LEAPFROG SMART PRODUCTS INC
Form 10QSB/A
December 06, 2001

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

Amendment No. 1
FORM 10-QSB

(Mark One)

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

For the nine months ended SEPTEMBER 30, 2001

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

For the transition period from ____________ to ____________

Commission file number: 000-20786

LEAPFROG SMART PRODUCTS, INC.

(Name of small business issuer in its charter)

COLORADO	84-1076959
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1011 MAITLAND CENTER COMMONS, MAITLAND, FLORIDA	32751
(Address of Principal Executive Offices)	(Zip Code)

Issuer's telephone number (407) 838-0400

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

NONE

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

COMMON STOCK, NO PAR VALUE PER SHARE
(Title of class)

Check whether the issuer (1) filed all reports required to be filed by Section13 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 [ ]

State issuer's revenues for its most recent fiscal year:

December 31, 2000--$972,724

As of December 4, 2001:

10,030,845 shares of the issuer's Common Stock were outstanding.

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ITEM 1. FINANCIAL STATEMENTS

FINANCIAL STATEMENTS

The unaudited condensed financial statements of Leapfrog Smart Products, Inc. for the nine and three months periods ended September 30, 2001 and 2000 follow. The financial statements reflect all adjustments which are, in the opinion of management, necessary to a fair statement of the results for the interim period represented.

It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto included in the annual report on Form 10-KSB for the year ended December 31, 2000.

INDEX TO FINANCIAL STATEMENTS

LEAPFROG SMART PRODUCTS, INC. AND SUBSIDIARIES
(A Development Stage Company)
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
ASSETS

	September 30, 2001	December 31, 2000
CURRENT ASSETS		
Cash	$ 7,810	$ 107,413
Accounts receivable	53,624	113,092
Inventory	107,749	122,382
Prepaid expenses	103,087	172,060
Notes receivable - related party	3,400	15,900
Other receivables	642	1,980
TOTAL CURRENT ASSETS	276,312	532,827
PROPERTY AND EQUIPMENT, NET	215,140	238,457
OTHER ASSETS		
Related-party advances	101,964	107,009
Deposits	37,638	38,136
Capitalized software costs, net of accumulated amortization of $36,286 and $24,884	178,593	169,137
Costs in excess of fair market value of assets acquired, net of accumulated amortization of $7,750 and $5,500	22,250	24,500
	$ 831,897	$1,110,066

LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND
STOCKHOLDERS' EQUITY (DEFICIT)

CURRENT LIABILITIES		
Notes payable - current portion	$ 3,057,435	$1,452,956
Notes payable - related party	537,162	355,258
Deferred Income	10,000	-
Accounts payable	1,251,475	1,043,453
Accrued expenses	877,179	212,255
TOTAL CURRENT LIABILITIES	5,733,251	3,063,922
LONG-TERM NOTES PAYABLE	84,310	-
TOTAL LIABILITIES	5,817,561	3,063,922
REDEEMABLE CONVERTIBLE PREFERRED STOCK		
7% Series B Convertible - 50,000 and 0 shares issued and outstanding (redemption value - $62,500 on June 15, 2002 and $100,000 on June 15, 2003)	53,646	-
STOCKHOLDERS' EQUITY (DEFICIT)		
Common stock - no par value; 30,000,000 shares authorized; 10,018,845 and 8,977,845		

shares issued and outstanding	11,200,203	10,488,908
Convertible preferred stock - no par value per share; 10,000,000 shares authorized;		
6% Series A - 125,000 shares issued and outstanding	480,000	480,000
Series F- (aggregate liquidation preference of $19,500), 195 shares issued and outstanding	14,625	14,625
Deficit accumulated during development stage	(16,734,138)	(12,937,389)
	(5,039,310)	(1,953,856)
	$ 831,897	$ 1,110,066

SEE ACCOMPANYING NOTES

LEAPFROG SMART PRODUCTS, INC. AND SUBSIDIARIES
(A Development Stage Company)

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Nine Months Ended Sept. 30, 2001	Nine Months Ended Sept. 30, 2000	Quarter Ended Sept. 30, 2001	Quarter Ended Sept. 30, 2000	Cumulative From April 11, 1996 (Inception) Through Sept. 30, 2001
REVENUES	$ 716,291	$ 802,345	$ 136,405	$ 634,605	$ 2,569,805
COST OF SALES	635,520	735,644	130,011	577,215	2,131,754
GROSS PROFIT	80,771	66,701	6,394	57,390	438,051
OPERATING EXPENSES					
Personnel and related expenses	2,212,091	1,981,589	594,381	751,402	8,826,562
Consulting fees	208,465	634,929	50,715	412,021	2,283,579
General and administrative	1,081,922	1,571,111	224,452	549,666	4,486,776
Depreciation and amortization	72,571	69,029	29,836	22,160	295,580
TOTAL OPERATING EXPENSES	3,575,049	4,256,658	899,384	1,735,249	15,892,497
OTHER INCOME (EXPENSE)					
Other income, net	12,567	40,966	(3,115)	875	75,001
Loss on disposal of assets	-	-	-	-	(30,389)
Equity interest in loss of subsidiary	-	-	-	-	(150,000)
Interest expense	(315,038)	(312,080)	(127,953)	(60,464)	(1,174,304)
	(302,471)	(271,114)	(131,068)	(59,589)	(1,279,692)
NET LOSS	$(3,796,749)	(4,461,071)	(1,024,058)	(1,737,448)	(16,734,138)

BASIC AND DILUTED NET LOSS PER COMMON SHARE	$ (0.41)	(0.70)	(0.11)	(0.24)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING	9,259,191	6,388,171	9,767,261	7,265,169

SEE ACCOMPANYING NOTES

LEAPFROG SMART PRODUCTS, INC. AND SUBSIDIARIES
(A Development Stage Company)

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY (DEFICIT)

NINE MONTHS ENDED SEPTEMBER 30, 2001

	Common Stock No Par Value		Convertible Preferred Stock No Par Value		Deficit Accumulated During Development Stage	Total Stockhold Equity (Deficit)
	Shares	Amount	Shares	Amount		
BALANCE - DECEMBER 31, 2000	8,977,845	$10,488,908	125,195	$494,625	$(12,937,389)	$(1,953,8
ISSUANCE OF COMMON STOCK AND OPTIONS FOR SERVICES AND INTEREST	30,000	186,559	-	-	-	186,5
ISSUANCE OF COMMON STOCK ON EXERCISE OF OPTIONS	61,000	15,250	-	-	-	15,2
ISSUANCE OF COMMON STOCK FOR CASH	950,000	513,132	-	-	-	513,1
ACCRETION OF REDEMPTION VALUE OF REDEEMABLE PREFERRED STOCK		(3,646)				(3,6
NET LOSS	-	-	-	-	(3,796,749)	(3,796,7
BALANCE - SEPTEMBER 30, 2001	10,018,845	$11,200,203	125,195	$494,625	$(16,734,138)	$(5,039,3

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SEE ACCOMPANYING NOTES

LEAPFROG SMART PRODUCTS, INC. AND SUBSIDIARIES
(A Development Stage Company)

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended Sept. 30, 2001	Nine Months Ended Sept. 30, 2000	Cumulative From April 11, 1996 (Inception) Through Sept. 30, 2001
CASH FLOWS FROM OPERATING ACTIVITIES			
Net loss	$ (3,796,749)	$ (4,461,071)	$ (16,734,138)
Reconciliation of net loss to net cash used in operating activities			
Depreciation	58,919	55,380	257,175
Depreciation and amortization charged to cost of sales	-	12,122	38,460
Amortization	13,652	13,650	35,394
Assets expensed to research and development	-	28,970	28,968
Loss on disposal of assets, net	-	14,775	33,639
Loss on write-off of related party note receivable	-	-	17,870
Gain on write-off of notes payable	(20,000)	-	(20,000)
Employee compensation for options issued below market	-	-	1,167,580
Common stock and options issued for services and interest	156,559	981,211	2,159,039
Discount on issuance of debt	(147,633)	-	(147,633)
Amortization of discount on debt	57,879	-	57,879
Cash provided by (used in) change in:			
Accounts receivable	59,468	(230,704)	(53,624)
Related party advances	5,045	(276,046)	(101,964)
Other receivables	1,338	6,708	(642)
Inventory	14,633	(16,172)	(107,749)
Prepaid expenses and other assets	69,471	(133,693)	(140,725)
Accounts payable	250,522	540,873	1,342,214
Accrued expenses	767,317	136,473	1,047,535
Deferred income	10,000	-	10,000
NET CASH USED IN OPERATING ACTIVITIES	(2,499,579)	(3,327,524)	(11,110,722)
CASH FLOWS FROM INVESTING ACTIVITIES			
Acquisition of property, plant and			

equipment	(35,600)	(107,118)	(573,211)
Net increase in notes receivable-related party	-	(13,654)	(63,124)
Capitalization of software costs	(20,858)	(75,861)	(214,879)
Proceeds from sale of vehicles	-	-	8,473
NET CASH USED IN INVESTING ACTIVITIES	(56,458)	(196,633)	(842,741)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of notes payable	2,000,000	701,902	5,217,768
Payments on notes payable	(301,952)	(474,910)	(1,128,927)
Proceeds from exercise of common stock options	15,250	21,250	485,120
Proceeds from sale of common stock	513,131	2,650,588	6,322,049
Proceeds from sale of preferred stock	50,000	480,000	530,000
Proceeds from related-party borrowings	190,843	140,000	553,501
Repayments of related-party borrowings	(10,838)	-	(18,238)
NET CASH PROVIDED BY FINANCING ACTIVITIES	2,456,434	3,518,830	11,961,273
NET INCREASE (DECREASE) IN CASH	(99,603)	(5,327)	7,810
CASH AT BEGINNING OF PERIOD	107,413	18,529	-
CASH AT END OF PERIOD	$ 7,810	$ 13,202	$ 7,810

SEE ACCOMPANYING NOTES

LEAPFROG SMART PRODUCTS, INC. AND SUBSIDIARIES
(A Development Stage Company)

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Nine Months Ended September 30, 2001 and 2000

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Leapfrog Smart Products, Inc. and Subsidiaries' operations include the design, development, and licensing of Smart card applications and related database management systems and services. The Smart card is a wallet-sized plastic card with an embedded computer chip carrying accessible data that is retrievable on demand and is capable of integrating various functions with security features.

Leapfrog Smart Products, Inc. ("Leapfrog") was incorporated under the laws of the State of Florida in 1996.

Effective February 18, 2000, Albara Corporation ("Albara"), a Colorado corporation, acquired, through its wholly owned subsidiary Leapfrog Merger, Inc., a Florida corporation, 100% of the outstanding common stock of Leapfrog in exchange for 5,350,049 shares of Albara common stock. Additionally, the outstanding stock options of Leapfrog were converted, on a pro rata basis, into 2,434,950 Albara stock options. Prior to the merger, Albara was a publicly held shell company with little revenues and insignificant expenses, assets and liabilities. Upon completion of the merger, the original shareholders of Albara held 616,796 shares of its common stock and 195 shares of its Series F Preferred Stock. As a result of the exchange, the former shareholders of Leapfrog gained control of Albara. For accounting purposes, the acquisition has been accounted for as a re-capitalization of Leapfrog with Leapfrog being treated as the acquiring entity (reverse acquisition) with no goodwill recorded. Accordingly, the historical financial statements prior to February 18, 2000 are those of Leapfrog Smart Products, Inc. and Subsidiaries with the related stockholders' equity section being retroactively restated to reflect the equivalent number of Albara shares received in the merger after giving effect to the differences in par value. In connection with the merger, Albara changed its name to Leapfrog Smart Products, Inc. Leapfrog recorded a charge to general and administrative expenses of $64,000 for direct and other merger related costs pertaining to the merger transaction. Merger transaction costs consisted primarily of fees for legal, investment banking and other related charges.

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Leapfrog owns approximately 95% of the outstanding common stock of Leapfrog Global IC Products, Inc. ("LGIC") and approximately 96% of the outstanding common stock of Conduit Healthcare Solutions, Inc. ("Conduit"). By licensing agreement, LGIC has the rights to all of Leapfrog's technology and distribution rights of its product line outside of North America, except for the territories subsequently granted to Smart Products, International Pte., Ltd. ("SPI") The LGIC agreement expires in 2009, calls for revenue sharing, and may be terminated if certain performance measures are not met. Certain employees and consultants of Leapfrog hold stock options to purchase an aggregate of 10% of LGIC at an exercise price of $11,500. These individuals also have the right to receive additional options to purchase up to an additional 48 % of LGIC for $48,000 if certain performance measures are met. In 2000, LGIC created Leapfrog China, Inc., as a wholly owned subsidiary, for the purpose of pursuing opportunities in China. The SPI license agreement has performance standards and may be terminated by the Company if these standards are not met. Leapfrog's Board of Directors has declared the license in default. Conduit was originally incorporated in 1997 under the name Leapfrog Healthcare Products, Inc. On April 2, 2001, the Company entered into an agreement for the sale of approximately 82% of Conduit. The Company and the purchaser mutually terminated the agreement in June 2001.

The consolidated financial statements include the accounts of Leapfrog Smart Products, Inc., Colorado, Leapfrog Smart Products, Inc. Florida, Conduit Healthcare Solutions, Inc., Leapfrog Global IC Products, Inc. and Leapfrog China, Inc. (collectively, the "Company"). In the first quarter of 2001, Leapfrog Merger, Inc. changed its name to Leapfrog Smart Products, Inc. The Company's 50% ownership interest in Smart Products International Pte., Ltd. is accounted for on the equity method. All significant intercompany transactions and balances have been eliminated in the consolidated financial statements.

These unaudited statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-QSB and of item 310 (b) of Regulation S-B. Accordingly, they do not include all of the information and footnotes necessary for a fair presentation of financial condition, results of operations and cash flows in conformity with generally accepted accounting principles. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the results of operations for the periods presented have been included. These unaudited statements should be read in conjunction with the Company's Annual Report on Form 10-KSB, which contains audited financial statements and notes thereto, together with Management's Discussion and Analysis, for the years ended December 31, 2000 and 1999. Operating results for the nine-month and three-month periods ended September 30, 2001 are not necessarily indicative of the results that may be expected for the full year.

Development Stage Company

Since its inception, the Company's planned principal operations have not yet begun to produce significant revenue; accordingly, the Company is considered to be a development stage enterprise. The Company has elected to expense rather than capitalize most of its development costs.

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue and Expense Recognition

Revenues are generally recognized when the service has been performed and related costs and expenses are recognized when incurred. Contracts for the development of software and installation of the related hardware that extend over more than one reporting period are accounted for using the percentage-of-completion method of accounting. Revenue recognized at the financial statement date under these contracts is that portion of the total contract price that costs expended to date bears to the total anticipated final cost, based on current estimates of cost to complete. Revisions in total costs and earnings estimated during the course of the contract are reflected in the accounting period in which the circumstances necessitating the revision become known. At the time a loss on a contract becomes known the entire amount of the estimated loss is recognized in the financial statements. Costs attributable to contract disputes are carried in the accompanying balance sheet only when realization is probable. Amounts received on contracts in progress in excess of the revenue earned, based upon the percentage of completion method, are recorded as deferred revenue and the related costs and expense incurred are recorded as deferred costs.

In 2000, the Company entered into a contract with the U.S. General Services Administration (GSA) to supply GSA with hardware and software products related to Smart card technologies and applications. Significant portions of these contracts may be fulfilled by independent dealers (the Dealers) authorized by the Company and GSA. Revenues earned under the GSA contract are recorded by the Company at the gross amount billed to GSA and the corresponding cost of sales are recorded at the amount serviced by the Dealers. Revenues recognized under the GSA contract during the nine- month periods ended September 30, 2001 and 2000 approximated $586,000 and $449,000, respectively. Cost of sales recognized under the GSA contract during the nine-month periods ended September 30, 2001 and 2000 approximated $563,000 and $436,000, respectively.

Net Loss Per Share of Common Stock

The basic and diluted net loss per common share in the accompanying consolidated statements of operations are based upon the net loss after the deduction of preferred dividends and the accretion of the redemption value of redeemable preferred stock divided by the weighted average number of common shares outstanding during the periods presented. Diluted net loss per common share is the same as basic net loss per common share since the inclusion of all potentially dilutive common shares that would be issuable upon the exercise of outstanding stock options and the convertible preferred stock and promissory notes would be anti-dilutive.

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Continued Operations

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. As shown in the accompanying financial statements during the three-month periods ended September 30, 2001 and 2000, the Company incurred losses of approximately $1.02 million and $1.74 million, respectively, and had a deficiency in working capital of approximately $5.46 million at September 30, 2001. The Company incurred losses of $3.8 million and $4.5 million for the nine months ended September 30, 2001 and September 30, 2000, respectively. These factors, among others, may indicate the Company will be unable to continue as a going concern for a reasonable period of time. The accompanying consolidated financial statements do not include any adjustments relating to the outcome of this uncertainty.

Liquidity and Plan of Operations

At September 30, 2001, the Company had cash of approximately $8,000 and a deficiency in working capital of $5.46 million.

The Company has a limited operating history and its prospects are subject to the risks, expenses and uncertainties frequently encountered in new and rapidly evolving markets such as Smart card products and services. These risks include the failure to develop and extend the Company's products and services, the rejection of such services by Smart card customers, vendors and/or advertisers, the inability of the Company to maintain and increase its customer base, as well as other risks and uncertainties. In the event that the Company does not successfully implement its business plan, certain assets may not be recoverable.

The Company's continuation as a going concern is dependent upon its ability to generate sufficient cash flow to meet its obligations on a timely basis. The Company's primary source of liquidity has been through the private placement of equity and debt securities. The Company has continued its effort to explore possibilities with respect to raising working capital through additional equity and/or debt financings in the near future. Subsequent to September 30, 2001 through December 4, 2001, the Company received proceeds of approximately $295,000 from the issuance of notes payable. During the same period, the Company received $3,000 in net proceeds from the exercise of employee stock options for 12,000 shares.

However, there can be no assurance that the Company will be successful in achieving profitable operations or acquiring additional capital or that such capital, if available, will be on terms and conditions favorable to the Company. Based upon its current business plan, the Company believes that it will generate sufficient cash flow through operations and external sources of capital to continue to meet its obligations. If anticipated financing transactions and operating results are not achieved, management has the intent and believes that it has the ability to delay or reduce expenditures so as not to require additional financial resources, if such resources were not available on terms acceptable to the Company.

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Reclassifications

Certain amounts in the 2000 financial statements have been reclassified to conform with the 2001 presentation.

NOTE 2 - NOTES PAYABLE

In the first quarter of 2001, the Company issued a note to a shareholder and noteholder for $2 million to be funded in various installments from January 25, 2001 through May 15, 2001. As of June 30, 2001, $2 million had been received. The note is collateralized by the assets of the Company. Interest accrues at 12% and is due and payable quarterly beginning July 1, 2001. The note matures on July 1, 2002. The note or any portion thereof, is convertible into shares of the Company's stock at the rate of $1.00 per share. As part of this financing agreement, the noteholder received an option to purchase up to 1,000,000 shares of the Company's common stock at $1.00 per share through June 30, 2002. These options were valued at $157,000. The value is recorded as a discount on the issuance of debt and will be amortized to interest expense through the due date of the note. The interest expense recognized in the nine months ended September 30, 2001 and the quarter ended September 30, 2001 was $67,000 and $30,000, respectively. Proceeds from the note were used to repay the $200,000 remaining balance on a note that was collateralized by the assets of the Company that was due in January 2000. The holder of this note and a second note in the amount of $100,000 has agreed to accept $1 million in cash with the remaining principal and accrued interest converted into common stock at the rate of $1.00 per share upon the Company's receipt of funds from a private placement transaction. There can be no assurance that the Company will be successful in raising these funds from a private placement transaction.

During the quarter ended September 30, 2001, the Company paid off part of the principal and interest of a $100,000 note with a bank through a series of installments. The note matures on October 1, 2002. The Company also received proceeds of approximately $84,000 from the issuance of a note during the quarter. The interest rate is 8% per annum. Principal and interest are due on the maturity date of the note which is December 31, 2002.

Cash paid for interest during the three months ended September 30, 2001 and 2000 was $1,615 and $17,447, respectively. Cash paid for interest during the nine months ended September 30, 2001 and 2000 was $91,750 and $59,237, respectively.

All notes payable remain past due at September 30, 2001 except for the $100,000 note with a bank, a $100,000 note to a related party which matures on December 31, 2001, and the approximate $84,000 note which was issued during the quarter ended September 30, 2001. The Company is attempting to work with noteholders to extend the due dates or change the terms.

NOTE 3 - REDEEMABLE CONVERTIBLE PREFERRED STOCK

During the second quarter of 2001, the Company issued an aggregate of 50,000 shares of its Series B Convertible Preferred stock for cash and received proceeds of $50,000. The holders of Series B Convertible Preferred Stock are entitled to cumulative dividends at the rate of 7% per annum. As of September 30, 2001, dividends in arrears total approximately $1,000. Each share is convertible to one share of freely tradable common stock at any time after one year. Holders of the Series B Convertible Preferred Stock have the right to "put" all preferred shares back to the Company on the first anniversary date at $1.25 per share or at $2.00 per share on the second anniversary date. The excess of liquidation value over the carrying value of the Series B convertible redeemable preferred stock is being amortized over the two-year term of the redeemable option. The cumulative amount of accretion as of September 30, 2001 is approximately $3,600. The Series B Convertible Preferred Stock is offered at $50,000 per unit to accredited investors. Each unit subscribed provides for 16,667 options for common stock exercisable at any time for three years at the exercise price of $1.00 per share.

NOTE 4 - STOCKHOLDERS' EQUITY

Issuances of Common or Preferred Stock

After the merger, the Company issued 125,000 shares of Series A Convertible Preferred Stock and received net proceeds of $480,000. The holders of the Series A Preferred Shares are entitled to cumulative dividends at the rate of 6% per annum. As of September 30, 2001, dividends in arrears total approximately $46,000. Each share of Series A convertible Preferred Stock is convertible into one share of common stock at the election of the holder thereof. The Company may require mandatory conversion of all, but not less than all, of the Series A Preferred shares on or after the first anniversary of the initial sale if certain stock trading prices are attained or if there is a reorganization of the Company involving an exchange of its common stock for shares of a United States domiciled corporation the shares of which are traded on a national exchange or an the NASDAQ national market system. For as long as at least 50% of the Series A Convertible Preferred shares are outstanding, the holders thereof may elect one board member to the Company's board of directors.

During the nine months ended September 30, 2001, the Company issued an aggregate of 1,011,000 shares of its common stock including shares issued upon the exercise of stock options and received net proceeds of approximately $528,000. During the three months ended September 30, 2001, the Company issued an aggregate of 721,350 shares of its common stock including shares issued upon the exercise of stock options and received net proceeds of approximately $327,000.

The shares issued to Albara shareholders in the merger consisted of 616,797 shares of common stock and 195 shares of preferred stock. The preferred stock is Series F and is entitled to receive dividends on a pro rata basis with holders of common stock. These holders are entitled to a $100 per share preference on any liquidation of the Company and shall share pro rata with the common stockholders in any remaining amounts distributed. Each share is convertible into 15 shares of common stock after August 31, 1993.

NOTE 4 - STOCKHOLDERS' EQUITY (CONTINUED)

Warrant

On January 31, 2000 the Company entered into a consulting agreement with the former majority shareholder of Albara. As part of the agreement, this shareholder would receive, after performing certain consultation services, the right to a warrant for 500,000 shares of common stock at $3.50 per share. If the warrant had been issued, it would expire on January 31, 2010. The exercise price of $3.50 is adjusted to $.035 in the event the Company has not closed an equity offering raising an aggregate of at least $2,500,000 by June 29, 2000. The Company is in litigation contesting the failure to provide consideration for the warrant.

NOTE 5 - LEGAL PROCEEDINGS

The Company is party to several legal proceedings. However, management does not believe the ultimate outcomes to any of these actions will have a material impact to the Company's financial position and there have been no material changes since the end of last quarter in the status of the proceedings.

NOTE 6 - SUBSEQUENT EVENTS

The Company is in the process of finalizing a private placement with accredited investors. Proceeds of the private placement, if successful, will be used for working capital, debt reduction and to expand sales and marketing in the healthcare and security industries. The Company is also exploring other possibilities with respect to raising working capital through additional equity and/or debt financings in the near future.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS OR PLAN OF OPERATION

The following discussion should be read in conjunction with the Financial Statements and notes thereto.

PLAN OF OPERATION

LEAPFROG did not have significant sources of working capital since inception except for the sale of stock to individuals and the issuance of short-term notes payable while it was a private company. On February 18, 2000, LEAPFROG merged with Albara Corporation through a reverse acquisition in which Albara acquired LEAPFROG and the existing shareholders of LEAPFROG obtained control of Albara. Even with the completion of this business combination transaction, there can be no assurance that the combined companies will have sufficient funds to undertake any significant development, marketing and manufacturing activities. Accordingly, the Company is being required to seek additional debt or equity financing or funding from third parties, in exchange for which the Company might be required to issue a substantial equity position.

During the six months ended June 30, 2001, the Company received $2 million in proceeds from the note issued in the first quarter of the year to a shareholder and noteholder. This note was funded in various installments from January 25, 2001 through May 15, 2001. The note is secured by the assets of the Company. Interest accrues at 12% and is due and payable quarterly beginning July 1, 2001. The note matures on July 1, 2002. The note or any portion thereof, is convertible into shares of the Company's stock at the rate of $1.00 per share. As part of this financing agreement, the noteholder received an option to purchase up to 1,000,000 shares of the Company's common stock at $1.00 per share through September 30, 2002.

During the quarter ended September 30, 2001, the Company paid off part of the principal and interest of a $100,000 note with a bank through a series of installments. The note matures on October 1, 2002. The Company also received proceeds of approximately $84,000 from the issuance of a note during the quarter. The interest rate is 8% per annum. Principal and interest are due on the maturity date of the note which is December 31, 2002.

All notes payable remain past due at September 30, 2001 except for the $100,000 note with a bank, the $100,000 note to a related party which matures on December 31, 2001, and the approximate $84,000 note which was issued during the quarter ended September 30, 2001. The Company is attempting to work with noteholders to extend the due dates or change the terms.

For the three months ended September 30, 2001, the Company issued an aggregate of 721,350 shares of its common stock including shares issued upon the exercise of stock options and received net proceeds of approximately $327,000.

For the three months ended September 30, 2000, shares of common stock totaling 1,129,619 were issued for cash of approximately $1.4 million for both the exercise of stock options and the private placements of stock with individuals.

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For the period of January 1, 2001 through September 30, 2001, total additional debt of approximately $2.2 million was issued to third parties, 1,011,000 shares of common stock were issued for cash and on the exercise of stock options for approximately $528,000 in net proceeds and 50,000 shares of Series B Convertible Redeemable Preferred Stock were issued for net proceeds of $50,000.

For the period of January 1, 2000 through September 30, 2000, total additional debt of $750,000 was issued to third parties and 1,595,119 shares of restricted common stock were issued for approximately $2.7 million and 125,000 shares of convertible preferred stock were issued for net proceeds of $480,000.

The Company is in the process of finalizing a private placement with accredited investors. Proceeds of the private placement, if successful, will be used for working capital, debt reduction and to expand sales and marketing in the healthcare and security industries.

There is no assurance that the Company will be able to obtain additional financing on terms acceptable to the Company. If Management is successful in obtaining additional funding, these funds will be used primarily to provide working capital needed for repayment of outstanding notes payable, software development, sales and marketing expense, to finance research, development and advancement of intellectual property concerns and for general administration.

RESULTS OF OPERATIONS

Revenues and Gross Profits:

LEAPFROG is a development stage company with revenues just beginning to be recognized. The Company has elected to expense rather than capitalize most of its development costs. Revenues for the nine months ended September 30, 2001 decreased $86,000 to $716,000 from the $802,000 reported for the nine months ended September 30, 2000. Revenues for the three months ended September 30, 2001 decreased $499,000, from $635,000 to $136,000 compared to the quarter ended September 30, 2000. The decrease in revenues in the third quarter of 2001 was attributable primarily to a decrease in purchases by the U.S. Government made through the Company's GSA contract. Gross margin for the three months ended September 30, 2001 was $6,400 or 4.7% of revenue. This margin can be broken down into the margin on the GSA revenues, which was 4%, and the margin on all other revenues, which was 84%. Gross margin for the nine months ended September 30, 2001 was $81,000 or 11.3% of revenue. This margin can be broken down into the margin on GSA revenues, which was 4%, and the margin on all other revenues, which was 36%. The margins on the GSA contract revenues are lower since the sales are currently being made through the contract using an agent company so the net to the Company is usually 4%. The margins on other revenues have improved as economies of scale have begun to be realized on additional installations of the Company's software solutions.

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Total Operating Expenses:

Total operating expenses for the quarter ended September 30, 2001 decreased $836,000 from $1.735 million to $899,000, a 48% decrease compared to the same period in 2000. This decrease is associated with decreases in personnel and related expenses, consulting fees and general and administrative expenses.

Total operating expenses for the nine months ended September 30, 2001 decreased $680,000 from $4.26 million to $3.58 million, a 16% decrease compared to the same period in 2000. This decrease is associated with decreases in consulting fees and general and administrative expenses. This decrease was partially offset by the increase in personnel and related expenses for the nine-month period.

Personnel and related expenses decreased $157,000 or 21% to $594,000 for the quarter ended September 30, 2001 compared to $751,000 for the same period in 2000. This net decrease was primarily due to a reduction in staff in the third quarter of 2001.

Personnel and related expenses increased $230,000 or 11.6% to $2.21 million for the nine months ended September 30, 2001 compared to $1.98 million for the same period in 2000. This net increase was due to a higher average number of staff, increased salaries and compensation expense recognized from the exercise of stock options compared to the same period of 2000.

Consulting fees decreased by $361,000 from the $412,000 incurred for the quarter ended September 30, 2000 to $51,000 for the quarter ended September 30, 2001. Consulting fees decreased by $427,000 from the $635,000 incurred for the nine months ended September 30, 2000 to $208,000 for the nine months ended September 30, 2001. The expenses in 2000 related primarily to fees paid to individuals and companies that assisted the Company in identifying potential contract opportunities and recruiting distributors and value added resellers. Additionally, the consulting fees also consisted of amounts paid for services in maintaining a public market presence. In 2001, the Company outsourced less of these services to consultants.

General and administrative expenses decreased to $224,000 for the quarter ended September 30, 2001 from $550,000 for the same period in 2000. This $326,000 or 59% decrease was due in part to decreased legal and other professional costs, trade show expenses and travel expenses.

General and administrative expenses decreased to $1.08 million for the nine months ended September 30, 2001 from $1.57 million for the same period in 2000. This $490,000 or 31% decrease was due in part to decreased legal and other professional costs and travel expenses.

Depreciation and amortization expenses increased by $8,000 or 36% to $30,000 for the quarter ended September 30, 2001 compared to $22,000 for the same period in 2000. Depreciation and amortization expenses increased by $4,000 or 5.8% to $73,000 for the nine months ended September 30, 2001 compared to $69,000 for the same period in 2000. Assets purchases have been close to the amount of assets disposed of and becoming fully depreciated accounting for the stable depreciation expense.

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Other income and expense:

Interest expense for the quarter ended September 30, 2001 increased $68,000 from $60,000 to $128,000 when compared to the same period in 2000. This increase was due primarily to the increase in notes payable balances. Interest expense for the nine months ended September 30, 2001 increased $3,000 from $312,000 to $315,000 when compared to the same period in 2000.

In the first quarter of 2001, the Company issued a note to a shareholder and noteholder for $2 million to be funded in various installments from January 25 through May 15, 2001. As part of this financing agreement, the noteholder received an option to purchase up to 1,000,000 shares of the Company's common stock at $1.00 per share through June 30, 2002. These options were valued at $157,000. The value is recorded as a discount on the issuance of debt and will be amortized to interest expense through the maturity date of the note which is July 1, 2002. The interest expense recognized in the nine months ended September 30, 2001 and the quarter ended September 30, 2001 was $67,000 and $30,000, respectively.

In January of 2000, $550,000 in debentures were issued with 75,000 shares of common stock issued as an incentive to enter into these agreements. These shares resulted in $56,250 in interest expense being recorded. Also, included in interest expense was $55,000 attributable to the value of the stock options issued with the $100,000 related party note on April 28, 2000.

Net loss:

The net loss for the quarter ended September 30, 2001 decreased by $720,000 from $1.74 million to $1.02 million, a 41% decrease compared to the quarter ended September 30, 2000. Net loss per share of common stock decreased from $.24 per share in 2000 to $.11 in 2001. This decrease is due to the decrease in losses realized and to the increase in the weighted average number of common shares outstanding from 7,265,169 for the quarter ended September 30, 2000 to 9,767,261 for the quarter ended September 30, 2001.

The net loss for the nine months ended September 30, 2001 decreased by $660,000 from $4.46 million to $3.8 million, a 15% decrease compared to the nine months ended September 30, 2000. Net loss per share of common stock decreased from $.70 per share in the first nine months of 2000 to $.41 in the same period for 2001. This decrease is due to the decrease in losses realized and to the increase in the weighted average number of common shares outstanding from 6,388,171 for the nine months ended September 30, 2000 to 9,259,191 for the nine months ended September 30, 2001.

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LIQUIDITY AND CAPITAL RESOURCES

Net cash used by operating activities decreased $800,000 from $3.3 million for the nine months ended September 30, 2000 to $2.5 million for the nine months ended September 30, 2001. The decrease is primarily due to lower net loss, lower receivables and lower prepaid expenses offset by the common stock and stock options issued for services and interest and the increase in accounts payable and accrued expenses.

Net cash used for investing activities decreased from $197,000 in the first nine months of 2000 compared to $56,000 in the same period of 2001. The decrease was primarily due to less fixed assets acquisitions.

Net cash provided by financing activities decreased $1.06 million from $3.52 million for the nine months ended September 30, 2000 to $2.46 million for the nine months ended September 30, 2001. Financing activities during the first nine months of 2001 consisted primarily of the issuance of notes payable of approximately $2.2 million that was partially used to pay down debt by

$313,000. The Company also received proceeds of $578,000 from issuing common and preferred stock. Financing activities during the first nine months of 2000 included the issuance of common and preferred stock providing $3.2 million in the aggregate and the issuance of notes payable and related-party borrowings, which provided $842,000 offset by $475,000 in repayments of existing notes payable.

In the past, LEAPFROG's Management has been successful in attracting accredited investors who have purchased newly issued common stock. However, there can be no assurance that the Company will be able to obtain additional equity financing on similar terms in the future. Over the past three years much of LEAPFROG's debt financing has been short-term notes payable. These notes can only be repaid if the Company successfully generates significant revenues or raises additional equity or debt financing. In addition to the cash requirement associated with repaying these notes, LEAPFROG will not be able to mount an effective national marketing campaign for its products without an additional infusion of capital. There can be no assurance that any additional funds will be available to the Company to allow it to repay its outstanding debt and to cover the expenses associated with executing its sales and marketing plan.

Y2K COMPLIANCE

LEAPFROG concluded its efforts concerning its exposure relative to year 2000 issues for both information and non-information technology systems. Management actively monitors the status of the readiness program of the Company. LEAPFROG's out of pocket costs associated with becoming Year 2000 compliant were not significant. These costs were expensed as incurred, and the Company does not anticipate any additional material expenditure as a result of Year 2000 issues. Based on operations since January 1, 2000, including the leap year date of February 29, 2000, the Company has not experienced any significant disruption or change, and does not expect any significant impact to its ongoing business a result of the Year 2000 issue. Additionally, the Company is not aware of any significant Year 2000 issues or problems that have arisen for its significant customers, vendors or service providers. As there can be no assurance that the

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Company's efforts to achieve Year 2000 readiness have been completely successful or that customers, vendors and service providers will not experience Year 2000 related failures in the future, the Company will continue to monitor its exposure to Year 2000 issues and will leave its contingency plans in place in the event that any significant Year 2000 related issues arise.

FORWARD LOOKING STATEMENT

This Management's Discussion and Analysis of Financial Condition and Results of Operations includes a number of forward-looking statements that reflect Management's current views with respect to future events and financial performance. Those statements include statements regarding the intent, belief or current expectations of LEAPFROG and members of its management team as well as the assumptions on which such statements are based. Prospective investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risk and uncertainties, and that actual results may differ materially from those contemplated by such forward-looking statements. Readers are urged to carefully review and consider the various disclosures made by the Company in this report and in the Company's other reports filed with the Securities and Exchange Commission. Important factors currently known to Management could cause actual results to differ materially from those in forward-looking statements. The Company undertakes no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes in the future operating results over time. The Company believes that its assumptions are based upon reasonable data derived from and known about its business and operations and the business and operations of LEAPFROG. No assurances are made that actual results of operations or the results of the Company's future activities will not differ materially from its assumptions.

PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company filed a lawsuit styled Leapfrog Smart Products, Inc. v. Real Provencher , in the U.S. District Court of the Middle District of Florida, Orlando Division with the following claims: 1) breach of contract under a Consulting Agreement; 2) breach of contract under the terms of a Bleed Out Agreement; 3) violation of Rule 16 of the Securities Act of 1934; 4) fraudulent misrepresentation and common law fraud; and 5) violation of Rule 144 of the Securities Act of 1934. The Company alleged compensatory damages, costs, and further relief, as the court finds appropriate. The Florida Court has transferred venue to the U.S. District Court for the Southern District of Texas, Houston Division and the two cases have been consolidated.

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Real Provencher v. Leapfrog Smart Products, Inc., f/k/a Albara Corporation, and American Securities Transfer Incorporated was filed, after the Company's suit, in the U.S. District Court for the Southern District of Texas, Houston Division. Plaintiff, a shareholder of Albara, now Leapfrog, has filed the following claims against the Company: 1) the Company breached its statutory duty to register and transfer Plaintiff's shares in the Company; 2) the Company violated his statutory right under Rule 144(k) of the Securities Act of 1934 to terminate restrictions to sell his shares; 3) the Company committed common law and statutory fraud; 4) breach of contract under a Bleed Out Agreement; 5) and tortuous interference with Plaintiff's contract to sell 77,300 shares of stock.

As part of the Consulting Agreement with Provencher, after services are rendered, a warrant would be issued for the right to purchase 500,000 shares of common stock at $3.50 per share on or after April 30, 2000. If the warrant had been issued, it would expire on January 31, 2010. The exercise price of $3.50 is adjusted to $0.035 in the event the Company has not closed an equity offering raising an aggregate of at least $2.5 million by July 16, 2000. Although Provencher has not attempted to exercise the warrant, as part of the lawsuit the Company is attempting to have the warrant declared null and void due to the alleged non-performance under the Consulting Agreement.

Discovery is underway in the case. We are unable to determine the likelihood of an unfavorable outcome in this case nor are we able to estimate the potential loss to the Corporation at this time. Accordingly, the financial statements include no provision or liability related to the ultimate outcome of this matter.

The lessor of a portion of the Company's former office space has sued the Company for breach of contract alleging the Company's failure to pay rent. Damages requested are approximately $70,000 plus attorney's fees and costs. The Company brought a counter suit against the lessor for a declaratory action, breach of lease, tortuous interference with an advantageous business relationship, and breach of good faith and fair dealings regarding reletting the property. The Company has accrued an insignificant portion of the lessor's claims in an amount equal to the unpaid lease payments that would have been due under the lease through December 31, 2000. No other amounts have been recorded in the accompanying financial statements for this uncertainty, as management cannot reasonably estimate the ultimate outcome.

The Company is party to a lawsuit brought by Andre David Blaquier in the Circuit Court of the Fifth Judicial Circuit in Florida regarding repayment of $30,000 in notes plus interest due to him from the Company.

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ITEM 2. CHANGES IN SECURITIES

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) EXHIBITS

The following documents are filed herewith or have been included as exhibits to previous filings with the Commission and are incorporated herein by this reference:

	Exhibit No.	Exhibit
###	2.1	Agreement and Plan of Merger
##	3(a)	Articles of Incorporation
##	3(b)	Bylaws
#	4(a)	Agreements Defining Certain Rights of Shareholders
#	4(b)	Specimen Stock Certificate
#	10(a)	Pre-incorporation Consultation and Subscription Agreement
##	10.1	Consultation Services Agreement
##	10.2	Legal Services Engagement Agreement
###	10.3	Bleed-Out Agreement

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###	10.4	Consulting Agreement
###	10.5	Warrant Agreement
###	10.6	Registration Rights Agreement
x	11	Statement re Computation of Earnings per Share [required unless the computation can be clearly determined from financials]
####	16	Letter on Change in Certifying Accountant
x	21	Subsidiaries of the Registrant
x	27	Financial Data Schedule
#	99.1	Safe Harbor Compliance Statement

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x filed herewith

previously filed with the Company's Definitive Information Statement on Schedule 14C on January 18, 2000.

previously filed with the Company's Registration Statement on Form S-8 on February 29, 2000

previously filed with the Company's Form 8-K dated March 8, 2000

previously filed with the Company's Form 8-K dated March 17, 2000

(b) REPORTS ON FORM 8-K

The Company filed the following reports on Form 8-K during the third quarter of the 2001 fiscal year:

Current Report on Form 8-K dated August 16, 2001

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SIGNATURES

In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

LEAPFROG SMART PRODUCTS, INC.

By: /s/ Randolph Tucker
Randolph Tucker, Chairman

Date: December 4, 2001

In accordance with the Exchange Act, this report has been signed below by the following persons in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Randolph Tucker	Chairman	December 4, 2001
Randolph Tucker		