12). The financing agreement contains certain covenants including limitations on the Company's ability to incur liens, enter into change of control transactions, maintain a minimum net worth at $9,000,000 and requires the maintenance of certain financial ratios. The interest rate on the previous facility was prime plus 2%. As of December 31, 2002, the Company owes approximately $1,750,000 on the term loan, of which $500,000 is classified as a current liability and the balance is classified as a long term liability. The Company has not utilized any borrowing availability on the $1.5 million revolving line of credit. The borrowing is collateralized by a first priority security interest and lien on all the assets of the Company.

[8] Income Taxes

The Company utilizes an asset and liability approach to determine the extent of any deferred income taxes, as described in SFAS No. 109, "Accounting for Income Taxes." This method gives consideration to the future tax consequences associated with differences between financial statement and tax bases of assets and liabilities.

During the year ended December 31, 2002, the Company utilized approximately $1.6

million of net operating loss carryforwards. At December 31, 2002 the Company has remaining net operating loss carryforwards of approximately $9,045,000 expiring by 2021. Pursuant to Section 382 of the Internal Revenue Code regarding substantial changes in Company ownership, utilization of approximately $6,500,000 of this net operating loss carryforward is limited to approximately $1,360,000 per year, plus any prior years' amounts not utilized. In addition, the tax benefit of approximately $1,800,000 of net operating losses generated in 2000 on exercise of non-qualified compensatory stock options and warrants will be credited to paid-in-capital as utilized.

The Company's provision for taxes for the year ended December 31, 2002 includes certain state and local taxes.

The expiration dates of net operating loss carryforwards are as follows:

December 31,	Amount
2015	$ 1,305,000
2016	2,413,000
2017	2,664,000
2018	716,000
2019	133,000
2020	1,810,000
2021	4,000
	$ 9,045,000

[8] Income Taxes - [Continued]

Provision for income taxes consists of the following:

	Year ended December 31,		
	2002	2001	2000
Current:			
Federal	$ --	$ (43,280)	$ 43,280
State	84,000	18,280	113,893
	84,000	(25,000)	157,173
Deferred:			
Federal	(400,000)	--	(442,000)
State	--	(6,000)	(52,000)
	(400,000)	(6,000)	(494,000)
Total	$ (316,000)	$ (31,000)	(336,827)

The difference between income taxes at the statutory Federal income tax rate and

income taxes reported in the income statement is as follows:

	Year ended December 31,		
	2002	2001	2000
Income taxes at the federal statutory rate	34%	34	34%
State and local income taxes net of Federal taxes	5%	5	5%
Nondeductible expenses	6%	9	5%
Federal Minimum Tax	--	--	2%
Stock Option Deduction	--	--	(46)%
Decrease in valuation allowance	(82)%	(14)%	(25)%
Overaccrual from prior year		(45)%	--
Other	1%	--	8%
	(36)%	(11)%	(17)%

Significant components of the Company's deferred tax assets are comprised of the following:

	December 31,	
	2002	2001
Net operating loss carryforward	$ 3,704,000	$ 4,178,000
Allowance for doubtful accounts	211,000	136,000
Accrued vacation and bonuses	202,000	122,000
Alternative minimum tax credit carryforward	43,000	43,000
Benefit of stock based compensation awards	502,000	502,000
Other	262,000	--
Total deferred tax assets	4,924,000	4,981,000
Valuation allowance	(4,024,000)	(4,481,000)
Net deferred tax assets	$ 900,000	$ 500,000

The valuation allowance decreased by $457,000 at December 31, 2002 The Company believes that it is more likely than not, to use at least a portion of its net operating loss carryforward.

[8] Income Taxes - [Continued]

The change in the valuation allowance for deferred tax assets are summarized as follows:

Year Ended December 31,		
2002	2001	2000

Beginning Balance	$ 4,481,000	$ 4,520,000	$ 5,425,000
Change in Allowance	(457,000)	(39,000)	(905,000)
Ending Balance	$ 4,024,000	$ 4,481,000	$ 4,520,000

[9] Stockholders' Equity

The Company's Board of Directors is authorized to issue preferred stock from time to time without stockholder action, in one or more distinct series. The Board of Directors is authorized to determine the rights and preferences of the preferred stock when issued. The Board of Directors has authorized the issuance of Series A, Series B and Series D preferred Stock. No shares of any series of preferred stock were outstanding on December 31, 2002.

Common Stock Issuances - During 2000, Series B Common Stock Purchase Warrants to purchase an aggregate of 192,105 shares of Common Stock at $6 per share were exercised. The Company received $1.1 million from the exercise of the warrants.

Treasury Stock - During 2002, stock options to purchase 327,183 shares were exercised and the Company received gross proceeds of $505,210. Pursuant to the option grants, employees have the right to pay for the exercise price of the options by delivering shares of common stock owned by them. During 2002, the Company received 61,759 shares having a value of $348,302, as the exercise price of the options. During 2000, stock options to purchase 328,321 shares were exercised, and the Company received gross proceeds of $381,541. Pursuant to the option grants, employees have the right to pay for the exercise price of the option by delivering shares of common stock owned by them. During 2000, the Company received 22,705 shares, having a value of $239,810, as the exercise price of the options.

Stock Options - See Note 13 for information relating to the Company's 1998, 1999 and 2001 Long-Term Incentive Plans.

On December 21, 2000, the stockholders of the Company approved the 1999 Employee Stock Purchase Plan. The plan reserves 150,000 shares of common stock. The plan provides eligible employees with the opportunity to purchase shares of common stock at a discounted price through regular payroll deductions. No options have been issued as of December 31, 2002 under this plan.

[10] Capital Lease Obligations

Future minimum payments under capital lease obligations as of December 31, 2002 are as follows:

Year ending December 31,	
2003	10,808
2004	1,801
Total Minimum Payments	12,609
Less Amount Representing Interest at 12.6% Per annum	859
Balance	$ 11,750

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NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, Sheet #12

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[10] Capital Lease Obligations - [Continued]

Capital lease obligations are collateralized by equipment which has a cost of $40,000 at December 31, 2002 and 2001 and accumulated amortization of $28,000 and $20,000 at December 31, 2002 and 2001 respectively. Amortization of $8,000 in each of 2002, 2001 and 2000, respectively, has been included in depreciation expense.

[11] Fair Value of Financial Instruments

The carrying amount of cash and cash equivalents, accounts receivable, and accounts payable approximate the fair value of these instruments because of their short maturities.

Long-term debt, including current maturities, has a carrying value of approximately $1,750,000 and an estimated fair value of $1,800,000. Estimated fair value is based on the expected current rates offered to the Company for instruments of the same or similar maturities, after considering the effect of the interest rate swap.

[12] Commitments and Contingencies

Leases

The Company leases space for its executive offices and facilities under non cancellable operating leases expiring December 31, 2003. In addition the Company leases three sales and service offices under non cancelable operating leases expiring at various times through July 2005.

Minimum annual rentals under noncancellable operating leases having terms of more than one year are as follows:

Year ending December 31,	
2003	$ 473,000
2004	77,000
2005	43,000
Total	$ 593,000

Rent expense amounted to $455,000, $482,000 and $464,000 respectively, for the years ended December 31, 2002, 2001 and 2000.

Employment Agreements

In January 2001, the Company entered into employment agreements with its four executive officers for terms of two or three years with the right of the employee to extend the agreement for an additional year. The aggregate base compensation for these officers for 2003 is $657,000, subject to annual increases equal to the greater of 5% or the increase in the cost of living index. Each of the officers also has the right, at any time on 90 days notice, to terminate his full time employment and continue as a consultant at an annual salary of $75,000 for five years following the expiration or termination of his employment. The agreements also provide the officers with an automobile allowance. In the event of a change of control, the executive may receive severance payments of between 30 and 36 months' compensation.

The Company also has a consulting agreement with a Director, which provides for annual fees of $75,000 through December 31, 2003. The agreement also provides the Director with an automobile allowance. In the event of a change of control, the Director may receive severance payments of between 30 and 36 months compensation.

[12] Commitments and Contingencies - [Continued]

Interest Rate Swap

In June 2001 the Company entered into an interest rate swap with a bank, which expires on June 1, 2006. The swap transaction was entered into to protect the Company from upward movement in interest rates relating to outstanding bank debt (See Note 7) and calls for a fixed rate of 7.95%. When the one-month LIBOR rate is below the fixed rate then the Company is obligated to pay the bank for the difference in rates. When the one-month LIBOR rate is above the fixed rate then the bank is obligated to pay the Company for the difference in rates. At December 31, 2002 and 2001 the fair value of the swap of $107,713 and $74,875, respectively, is recorded as a non-current liability. The swap transaction has been accounted for as a hedge, and accordingly, the change in the fair value of the swap of $32,838 and $74,875 during the years ended December 31, 2002 and 2001, respectively, has been recorded as part of comprehensive income.

[13] Stock-Based Compensation

Long Term Incentive Plans - The Company has three long-term incentive plans, the 1998 Long-Term Incentive Plan (the "1998 Plan"), as amended, the 1999 Long-Term Incentive Plan (the "1999 Plan") and the 2001 Long-Term Incentive Plan (the "2001 Plan"). The 2001 Plan was approved by the stockholders on March 7, 2002 and provides for the issuance of 180,000 shares of common stock. In January 2003, the 2001 Plan was amended and approved by the stockholders to provide for an increase in the number of shares subject to the plan from 180,000 to 550,000. The 1999 Plan was approved by the stockholders in December 2000 and provides for the issuance of 300,000 shares of common stock. The Company may issue 790,000, 300,000 and 550,000 shares of Common Stock pursuant to the 1998 Plan, the 1999 Plan and the 2001 Plan respectively. The options, when granted vest ratably over one year. At December 31, 2002 there were 11,500, 2,000 and 1,500 shares available for further issuance under the 1998 Plan, the 1999 Plan and 2001 Plan, respectively, exclusive of any options available for grant as a result of the increase in the 2001 Plan.

The 1998 Plan, the 1999 Plan and the 2001 Plan (collectively, the "Plans") are administered by the Compensation Committee of the board of directors. Officers and other key employees, consultants and directors (other than non-employee directors) are eligible to receive options or other equity-based incentives under the Plans.

The Plans provides that each non-employee director automatically receives a nonqualified stock option to purchase 5,000 shares of common stock on April 1 of each year. However, if there are not sufficient shares available under the applicable Plan, the non-employee director will receive a lesser number of shares.

During 2002, pursuant to an arrangement with a consultant, the Company issued a non-qualified stock option to purchase 10,000 shares of stock at an exercise price of $2.75, which was the fair market value of the stock at the date of grant. The options were valued at $.57 per option based upon the Black-Scholes calculation, which had an interest rate of 4% and a volatility rate of .48. These options had a term of one year, however, they were exercised during 2002. The Company recognized a charge to income under the Black-Scholes formula in the amount of $5,673.

During 2000, pursuant to an employment contract with a newly hired executive, the Company issued a non-qualified stock option to purchase 75,000 shares of stock at an exercise price of $6.50 per share.

[13] Stock-Based Compensation - [Continued]

A summary of the activity under the Plans is as follows:

	2002		2001		2000	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding - Beginning of Year	793,385	$1.917	809,718	$1.908	783,041	$1.176
Granted During the Year	198,500	2.505	3,500	1.900	375,000	2.748
Canceled During the Year	--	--	(5,278)	1.810	(20,002)	1.250
Exercised During the Year	(327,183)	1.544	(14,555)	1.500	(328,321)	1.167
Outstanding - End of Year	664,702	$2.276	793,385	$1.917	809,718	$1.908
Exercisable - End of Year	575,451	$2.242	789,885	$1.917	434,718	$1.183

The following table summarizes stock option information as of December 31, 2002:

Exercise Prices	Number Outstanding	Options Outstanding Weighted Average Remaining Contractual Life	Options Exercisable
$6.50	75,000	2.25 Years	75,000
$2.50	165,503	4.25 Years	82,752
$2.38	8,000	4.5 Years	4,000
$2.40	5,000	4.5 Years	2,500
$1.90	3,500	3.83 Years	3,500
$1.81	160,699	3 Years	160,699
$1.50	72,500	.42 Years	72,500
$1.00	174,500	.83 Years	174,500
Totals	664,702	2.41 Years	575,451

Warrants Issued as Compensation - In December 1999, the Company's $6 and $12 Series B Common Stock Purchase Warrants totaling 287,500 and 448,544, respectively, were extended to February 29, 2000. These warrants had a previous expiration date of December 31, 1999. The Company recognized a financing cost of $81,000 with respect to this extension in 1999. In February 2000, these warrants were further extended to April 30, 2000 and the Company recognized additional financing costs of $125,000 in 2000. At the end of April 2000, 192,105 of the $6 warrants were exercised and 95,395 expired. During the course of 2001 the 448,544 $12 warrants were extended to January 31, 2002. In January 2002, the 448,544 $12 warrants were further extended to July 31, 2002. In July 2002, the $12 warrants were further extended to January 31, 2003. There was no financing costs associated with the warrant extensions in 2001 and 2002 because of the variance between the $12 exercise price and the current market value of the Company's stock at the date of the warrant extension.

[13] Stock-Based Compensation - [Continued]

During 2002, the Company issued warrants to purchase 200,000 shares in connection with a financial advisory agreement whereby the Company will pay consulting fees in addition to the issuance of warrants. These warrants, which expire over various times ranging from one to two years, were valued at $.24 per warrant, which represented the costs of the services based upon the contractual agreement. Either party may terminate the agreement. The warrants have the following exercise price, vesting dates and expiration date for the number of shares set forth below:

Shares	Exercise Price	Vesting Date	Expiration Date

50,000	$2.70	April 10, 2002	March 31, 2003
30,000	$4.00	June 1, 2002	May 31, 2003
30,000	$5.00	September 1, 2002	February 28, 2004
30,000	$6.00	November 1, 2002	April 30, 2004
30,000	$7.00	January 1, 2003	December 31, 2004
30,000	$8.00	February 28, 2003	January 31, 2005

The $48,000 value of the warrants is being charged to operations over the vesting period. As a result, $33,600 was charged to operations in 2002 and $14,400 will be charged to operations in the quarter ending March 31, 2003.

In October 2001, the Company issued warrants to purchase 40,000 shares in connection with a public and investor relations agreement whereby the Company will pay a monthly fee in addition to the issuance of the warrants. The warrants have an exercise price of $2.50 for the first 5,000 shares; $3.00 for the next 5,000 shares; $3.50 for 15,000 shares and $4.00 for the final 15,000 shares. These warrants were valued at an average price of $.14 per warrant based upon the Black-Scholes calculation, which had an interest rate of 5.5% and a volatility rate of .6. These warrants expired on October 28, 2002.

A summary of warrant activity is as follows:

	2002		2001		2000	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding - Beginning of Year	608,544	$10.11	568,544	$10.57	790,044	$ 9.35
Granted During the Year	648,544	$ 9.89	488,544	$11.30	514,544	$11.13
Expired During the Year	(488,544)	$11.30	(448,544)	$12.00	(543,939)	$10.95
Exercised During the Year	--	--	--	--	(192,105)	$ 6.00
Outstanding - End of Year	768,544	$ 9.17	608,544	$10.11	568,544	$10.57
Exercisable - End of Year	708,544	$ 9.31	578,544	$10.44	568,544	$10.57

[13] Stock-Based Compensation - [Continued]

The following table summarizes warrant information as of December 31, 2002:

Weighted

Average Remaining

Exercise Prices	Shares	Contractual Life
$12.00	448,544	.08 Years
$ 8.00	30,000	2.08 Years
$ 7.00	30,000	2.00 Years
$ 6.00	30,000	1.33 Years
$ 5.45	100,000	1.75 Years
$ 5.00	30,000	1.17 Years
$ 4.20	20,000	1.75 Years
$ 4.00	30,000	.42 Years
$ 2.69	50,000	.25 Years
Total	768,544	.61 Years

The Company applies Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees", and related interpretations, for stock options issued to employees in accounting for its stock options plans. There was no compensation cost recognized for stock based employee compensation awards for 2002, 2001and 2000.

NETSMART TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, Sheet #17

[14] Operating Segments

The Company currently classifies its operations into two business segments: (1) Software and Related Systems and Services and (2) Data Center Services. Software and Related Systems and Services is the design, installation, implementation and maintenance of computer information systems that provide comprehensive healthcare information technology solutions including billing, patient tracking and scheduling for inpatient and outpatient environments, as well as clinical documentation and medical record generation and management. Data Center Services involve Company personnel performing data entry and data processing services for customers. Intersegment sales and sales outside the United States are not material. Information concerning the Company's business segments is as follows:

	Year ended December 31,		
	2002	2001	2000
Revenues:			
Software and Related Systems and Services	$20,168,785	$16,077,323	$17,907,973
Data Center Services	1,957,392	2,042,098	2,262,676
Total Revenues	$22,126,177	$18,119,421	$20,170,649
Gross Profit:			
Software and Related Systems and Services	$ 6,635,931	$ 5,095,038	$ 6,977,035

Data Center Services	945,790	1,023,148	1,238,153
Total Gross Profit	$ 7,581,721	$ 6,118,186	$ 8,215,188
Income (loss) From Continuing Operations before Income Taxes:			
Software and Related Systems and Services	$ 481,242	$ (242,072)	$ 1,208,445
Data Center Services	397,976	526,494	770,747
Total Income From Continuing Operations before Income Taxes	$ 879,218	$ 284,422	$ 1,979,192
Depreciation and Amortization:			
Software and Related Systems and Services	$ 866,115	$ 847,369	$ 579,900
Data Center Services	170,606	163,452	137,876
Total Depreciation and Amortization	$ 1,036,721	$ 1,010,821	$ 717,776
Capital Expenditures:			
Software and Related Systems and Services	$ 248,201	$ 116,951	$ 850,893
Data Center Services	6,266	3,814	21,947
Total Capital Expenditures	$ 254,467	$ 120,765	$ 872,840
Identifiable Assets:			
Software and Related Systems and Services	$20,411,376	$16,104,973	$12,659,935
Data Center Services	1,863,285	1,902,400	2,146,778
Total Identifiable Assets	$22,274,661	$18,007,373	$14,806,713

[15] Legal Proceedings

In October 2000, the Company's subsidiary, CSM, commenced an action against the City of Richmond, in the Supreme Court of the State of New York, County of Suffolk, which action was subsequently removed to the United States District Court for the Eastern District of New York, for failure to pay more than $1 million pursuant to a contract between the Company and Richmond. Richmond

advised the court that it intended to move to dismiss the complaint for lack of personal jurisdiction in New York and improper venue. In November 2000, Richmond filed a complaint in the Circuit Court for the City of Richmond, Richmond, Virginia, alleging, among other things, that the contract with CSM was procured through fraudulent misrepresentations concerning the nature of the work to be performed and the price for the services and that CSM failed to perform its obligations under the agreement, seeking damages of $373,000 and a finding that it owes no additional amounts to CSM. The parties entered into a stipulation staying the Richmond action until a determination of Richmond's jurisdictional challenges to the New York action. On August 21, 2002, the United States District Court for the Eastern District of New York denied Richmond's motion to dismiss the Company's complaint for lack of personal jurisdiction in New York on the basis of improper venue. The Company believes it has valid claims against Richmond and intends to vigorously pursue those claims. The Company also believes that the allegations contained in Richmond's complaint are without merit and intends to vigorously defend against those claims. The outcome of this case is not expected to have a material effect on the Company's consolidated financial position or results of operations.

The Company is involved in other litigation through the normal course of business. The Company believes that the resolution of these matters will not have a material adverse effect on the Company's consolidated financial position and results of operations.

[16] Subsequent Event

On January 27, 2003, the Company granted 217,500 options under the 2001 Plan, following stockholder approval of the amendment to the 2001 Plan to increase the number of shares of common stock subject to the plan to employees at a price of $4.93, which was the fair market value at the date. The options vest 50% after six months and 100% after one year.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, this amended report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

NETSMART TECHNOLOGIES, INC.

Dated: August 21, 2003

By:/s/James L. Conway

James L. Conway, Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this amended report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date

Signature	Title	Date
/s/James L. Conway ---------------------- James L. Conway	Chief Executive Officer and Director (Principal Executive Officer)	August 21, 2003
/s/Anthony F. Grisanti ---------------------- Anthony F. Grisanti	Chief Financial Officer (Principal Financial and Accounting Officer)	August 21, 2003
* ---------------------- Edward D. Bright	Director	August 21, 2003
* ---------------------- John F. Phillips	Director	August 21, 2003
* ---------------------- Gerald O. Koop	President and Director	August 21, 2003
* ---------------------- Joseph G. Sicinski	Director	August 21, 2003
* ---------------------- Francis J. Calcagno	Director	August 21, 2003
* ---------------------- John S.T. Gallagher	Director	August 21, 2003

* by James L. Conway, Attorney-in-Fact