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5B TECHNOLOGIES CORP
Form 10-Q
May 21, 2001

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE

SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2001

COMMISSION FILE NUMBER 0-27190

5B TECHNOLOGIES CORPORATION
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE
(STATE OR OTHER JURISDICTION OF
INCORPORATION OR ORGANIZATION)

11-3529387
(I.R.S. EMPLOYER IDENTIFICATION NO.)

100 SUNNYSIDE BOULEVARD, WOODBURY, NEW YORK
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)

11797
(ZIP CODE)

(516) 677-6100
(REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE)

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

NUMBER OF SHARES OUTSTANDING AT MAY 15, 2001:

2,174,065 SHARES OF COMMON STOCK, PAR VALUE \$0.04 PER SHARE.

5B TECHNOLOGIES CORPORATION

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MARCH 31, 2001

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PART I: FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

5B TECHNOLOGIES CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

| | March 31, 2001 | December 31, 2000 |
|---|-------------------|----------------------|
| ASSETS | (Unaudited) | (Restated) |
| ----- | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 695,327 | \$ 1,156,436 |
| Investments available for sale (includes \$256,000 and \$298,000 respectively, restricted as collateral) | 503,835 | 499,778 |
| Accounts receivable, net of allowance for doubtful accounts of \$146,000 | 947,720 | 1,501,523 |
| Note receivable for services provided | 427,590 | 427,590 |
| Other current assets | 117,625 | 64,385 |

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| | | |
|--|---------------------|---------------------|
| Total current assets | 2,692,097 | 3,649,712 |
| Goodwill & other intangibles, net | 897,290 | 939,900 |
| Net assets of discontinued operations | 661,619 | 1,247,094 |
| Other assets | 524,101 | 509,610 |
| TOTAL ASSETS | \$ 4,775,107 | \$ 6,346,316 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Notes payable | \$ 923,310 | \$ 850,159 |
| Accounts payable | 711,924 | 1,129,308 |
| Accrued expenses | 158,807 | 332,273 |
| Unearned sales revenue | 120,401 | 174,527 |
| Total current liabilities | 1,914,442 | 2,486,267 |
| Notes payable | 10,427 | 11,928 |
| TOTAL LIABILITIES | 1,924,869 | 2,498,195 |
| REDEEMABLE PREFERRED STOCK | 1,250,000 | 1,250,000 |
| COMMITMENTS AND CONTINGENCIES | | |
| STOCKHOLDERS' EQUITY: | | |
| Preferred stock, \$.01 par value; 5,000,000 shares authorized, 1,000 shares issued and outstanding | -- | -- |
| Common stock, \$.04 par value, 17,500,000 shares authorized, 2,198,565 and 2,165,036 shares issued and outstanding, respectively | 87,943 | 86,601 |
| Additional paid-in capital | 14,574,233 | 14,525,450 |
| Stock subscription receivable | (812,500) | (812,500) |
| Accumulated deficit | (12,198,833) | (11,150,825) |
| Treasury stock at cost, 24,500 shares | (50,605) | (50,605) |
| TOTAL STOCKHOLDERS' EQUITY | 1,600,238 | 2,598,121 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 4,775,107 | \$ 6,346,316 |

See accompanying notes to consolidated financial statements.

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5B TECHNOLOGIES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE THREE MONTHS ENDED MARCH 31,

UNAUDITED

| | |
|-----------|-----------|
| March 31, | March 31, |
| 2001 | 2000 |

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| | (Unaudited) | (Unaudited) |
|--|----------------|----------------|
| Net sales | \$ 1,603,872 | \$ 1,916,310 |
| Cost of sales | 1,220,279 | 1,255,983 |
| ----- | | |
| Gross profit | 383,593 | 660,327 |
| ----- | | |
| Expenses: | | |
| Selling | 365,005 | 193,619 |
| General and administrative expenses | 807,270 | 730,023 |
| ----- | | |
| Total expenses | 1,172,275 | 923,642 |
| ----- | | |
| Loss from operations | (788,682) | (263,315) |
| Other income (expense): | | |
| Interest expense | (24,267) | (35,146) |
| Interest income | 11,733 | 9,233 |
| ----- | | |
| Loss before provision for (benefit from) income taxes and discontinued operations | (801,216) | (289,228) |
| State and local taxes | 19,806 | 944 |
| ----- | | |
| Loss from continuing operations | (821,022) | (290,172) |
| Discontinued operations: | | |
| Income (loss) from discontinued operations, net of income taxes of \$0 and \$80,892 respectively | (681,193) | (181,685) |
| Gain on disposal of discontinued operations | 472,957 | (856,198) |
| ----- | | |
| Net loss | \$ (1,029,258) | \$ (1,328,055) |
| Preferred dividends | (18,750) | -- |
| ----- | | |
| Net loss attributable to common shareholders | \$ (1,048,008) | \$ (1,328,055) |
| ----- | | |
| WEIGHTED AVERAGE COMMON SHARES OUTSTANDING | | |
| Basic and diluted | 2,160,016 | 2,135,500 |
| ----- | | |
| BASIC AND DILUTED LOSS PER COMMON SHARE: | | |
| Continuing operations | \$ (0.39) | \$ (0.13) |
| ----- | | |
| Discontinued operations | \$ (0.10) | \$ (0.49) |
| ----- | | |
| Net loss per share | \$ (0.49) | \$ (0.62) |
| ----- | | |

See accompanying notes to consolidated financial statements.

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5B TECHNOLOGIES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE THREE MONTHS ENDED MARCH 31,

UNAUDITED

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| | March 31, 2001 | March 31, 2000 |
|--|-------------------|-------------------|
| ----- | | |
| CASH FLOWS FROM OPERATING ACTIVITIES: | (Unaudited) | (Unaudited) |
| Net loss | \$ (1,029,254) | \$ (1,328,05 |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Loss from discontinued operations | 681,193 | 181,68 |
| (Gain) loss from disposal of discontinued operations | (472,957) | 856,19 |
| Depreciation and amortization | 60,157 | 69,69 |
| Issuance of options and warrants for services | -- | 16,30 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 553,803 | 117,08 |
| Other assets | (76,086) | (67,75 |
| Accounts payable | (85,788) | (61,41 |
| Accrued expenses | (246,345) | (198,14 |
| ----- | | |
| NET CASH USED IN OPERATING ACTIVITIES FROM CONTINUING OPERATIONS | (615,277) | (414,40 |
| ----- | | |
| NET CASH PROVIDED BY OPERATING ACTIVITIES FROM DISCONTINUED OPERATIONS | 277,352 | 1,221,08 |
| ----- | | |
| NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES | (337,925) | 806,67 |
| ----- | | |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of investments | (4,057) | (5,52 |
| Purchase of equipment | (9,192) | -- |
| ----- | | |
| NET CASH USED IN INVESTING ACTIVITIES FROM CONTINUING OPERATIONS | (13,249) | (5,52 |
| ----- | | |
| NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES OF DISCONTINUED OPERATIONS | (494,081) | 2,616,58 |
| ----- | | |
| NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES | (507,330) | 2,611,05 |
| ----- | | |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from sale of common stock | 50,124 | -- |
| Proceeds from notes payable | 161,481 | 142,62 |
| Repayment of notes payable | (421,428) | (412,16 |
| ----- | | |
| NET CASH USED IN FINANCING ACTIVITIES FROM CONTINUING OPERATIONS | (209,823) | (269,54 |
| ----- | | |
| NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES FROM DISCONTINUED OPERATIONS | 593,969 | (3,834,34 |
| ----- | | |
| NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES | 384,146 | (4,103,88 |
| ----- | | |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 1,156,436 | 1,003,75 |
| ----- | | |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 695,327 | \$ 317,60 |
| ===== | | |

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| | | | | |
|--|----|--------|----|--------|
| Cash paid for income taxes | \$ | 3,399 | \$ | 1,69 |
| Cash paid for income taxes for discontinued operations | \$ | 16,207 | \$ | 70,96 |
| Cash paid for interest | \$ | 24,267 | \$ | 35,14 |
| Cash paid for interest for discontinued operations | \$ | 49,574 | \$ | 271,13 |

See accompanying notes to consolidated financial statements.

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5B TECHNOLOGIES CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q and Regulation S-X related to interim period financial statements and, therefore, do not include all information and footnotes required by generally accepted accounting principles. However, in the opinion of management, all adjustments (consisting of normal recurring adjustments and accruals) considered necessary for a fair presentation of the financial position of 5B Technologies Corporation and subsidiaries (the "Company") at March 31, 2001 and its results of operations and cash flows for the three months ended March 31, 2001 and 2000, respectively, have been included (See Note 2).

The financial statements for the three months ended March 31, 2001 include the results of the Company and its wholly owned subsidiaries. All material intercompany balances and transactions have been eliminated.

The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the entire year.

Reference should be made to the annual financial statements, including footnotes thereto, included in the Company's Form 10-K for the fiscal year ended December 31, 2000.

2. DISCONTINUED OPERATION

On May 14, 2001, the Company sold its legal staffing, which was maintained through a wholly owned subsidiary, Deltaforce Personnel Services, Inc. ("DeltaGroup"), for approximately \$1,500,000, plus 50% of DeltaGroup revenue in excess of \$7.25 million and \$7.5 million in the first and second years, respectively, after closing. Accordingly, DeltaGroup has been presented as a discontinued operation for the three months ended March 31, 2001, and the balance sheet as of December 31, 2000 and the statements of operations and cash flows for the three months ended March 31, 2000 have been restated to conform to this presentation. The loss on disposal of DeltaGroup includes provisions for estimated losses of approximately \$681,000 and a gain on sale, exclusive of contingent consideration, of approximately \$473,000, for a total loss of approximately \$208,000. The provision for estimated losses of approximately \$681,000 is based on management's estimate of future expenses relating to contractual obligations and other expenses related to the staffing business. Net sales for DeltaGroup were approximately \$1,823,000 and \$1,967,000 for the three months ended March 31, 2001 and 2000, respectively.

On May 2, 2000, the Company sold the majority of its lease portfolio (the "Assets"), which was maintained through a wholly owned subsidiary, Paramount Operations Inc. ("Paramount"), for approximately \$700,000 and the assumption

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of approximately \$6,117,000 of indebtedness related to the Assets. Accordingly, Paramount has been presented as a discontinued operation as of March 31, 2001 and December 31, 2000 and for the three months ended March 31, 2001 and 2000, respectively. The loss on disposal of Paramount

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includes provisions for estimated losses of approximately \$602,000 and a loss on sale of approximately \$254,000, for a total loss of approximately \$856,000. The provision for estimated losses of approximately \$602,000 is based on management's estimate of future income and expenses relating to the remaining lease portfolio and write-downs of certain related assets. Net sales for Paramount were approximately \$156,000 and \$1,588,000 for the three months ended March 31, 2001 and 2000, respectively.

The components of net assets of discontinued operation included in the Company's Consolidated Balance Sheets at March 31, 2001 and December 31, 2000, are as follows:

| | 2001 | 2000 |
|---|-------------|--------------|
| | ----- | ----- |
| DELTAFORCE PERSONNEL SERVICES, INC. | | |
| Accounts receivable | 869,927 | 932,219 |
| Other assets | 124,765 | 122,706 |
| Goodwill and intangibles | 1,017,454 | 1,056,772 |
| Accounts payable | (61,002) | (77,758) |
| Accrued expenses | (220,876) | (89,574) |
| Notes payable | (750,000) | (750,000) |
| | ----- | ----- |
| | 980,268 | 1,194,365 |
| | ----- | ----- |
| PARAMOUNT OPERATIONS INC. | | |
| Accounts receivable | 51,299 | 103,528 |
| Net investment in direct finance and sales-type leases | 3,692,785 | 3,198,704 |
| Assets held under operating leases, net of accumulated depreciation | 228,216 | 261,737 |
| Other assets | - | 162,000 |
| Accrued expenses | (404,057) | (380,317) |
| Notes payable | (57,744) | (76,384) |
| Obligations for financed equipment - non-recourse | (3,829,148) | (3,216,539) |
| | ----- | ----- |
| | (318,649) | 52,729 |
| | ----- | ----- |
| | \$ 661,619 | \$ 1,247,094 |
| | ===== | ===== |

3. LINES OF CREDIT

At March 31, 2001, the Company had two credit lines available:

TERM LOAN: In April 1998, Paramount entered into a \$500,000 term loan with a bank collateralized by \$600,000 in cash maintained in an investment account.

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Principal payments of approximately \$41,600 and interest are due on a quarterly basis through April 20, 2001. On July 20, 1999 the Company borrowed an additional \$215,000 as a demand note. Interest payments are being made on this additional borrowing and the Company is undergoing negotiations with the bank to establish repayment terms. As of March 31, 2001, approximately \$256,000 remained outstanding under these loans collateralized by up to \$600,000 in cash maintained in an investment account. Under the agreement, the Company was not in compliance with the debt covenant-requiring minimum net worth of at least \$5.5 million. The Company has obtained a

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waiver from the bank for non-compliance with the aforementioned covenant for the three months ended March 31, 2001.

5B GROUP EQUIPMENT ACQUISITION CREDIT FACILITY: 5B Group has a \$2,000,000 revolving line of credit agreement with a finance company secured by accounts receivable and inventory. Interest on outstanding borrowings accrues at the prime rate plus 1 1/2 %. Borrowings are limited to 85% of eligible accounts receivable, as defined. This facility allows the Company to purchase computer hardware from its vendors with net 30-day terms interest free. At the expiration of the net 30-day period, the Company has the option of paying the amount due or, provided the Company has sufficient eligible collateral, borrowing under the credit facility. As of March 31, 2001, 5B Group had \$487,000 outstanding under this line, of which approximately \$386,000 is classified as debt and approximately \$101,000 is included in accounts payable. Under the agreement, the Company's 5B Group subsidiary was not in compliance with the net profit after tax to revenue ratio of greater than 1%. Pursuant to this default the Company has received a forbearance agreement from the finance company which states that the credit facility has been reduced to \$500,000 and is payable in full by July 15, 2001. The Company is currently negotiating with the finance company to initiate a secured credit facility and it is also negotiating with its vendors to establish terms and plans to utilize, when closed, the Connecticut Bank of Commerce financing (see below) to replace this credit facility.

Each of the Company's two credit lines contains cross-default provisions, so that any uncured or unwaived default under any of these credit lines would cause there to be a default under the other credit lines.

As described above, the Company has received waivers from the lenders under the Term Loan as a result of the Company's non-compliance at March 31, 2001 with certain covenants under such facility. The Company believes that it will not satisfy these covenants in the future. The Company has regularly obtained waivers of compliance from the respective lenders under this facility, and believes that it will be able to obtain waivers in the future. However, if any waiver cannot be obtained in the future, that lender would be able to declare a default under its credit line, which would have the effect of also causing a default under the Company's other credit lines. Among other things, if such defaults were to occur, any or all of the lenders could declare all amounts, which aggregated approximately \$743,000 as of March 31, 2001, under its respective credit lines immediately due and payable.

On April 11, 2001 the Company received a banking commitment from the Connecticut Bank of Commerce ("CBC") and is currently finalizing the documents and expects to have the credit facilities in place shortly. The commitment extends two types of credit facilities:

5B GROUP REVOLVING CREDIT FACILITY: 5B Group will receive upon the closing of the financing a revolving credit facility secured by eligible accounts receivable, as defined. The term of the credit facility is two years from the date of closing. Borrowings are limited to 75% of eligible accounts

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receivable. The rate of interest charged on the facility will be 1 1/2% above the Wall Street prime commercial lending rate.

MEZZANINE FACILITY: 5B Technologies Corporation will receive upon the closing of the financing, a maximum mezzanine facility of \$1,500,000, to be used for future

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acquisitions and other agreed to purposes. The maximum amount of the mezzanine facility will be limited to 110% of the total cash, cash equivalents, marketable securities and accounts receivable of the Company less the outstanding amount of the revolving credit facility. Additionally, the mezzanine facility may not be utilized until either (a) the amount of the mezzanine facility to be used is secured by cash collateral acceptable to CBC, or (b) (i) the sale of certain material assets, (ii) 5B has demonstrated a return to profitability, and (iii) a settlement of the redeemable preferred stock. The mezzanine facility will mature within two years, or be rolled into the 5B Group revolving credit facility. The rate of interest charged on the facility will be 2% above the Wall Street prime commercial lending rate.

4. REDEEMABLE PREFERRED STOCK

On April 17, 2000, the Company received an equity investment of \$874,465 (\$1,000,000 less transaction costs of \$125,535) from La Vista Investors, LLC ("La Vista"), a fund managed by WEC Asset Management LLC, a New York-based investment company.

In connection with its investment, La Vista received (i) 1,000 shares of the Company's Series A 6% Convertible Preferred Stock, par value \$0.01 per share (the "Series A Preferred Stock"), and (ii) a warrant convertible into 100,000 shares of the Company's Common Stock at an exercise price of \$10.00 per share of Common Stock (which was deemed to have an immaterial fair value), subject to certain anti-dilution adjustments for stock splits, subdivisions, other similar events and certain below-market price issuances of Common Stock. Each share of Series A Preferred Stock is convertible into such number of shares of Common Stock as is determined by dividing \$1,000, plus the amount of any accrued and unpaid dividends, by the Conversion Price (as defined below) in effect at the time of conversion. The Conversion Price at which shares of Common Stock shall be deliverable upon conversion of Series A Preferred Stock, without the payment of additional consideration by the holder thereof, shall be the lower of (i) nine dollars (\$9.00) or (ii) 80% of the average of the three lowest Closing Bid Prices (as defined in the Certificate of Designations of the Series A Preferred Stock) of the Company's Common Stock during the thirty (30) trading days immediately preceding the date of notice from a holder of the Series A Preferred Stock of any such conversion. On the commitment date, the conversion price exceeded the market price of the Company's Common Stock. In August, 2000, the Company and the holders of the Company's Series A Preferred Stock agreed to exchange the Series A Preferred Stock for the Series B Preferred Stock on a one-for-one basis. The terms of the Series A Preferred Stock were identical to those of the Series B Preferred except that the holders of the Series A Preferred Stock had the right to vote together with the holders of Common Stock as a single class.

In addition to the right of the selling stockholder to voluntarily convert its Series B Preferred Stock into shares of our common stock, all unconverted shares of the Series B Preferred Stock will automatically convert into shares of common stock, at the then-applicable conversion formula, on April 17, 2003.

REDEMPTION RIGHTS OF REDEEMABLE PREFERRED STOCK

The Company may be obligated to redeem the Series B Preferred Stock in two types of situations: (1) if the number of shares issued upon conversion of the Series B Preferred Stock were to exceed 19.9% of our outstanding common stock, and (2) if we fail to conclude certain required actions or if certain enumerated events were to occur.

IF THE UNDERLYING SHARES EXCEED 19.9%. If the number of shares of common stock issued upon conversion of the Series B Preferred Stock and in lieu of cash dividends (see below for a description of this concept) exceeds 19.9% of our outstanding common stock, we must take, at our option, one of two actions: (i) redeem all of the remaining shares of Series B Preferred Stock at a price equal to 120% of the Liquidation Preference, as defined (ii) call a special meeting of the Company's stockholders to approve of the issuance of the common stock (and any other matters requiring stockholder approval under the applicable rules of the NASDAQ Stock Market) and use the Company's best efforts to obtain such approval.

The Company cannot predict which of the foregoing two alternatives it will elect.

In any event, the Company's ability to elect the first alternative (i.e., make a redemption at 120% of the Liquidation Value of the Series B Preferred Stock) will depend on numerous factors in the future, including whether it has sufficient funds to make such redemption. At December 31, 2000, the Series B Preferred Stock could be converted into 1,618,899 shares of Common Stock, which exceeds 19.9% (see above).

FAILURE TO CONCLUDE ACTIONS/OCCURRENCE OF EVENTS. The Company will be required to redeem the outstanding Series B Preferred Stock at a price equal to 125% of the Liquidation Preference as defined if any of the following events (among others) were to happen (unless the selling stockholder at the time agreed with the Company otherwise): (i) if the registration statement is not effective by September 27, 2000, (ii) if the Company breaches the terms of the Series B Preferred Stock and does not cure such breach within 10 days of notice to us of such breach, (iii) if the Company becomes bankrupt by court order or if we voluntarily institute bankruptcy proceedings or if other similar events occur (iv) if the Company defaults under any of our material contracts in our businesses or lose a final judgment, where the default or judgment is in excess of \$250,000, (v) if there is a Change of Control, as defined.

On September 28, 2000 the Company received notification from La Vista demanding redemption of outstanding Series B Preferred Stock in accordance with the terms of the Series B Preferred Stock due to the Company's failure to have a registration statement effective by September 27, 2000. Accordingly, the Company has increased the value of the redeemable preferred stock to \$1,250,000. The Company filed a registration statement relating to the Series B Preferred Stock and it was declared effective on February 16, 2001.

5. SEGMENT INFORMATION

The Company's results of operations are reviewed and managed through two segments (i) corporate overhead ("5B") and (ii) Internet, e-commerce and systems integration ("5B Group"). The accounting policies of the segments are the same as those described in the Summary of Significant Accounting Policies, which can be found on pages F-7 through F-11 of the Company's Annual Report on Form 10-K (for the year ended December 31, 2000).

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The following represents selected financial information for the Company's segments for the three months ended March 31, 2001 and 2000:

| | 5B | 5B Group | Total |
|--------------------|-------------|-------------|-------------|
| ----- | | | |
| Three months ended | | | |
| March 31, 2001 | | | |
| ----- | | | |
| Revenues | \$ -- | \$1,603,872 | \$1,603,872 |
| Cost of sales | -- | 1,220,279 | 1,220,279 |
| Selling | 49,536 | 315,469 | 365,005 |
| General and | | | |
| Administrative | 144,010 | 663,256 | 807,266 |
| Interest expense | 8,642 | 15,625 | 24,267 |
| Pre-tax loss | (190,455) | (610,757) | (801,212) |
| Assets | \$2,251,005 | \$2,524,102 | \$4,775,107 |
| | | | |
| Three months ended | | | |
| March 31, 2000 | | | |
| ----- | | | |
| Revenues | \$ -- | \$1,916,310 | \$1,916,310 |
| Cost of sales | -- | 1,255,983 | 1,255,983 |
| Selling | 14,275 | 179,344 | 193,619 |
| General and | | | |
| Administrative | 270,148 | 459,872 | 730,020 |
| Interest expense | 12,012 | 23,134 | 35,146 |
| Pre-tax loss | (287,205) | (2,023) | (289,228) |
| Assets | \$3,344,441 | \$3,001,875 | \$6,346,316 |
| ===== | | | |

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

The following discussion and analysis should be read in conjunction with, and is qualified in its entirety by, the unaudited financial statements, including the notes thereto, appearing elsewhere in this 10-Q.

RECENT DEVELOPMENTS

On May 14, 2001, the Company sold the majority of its assets related to its legal staffing subsidiary, Deltaforce Personnel Services, Inc. ("DeltaGroup"), for approximately \$1,500,000, plus 50% of DeltaGroup revenue in excess of \$7.25 million and \$7.5 million in the first and second years, respectively, after closing. Accordingly, DeltaGroup has been presented as a discontinued operation for the three months ended March 31, 2001, and the balance sheet as of December 31, 2000 and the statements of operations and cash flows for the three months ended March 31, 2000 have been restated to

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conform to this presentation. The loss on disposal of DeltaGroup includes provisions for estimated losses of approximately \$681,000 and a gain on sale, exclusive of contingent consideration, of approximately \$473,000, for a total loss of approximately \$208,000. The provision for estimated losses of approximately \$681,000 is based on management's estimate of future expenses relating to contractual obligations and other expenses related to the staffing business. Net sales for DeltaGroup were approximately \$1,823,000 and \$1,967,000 for the three months ended March 31, 2001 and 2000, respectively.

The sale of DeltaGroup was prompted by the Companies commitment to its technology subsidiary (5B Technologies Group, Inc., "5B Group") and the DeltaGroup's continued losses. 5B Technologies Corporation ("5B") originally purchased Deltaforce Personnel Services, Inc. in January 1998 and in July 1998 purchased RBW Staffing Inc. and merged its operations into Deltaforce Personnel Services, Inc. and renamed the entity DeltaGroup. At that time the Company planned to be a business solutions provider and offer staffing services in various areas. As 5B Group continued to expand the management of 5B felt that the focus of the Company was technology and that the DeltaGroup, being a legal staffing entity, did not fit the Companies mission and long-term objectives, which had changed since 1998. 5B also felt, that the DeltaGroup, being in a very specific niche market, was susceptible to downtrends in the economy, slow downs by law firms and an increase in unemployment. Based on these factors and a shift in 5B's mission and long-term objectives 5B decided to sell the DeltaGroup subsidiary. The sale will bring a new focus to the technology subsidiary, increased cash reserves and availability and improved financial results in the future.

RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2001 COMPARED TO THREE MONTHS ENDED MARCH 31, 2000

For the three months ended March 31, 2001, the Company recorded sales revenue of \$1.6 million; a \$300,000 decrease from the \$1.9 million recorded during the three months ended March 31, 2000. The decrease in sales at 5B Group is a result of the timing of new projects being authorized, which the Company believes is due to the economy.

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Cost of sales consists of all direct labor costs and other costs, such as payroll taxes, employee benefits, outside contractors and equipment purchases, related to each project or individual sale. For the three months ended March 31, 2001, the Company recorded cost of sales of \$1.2 million; a decrease of \$100,000 compared to the \$1.3 million recorded for the three months ended March 31, 2000. The reason for this decrease is the decrease in related sales and the product mix of the sales. There were fewer services and more equipment sales for the three months ended March 31, 2001 compared to the three months ended March 31, 2000 resulting in a lower gross profit.

Selling expense consists of all sales force salaries, commissions and associated costs. Selling expense for the three months ended March 31, 2001 was \$365,000, an 88% increase over the \$194,000 recorded in the comparable prior period. 5B Group reported selling expenses of \$315,000, or 20%, of revenue for the three months ended March 31, 2001 compared to \$179,000, or 9%, of revenue for the three months ended March 31, 2000. The increase in selling expenses for 5B Group is predominantly due to the addition of more salespeople.

General and administrative expenses totaled \$733,000 or 46%, of revenue for the three months ended March 31, 2001, representing an increase of \$3,000 compared to the \$730,000, or 38%, of revenue recorded during the three months

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ended March 31, 2000. 5B Group reported general and administrative expenses of \$663,000 or 41%, of revenue for the three months ended March 31, 2001 compared to \$460,000, or 24%, of revenue for the three months ended March 31, 2000. The increase is attributable to the Company's expansion and new facilities.

LIQUIDITY AND CAPITAL RESOURCES

As of March 31, 2001, the Company had \$1.2 million in cash and cash equivalents and investments available for sale. Substantially this entire amount was invested in interest-bearing savings accounts, money market accounts established by major commercial banks or in United States Government, other AA rated obligations and mutual funds. Primarily as a result of the continued investment in 5B Group and the acquisitions it made in prior years the Company experienced a decrease in net cash and investments available for sale during the three months ended March 31, 2001 of \$457,052.

The Company continues to use its cash balances to fund its operations. In order to expand its operations, which the Company is aggressively seeking to accomplish, the Company will need to utilize its cash balances to promote internal growth and fund potential future acquisitions. However, the Company is limited to its current cash balances for funding such internal growth and add-on acquisitions, unless the Company is able in the future to raise significant additional financing. There can be no assurance that the Company will be able to raise any such financing. Further, the Company's cash funds for acquisitions might be limited to the extent that the Company's current operations or the operations of any future acquisitions require the funding of losses or the incurrence of capital outlay.

At March 31, 2001, the Company had two credit lines available:

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TERM LOAN: In April 1998, Paramount entered into a \$500,000 term loan with a bank collateralized by \$600,000 in cash maintained in an investment account. Principal payments of approximately \$41,600 and interest are due on a quarterly basis through April 20, 2001. On July 20, 1999 the Company borrowed an additional \$215,000 as a demand note. Interest payments are being made on this additional borrowing and the Company is undergoing negotiations with the bank to establish repayment terms. As of March 31, 2001, approximately \$256,000 remained outstanding under these loans collateralized by up to \$600,000 in cash maintained in an investment account. Under the agreement, the Company was not in compliance with the debt covenant-requiring minimum net worth of at least \$5.5 million. The Company has obtained a waiver from the bank for non-compliance with the aforementioned covenant for the three months ended March 31, 2001.

5B GROUP EQUIPMENT ACQUISITION CREDIT FACILITY: 5B Group has a \$2,000,000 revolving line of credit agreement with a finance company secured by accounts receivable and inventory. Interest on outstanding borrowings accrues at the prime rate plus 1 1/2 %. Borrowings are limited to 85% of eligible accounts receivable, as defined. This facility allows the Company to purchase computer hardware from its vendors with net 30-day terms interest free. At the expiration of the net 30-day period, the Company has the option of paying the amount due or, provided the Company has sufficient eligible collateral, borrowing under the credit facility. As of March 31, 2001, 5B Group had \$487,000 outstanding under this line, of which approximately \$386,000 is classified as debt and approximately \$101,000 is included in accounts payable. Under the agreement, the Company's 5B Group subsidiary was not in compliance with the net profit after tax to revenue ratio of greater than 1%. Pursuant to this default the Company has received a forbearance agreement from the finance company which states that the credit facility has been reduced to \$500,000 and is payable in full by July 15, 2001. The company is currently negotiating with the finance company to

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initiate a secured credit facility and it is also negotiating with its vendors to establish terms and plans to utilize, when closed, the Connecticut Bank of Commerce financing (see below) to replace this credit facility.

Each of the Company's two credit lines contains cross-default provisions, so that any uncured or unwaived default under any of these credit lines would cause there to be a default under the other credit lines.

As described above, the Company has received waivers from the lenders under the Term Loan as a result of the Company's non-compliance at March 31, 2001 with certain covenants under such facility. The Company believes that it will not satisfy these covenants in the future. The Company has regularly obtained waivers of compliance from the respective lenders under this facility, and believes that it will be able to obtain waivers in the future. However, if any waiver cannot be obtained in the future, that lender would be able to declare a default under its credit line, which would have the effect of also causing a default under the Company's other credit lines. Among other things, if such defaults were to occur, any or all of the lenders could declare all amounts, which aggregated approximately \$743,000 as of March 31, 2001, under its respective credit lines immediately due and payable.

On April 11, 2001 the Company received a banking commitment from the Connecticut Bank of Commerce ("CBC") and is currently finalizing the documents and expects to have the credit facilities in place shortly. The commitment extends two types of credit facilities:

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5B GROUP REVOLVING CREDIT FACILITY: 5B Group will receive upon the closing of the financing a revolving credit facility secured by eligible accounts receivable, as defined. The term of the credit facility is two years from the date of closing. Borrowings are limited to 75% of eligible accounts receivable. The rate of interest charged on the facility will be 1 1/2% above the Wall Street prime commercial lending rate.

MEZZANINE FACILITY: 5B Technologies Corporation will receive upon the closing of the financing, a maximum mezzanine facility of \$1,500,000, to be used for future acquisitions and other agreed to purposes. The maximum amount of the mezzanine facility will be limited to 110% of the total cash, cash equivalents, marketable securities and accounts receivable of the Company less the outstanding amount of the revolving credit facility. Additionally, the mezzanine facility may not be utilized until either (a) the amount of the mezzanine facility to be used is secured by cash collateral acceptable to CBC, or (b) (i) the sale of certain material assets, (ii) 5B has demonstrated a return to profitability, and (iii) a settlement of the redeemable preferred stock. The mezzanine facility will mature within two years, or be rolled into the 5B Group revolving credit facility. The rate of interest charged on the facility will be 2% above the Wall Street prime commercial lending rate.

On April 17, 2000, the Company received an equity investment of \$874,465 (\$1,000,000 less transaction costs of \$125,535) from La Vista Investors, LLC ("La Vista"), a fund managed by WEC Asset Management LLC, a New York-based investment company.

In connection with its investment, La Vista received (i) 1,000 shares of the Company's Series A 6% Convertible Preferred Stock, par value \$0.01 per share (the "Series A Preferred Stock"), and (ii) a warrant convertible into 100,000 shares of the Company's Common Stock at an exercise price of \$10.00 per share of Common Stock (which was deemed to have an immaterial fair value), subject to certain anti-dilution adjustments for stock splits, subdivisions, other similar

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events and certain below-market price issuances of Common Stock. Each share of Series A Preferred Stock is convertible into such number of shares of Common Stock as is determined by dividing \$1,000, plus the amount of any accrued and unpaid dividends, by the Conversion Price (as defined below) in effect at the time of conversion. The Conversion Price at which shares of Common Stock shall be deliverable upon conversion of Series A Preferred Stock, without the payment of additional consideration by the holder thereof, shall be the lower of (i) nine dollars (\$9.00) or (ii) 80% of the average of the three lowest Closing Bid Prices (as defined in the Certificate of Designations of the Series A Preferred Stock) of the Company's Common Stock during the thirty (30) trading days immediately preceding the date of notice from a holder of the Series A Preferred Stock of any such conversion. On the commitment date, the conversion price exceeded the market price of the Company's Common Stock. In August, 2000, the Company and the holders of the Company's Series A Preferred Stock agreed to exchange the Series A Preferred Stock for the Series B Preferred Stock on a one-for-one basis. The terms of the Series A Preferred Stock were identical to those of the Series B Preferred except that the holders of the Series A Preferred Stock had the right to vote together with the holders of Common Stock as a single class.

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In addition to the right of the selling stockholder to voluntarily convert its Series B Preferred Stock into shares of our common stock, all unconverted shares of the Series B Preferred Stock will automatically convert into shares of common stock, at the then-applicable conversion formula, on April 17, 2003.

REDEMPTION RIGHTS OF REDEEMABLE PREFERRED STOCK

The Company may be obligated to redeem the Series B Preferred Stock in two types of situations: (1) if the number of shares issued upon conversion of the Series B Preferred Stock were to exceed 19.9% of our outstanding common stock, and (2) if we fail to conclude certain required actions or if certain enumerated events were to occur.

IF THE UNDERLYING SHARES EXCEED 19.9%. If the number of shares of common stock issued upon conversion of the Series B Preferred Stock and in lieu of cash dividends (see below for a description of this concept) exceeds 19.9% of our outstanding common stock, we must take, at our option, one of two actions: (i) redeem all of the remaining shares of Series B Preferred Stock at a price equal to 120% of the Liquidation Preference, as defined (ii) call a special meeting of the Company's stockholders to approve of the issuance of the common stock (and any other matters requiring stockholder approval under the applicable rules of the NASDAQ Stock Market) and use the Company's best efforts to obtain such approval.

The Company cannot predict which of the foregoing two alternatives it will elect.

In any event, the Company's ability to elect the first alternative (i.e., make a redemption at 120% of the Liquidation Value of the Series B Preferred Stock) will depend on numerous factors in the future, including whether it has sufficient funds to make such redemption. At December 31, 2000, the Series B Preferred Stock could be converted into 1,618,899 shares of Common Stock, which exceeds 19.9% (see above).

FAILURE TO CONCLUDE ACTIONS/OCCURRENCE OF EVENTS. The Company will be required to redeem the outstanding Series B Preferred Stock at a price equal to 125% of the Liquidation Preference as defined if any of the following events (among others) were to happen (unless the selling stockholder at the time agreed with the Company otherwise): (i) if the registration statement is not effective

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by September 27, 2000, (ii) if the Company breaches the terms of the Series B Preferred Stock and does not cure such breach within 10 days of notice to us of such breach, (iii) if the Company becomes bankrupt by court order or if we voluntarily institute bankruptcy proceedings or if other similar events occur (iv) if the Company defaults under any of our material contracts in our businesses or lose a final judgment, where the default or judgment is in excess of \$250,000, (v) if there is a Change of Control, as defined.

On September 28, 2000 the Company received notification from La Vista demanding redemption of outstanding Series B Preferred Stock in accordance with the terms of the Series B Preferred Stock due to the Company's failure to have a registration statement effective by September 27, 2000. Accordingly, the Company has increased the value of the redeemable preferred stock to \$1,250,000. The Company filed a registration statement relating to the Series B Preferred Stock and it was declared effective on February 16, 2001.

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Because of our present stock price, it is highly unlikely that we will be able to raise funds through the sale of our equity securities, and our financial condition prevents us from issuing debt securities. In the event that we are unsuccessful in our litigation with the holder of our redeemable preferred stock, we cannot assure you that we will be able to generate funds to enable the Company to pay its financial obligations. In addition, our auditors included in their report on our financial statement for the year ended December 31, 2000 in our Form 10-K, an explanatory paragraph about our ability to continue as a going concern.

INFLATION

Management does not believe inflation had a material adverse effect on the financial statements for the periods presented.

FORWARD LOOKING STATEMENTS AND ASSOCIATED RISK

Statements contained in this Form 10-Q, which are not historical facts, are forwarding-looking statements. The forward-looking statements in this Form 10-Q are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements made herein contain a number of risks and uncertainties that could cause actual results to differ materially. These risks and uncertainties include, but are not limited to, specific factors impacting the Company's business, including increased competition; the ability of the Company to expand its operations and attract and retain qualified sales representatives and technically trained consultants experienced in the Internet and IT sectors; the ability of the Company to attract and retain Internet solutions and IT professionals skilled in specific applications; the ability of the Company to attract and retain qualified personnel in the legal staffing sector; the availability of computer equipment; competition in the Internet solutions and IT consulting sector and general economic conditions and the Company's need for additional capital to finance the growth of its operations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

"Quantitative and Qualitative Disclosure About Market Risk", on page 24 of the Company's Annual Report on Form 10-K, is incorporated herein by reference. No material changes have occurred from the disclosure in Form 10-K, through the three months ended March 31, 2001.

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PART II: OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

None.

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SIGNATURES

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

5B TECHNOLOGIES CORPORATION

Date: May 21, 2001

By: /s/ Glenn Nortman

Glenn Nortman, Chief Executive Officer

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