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SITESTAR CORP  
Form 10QSB  
August 19, 2002

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

FORM 10-QSB

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2002

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

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

000-27763  
(Commission file number)

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

NEVADA  
(State or other jurisdiction  
of incorporation or organization)

88-0397234  
(IRS Employer  
Identification No.)

15303 VENTURA BOULEVARD, SUITE 1510, SHERMAN OAKS, CA 91403  
(Address of principal executive offices)

(818) 380-8180  
(Issuer's telephone number)

(Former name, former address and former fiscal year,  
if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity. As of June 30, 2002 - 98,624,892 shares of Common Stock

Transitional Small Business Disclosure Format (check one): Yes  No

SITESTAR CORPORATION

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PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	

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JUNE 30, 2002

ASSETS

CURRENT ASSETS	
Cash and cash equivalents	\$ 98,674
Marketable securities	27,248
Accounts receivable, net of allowance of \$434,988	365,592
Inventory	94,950
Other current assets	112,672
	-----
Total current assets	699,136
PROPERTY AND EQUIPMENT, net	381,896
CUSTOMER LIST, net	950,373
GOODWILL	2,472,719
INVESTMENTS	130,500
	-----
TOTAL ASSETS	\$ 4,634,624
	=====

See the accompanying notes to the consolidated financial statements

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SITESTAR CORPORATION AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEET, CONTINUED  
JUNE 30, 2002

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES	
Accounts payable and accrued expenses	\$ 373,914
Deferred revenue	211,125
Convertible debenture	151,612
Line of credit	77,493
Note payable - stockholders, current portion	123,314

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Notes payable, current portion	183,668
Capital lease obligations, current portion	6,598
	-----
Total current liabilities	1,127,724
NOTES PAYABLE - STOCKHOLDERS, less current portion	398,854
NOTES PAYABLE, less current portion	167,640
CAPITAL LEASE OBLIGATIONS, less current portion	4,400
	-----
TOTAL LIABILITIES	1,698,618
	-----
COMMITMENTS AND CONTINGENCIES	
STOCKHOLDERS' EQUITY	
Preferred Stock, \$.001 par value, 10,000,000 shares authorized, 0 shares issued and outstanding	-
Common Stock, \$.001 par value, 300,000,000 shares authorized, 98,624,892 shares issued and outstanding	98,625
Additional paid-in capital	13,608,541
Accumulated deficit	(10,771,160)
	-----
Total stockholders' equity	2,936,006
	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 4,634,624
	=====

See the accompanying notes to the consolidated financial statements

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SITESTAR CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE THREE MONTHS ENDED JUNE 30, 2002 AND 2001

	2002	2001
	-----	-----
REVENUE	\$ 995,682	\$ 919,959
COST OF REVENUE	542,024	386,653
	-----	-----
GROSS PROFIT	453,658	533,306
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	529,611	1,081,634
	-----	-----

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LOSS FROM OPERATIONS	(75,953)	(548,328)
OTHER INCOME (EXPENSES)		
Other income	2,016	13,313
Increase in market value of marketable securities	-	89,446
Interest expense	(49,833)	(65,601)
	-----	-----
LOSS BEFORE INCOME TAXES	(123,770)	(511,170)
INCOME TAXES	-	-
	-----	-----
NET LOSS	\$ (123,770)	\$ (511,170)
	=====	=====
BASIC AND DILUTED LOSS PER SHARE	\$ (0.00)	\$ (0.01)
	=====	=====
WEIGHTED AVERAGE SHARES OUTSTANDING - BASIC AND DILUTED	98,624,892	68,749,662
	=====	=====

See the accompanying notes to the consolidated financial statements

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SITESTAR CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE SIX MONTHS ENDED JUNE 30, 2002 AND 2001

	2002	2001
	-----	-----
REVENUE	\$ 2,130,914	\$ 1,832,133
COST OF REVENUE	1,070,189	714,633
	-----	-----
GROSS PROFIT	1,060,725	1,117,500
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	1,166,064	1,813,779
	-----	-----
LOSS FROM OPERATIONS	(105,339)	(696,279)
OTHER INCOME (EXPENSES)		
Other income	2,016	96,517

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Increase in market value of marketable securities	-	130,688
Interest expense	(104,306)	(168,374)
	-----	-----
LOSS BEFORE INCOME TAXES	(207,629)	(637,448)
	-----	-----
INCOME TAXES	-	-
	-----	-----
NET LOSS	\$ (207,629)	\$ (637,448)
	=====	=====
BASIC AND DILUTED LOSS PER SHARE	\$ (0.00)	\$ (0.01)
	=====	=====
WEIGHTED AVERAGE SHARES OUTSTANDING - BASIC AND DILUTED	98,372,064	65,669,261
	=====	=====

See the accompanying notes to the consolidated financial statements

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SITESTAR CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE SIX MONTHS ENDED JUNE 30, 2002 AND 2001

	2002	2001
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (207,629)	\$ (637,448)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization expense	237,297	566,928
Amortization of debt financing costs	-	97,315
Increase in market value of marketable securities	-	(130,688)
Stock issued in lieu of compensation and professional fees	125,000	450,377
Value of common shares cancelled	-	(96,517)
Net purchases of marketable securities	-	101,499
(Increase) decrease in:		
Accounts receivable	58,103	(46,686)
Inventory	(4,950)	6,234
Other assets	(21,308)	56,270
Increase (decrease) in:		
Accounts payable and accrued expenses	8,011	(228,721)
Deferred revenue	48,531	(103,350)
	-----	-----
Net cash provided by operating activities	243,055	35,213
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(24,231)	(7,418)
Purchase of investments	(35,500)	-

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Deposit paid for acquisition	-	(150,000)
	-----	-----
Net cash used in investing activities	(59,731)	(157,418)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in line of credit	(2,316)	-
Repayment of notes payable	(59,124)	(29,625)
Repayment of convertible debenture	(325,000)	-
Repayment of notes payable - stockholders	(55,340)	(30,861)
Payment on capital lease obligation	(21,577)	(15,607)
	-----	-----
Net cash used in financing activities	(463,357)	(76,093)
	-----	-----
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(280,033)	(198,298)
CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD	378,707	289,294
	-----	-----
CASH AND CASH EQUIVALENTS - END OF PERIOD	\$ 98,674	\$ 90,996
	=====	=====

See the accompanying notes to the consolidated financial statements

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SITESTAR CORPORATION AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE SIX MONTHS ENDED JUNE 30, 2002 AND 2001 (CONTINUED)

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

During the six months ended June 30, 2002 and 2001, the Company paid no income taxes and interest of approximately \$ 104,000 and \$ 25,000, respectively.

NON-CASH INVESTING AND FINANCING TRANSACTIONS:

During the six months ended June 30, 2002, the Company issued 3,720,238 shares of common stock for executive compensation of \$125,000 and issued 2,000,000 shares of common stock to the original Sitestar.net shareholders that represented the contingent shares to be issued if no additional liabilities arose during the first two years after the acquisition. The value of these shares issued was \$60,000 which is recorded as additional goodwill.

During the six months ended June 30, 2001, the Company converted \$192,443 of the convertible debenture into 4,581,984 shares of common stock, issued 2,193,674 shares of common stock for professional services valued at \$93,377, issued 7,140,000 shares of common stock for officers' salaries of \$357,000 and canceled 1,741,418 shares of common stock valued at \$96,517. In addition, during the six months ended June 30, 2001, the Company entered into capital lease obligations of \$12,253.

See the accompanying notes to the consolidated financial statements

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SITESTAR CORPORATION  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

The unaudited Condensed Consolidated Financial Statements have been prepared by Sitestar Corporation (the "Company" or "Sitestar"), pursuant to the rules and regulations of the Securities and Exchange Commission. The information furnished herein reflects all adjustments (consisting of normal recurring accruals and adjustments) which are, in the opinion of management, necessary to fairly present the operating results for the respective periods. Certain information and footnote disclosures normally present in annual consolidated financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to such rules and regulations. These financial statements should be read in conjunction with the audited consolidated financial statements and footnotes for the year ended December 31, 2001 included in the Company's Annual Report on Form 10-KSB. The results of the six months ended June 30, 2002 are not necessarily indicative of the results to be expected for the full year ending December 31, 2002.

NOTE 2 - EARNINGS PER SHARE

In 1997, the Financial Accounting Standard Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings per Share." SFAS No. 128 replaced the previously reported primary and fully diluted earnings per share with basic and diluted earnings per share. Unlike primary earnings per share, basic earnings per share excludes any dilutive effects of options, warrants, and convertible securities. Diluted earnings per share is very similar to the previously reported fully diluted earnings per share. Basic earnings per share is computed using the weighted-average number of common shares outstanding during the period. Common equivalent shares are excluded from the computation if their effect is anti-dilutive. As of June 30, 2002 the Company has outstanding 500,000 warrants to purchase shares of common stock at \$0.77.

SITESTAR CORPORATION  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

NOTE 3 - CONVERTIBLE DEBENTURE

On May 11, 2000, the Company issued two convertible debentures aggregating \$500,000. The debentures bear interest at 12% per annum and were due on May 1, 2001. On August 14, 2000, the Company issued another two convertible debenture aggregating \$500,000 to the holders of the above-mentioned debentures for the same terms described above, except for the due date of August 14, 2001.

As of June 30, 2002, the holder of the debentures converted \$513,388 in principal and \$90,822 of accrued interest into 13,100,906 and 5,176,365, respectively, shares of the Company's common stock. Also as of June 30, 2002, the Company has repaid \$335,000 of this debenture in cash.

As of June 30, 2002, the convertible debentures are past their maturity and callable at anytime by the debenture holders. The debenture holder has also served notice to the Company that the convertible debentures are in default. The Company has not converted any of the outstanding balances into the Company's common stock for the last 3 quarters. The Company also has not redeemed any of the convertible debentures since February 2002.

As of June 30, 2002, there is a discrepancy between the balance maintained by the Company and the balance calculated by the debenture holders. The balance the Company has disclosed in its financial statements is derived from all the conversion notices and confirmation received from our debenture holders as of the last fiscal year's audited financial statements. The Company and the representatives of the debenture holders are working to reconcile and resolve the balance discrepancies.

The Company believes that it has proper documentation to support its position in this matter; however, in the event the Company is not successful in reconciling and resolving this matter, the outstanding balance of the convertible debenture could increase significantly. As of June 30, 2002, the Company has disclosed that the outstanding principal balance is \$151,612. This outstanding balance could increase to over \$300,000 if the debenture holders are able to assert that their balance is the correct balance.

NOTE 4 - COMMON STOCK

During the six months ended June 30, 2002, the Company issued 3,720,238 shares of common stock for executive compensation of \$125,000.

In addition, in January 2002 the Company issued 2,000,000 shares of common stock to the original Sitestar.net shareholders that represented the contingent shares to be issued if no additional liabilities arose during the first two years after the acquisition. The value of these shares issued was \$60,000 which is recorded as additional goodwill in the accompanying financial statements. The value of the shares issued was the market value of the shares at the date of issuance.

SITESTAR CORPORATION  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

NOTE 5 - SEGMENT INFORMATION

The Company has four business units that have separate management and reporting infrastructures that offer different products and services. The business units have been aggregated into four reportable segments: Corporate, Internet, Development and Retail. The Corporate group is the holding company and oversees the operating of the other business units. The Corporate group also arranges financing for the entire organization. The Internet group provides Internet access to customers in the Martinsville and Lynchburg, Virginia and Mt. Airy, North Carolina areas. The Development group provides customer software programming to companies, principally in the manufacturing industries. The Retail group operates a retail computer store in Lynchburg, Virginia as well as providing computer training to customers.

The Company evaluates the performance of its operating segments based on income from operations, before income taxes, accounting changes, non-recurring items, and interest income and expense.

Summarized financial information concerning the Company's reportable segments is shown in the following table for the six months ended June 30, 2002 and 2001:

	June 30, 2002				
	Corporate	Internet	Development	Retail	Consolidated
Revenue	\$ -	\$ 1,692,223	\$ 144,861	\$ 293,830	\$ 2,130,914
Operating income (loss)	\$ (415,863)	\$ 249,727	\$ 9,573	\$ 51,224	\$ (105,339)
Depreciation and amortization	\$ 2,639	\$ 226,202	\$ 6,516	\$ 1,940	\$ 237,297
Interest expense	\$ (12,014)	\$ (92,292)	\$ -	\$ -	\$ (104,306)
Intangible assets	\$ -	\$ 3,423,092	\$ -	\$ -	\$ 3,423,092
Identifiable assets	\$ 334,247	\$ 4,106,180	\$ 28,880	\$ 165,317	\$ 4,634,624

  

	June 30, 2001				
	Corporate	Internet	Development	Retail	Consolidated
Revenue	\$ -	\$ 1,325,621	\$ 148,478	\$ 358,034	\$ 1,832,133
Operating loss	\$ (770,000)	\$ 53,164	\$ (34,553)	\$ 55,110	\$ (696,279)
Depreciation and amortization	\$ 1,715	\$ 559,947	\$ 3,496	\$ 1,770	\$ 566,928
Interest expense	\$ 135,571	\$ 33,528	\$ (17)	\$ (708)	\$ 168,374

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### SITESTAR CORPORATION NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

#### NOTE 6 - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

The Company has adopted SFAS No. 142, "Goodwill and Other Intangibles" and accordingly has ceased amortizing Goodwill. Amortization expense related to Goodwill for the six months ended June 30, 2001 was \$237,690. Pursuant to the standard, the Company performed the first tier Goodwill impairment test based on criteria in effect at date of Adoption, January 1, 2002, and determined that there is no indication of impairment. The Company has not yet determined the date of the annual impairment test, and therefore may perform the test again before the year end December 31, 2002, but does not expect the result to have a material impact on financial position and results of operations.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS 144 requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that its carrying amount may not be recoverable and is measured by a comparison of the carrying amount of an asset to undiscounted future net cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future undiscounted cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the fair value of the asset. SFAS 144 requires companies to separately report discontinued operations and extends that reporting to a component of an entity that either has been disposed of (by sales, abandonment or in a distribution to owners) or is classified as held for sale. Assets to be disclosed are reported at the lower of the carrying amount or fair value less costs to sell. The Company has adopted SFAS 144 on January 1, 2002. The provisions of this statement for assets held for sale or other disposal generally are required to be applied prospectively after the adoption date to newly initiated disposal activities and, therefore, will depend on future actions initiated by management. As a result, we cannot determine the potential effects that adoption of SFAS 144 will have on our consolidated financial statements with respect to future disposal decisions, if any.

In April 2002, the FASB issued Statement No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." This Statement rescinds FASB Statement No. 4, "Reporting Gains and Losses from Extinguishment of Debt", and an amendment of that Statement, FASB Statement No. 64, "Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements" and FASB Statement No. 44, "Accounting for Intangible Assets of Motor Carriers". This Statement amends FASB Statement No. 13, "Accounting for Leases", to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. The Company does not expect the adoption to have a material impact to the Company's financial position or results of operations.

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#### NOTE 7 - SUBSEQUENT EVENT

In July 2002, the Company acquired, through its affiliate, Sitestar SMS Partners, LLC, a minority equity stake in Chikka Holdings, Ltd., a British Virgin Islands registered company operating in the Asia Pacific region,

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specifically in the Philippines. Chikka is a leading provider of mobile messaging and other enhanced data services to mobile carriers. Sitestar SMS Partners is managed by the Company and is composed of various third party limited investors, which include current Sitestar shareholders. Sitestar SMS Partners invested \$500,000 in exchange for a minority equity stake in Chikka.

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

#### GENERAL

The following discussion and analysis should be read in conjunction with our consolidated financial statements and related footnotes for the year ended December 31, 2001 included in our Annual Report on Form 10-KSB. The discussion of results, causes and trends should not be construed to imply any conclusion that such results or trends will necessarily continue in the future.

#### OVERVIEW

We are a technology holding company with a broad strategy of acquiring and investing in technology related enterprises. Our primary strategy is acquiring and operating small independent Internet Service Providers in the rural areas of the mid-Atlantic region. Our specific mission is to develop our operating ISP subsidiaries and future ISP acquisitions into a successful collaborative ISP network. We intend to achieve this success by harnessing the synergistic potentials that exists among these acquisitions by consolidating all the administrative functions and streamlining the corporate functions that may exist with each acquisition.

In July 1999, we began to implement our broader strategy of acquiring and investing in emerging technology-based enterprises to create a broad and diverse set of core electronic businesses that deliver a variety of online solutions. In addition to developing and integrating technology-based technologies, our broader objective is to create a mix of Internet operating companies and technology-related portfolio investments that will enhance the value of our core holdings.

Our Internet operating subsidiaries provide Internet services to our customers by providing Internet access and enhanced products and services to small and

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medium sized enterprises in selected high growth markets. We target primarily small and medium sized enterprise customers located in selected high growth secondary markets. We currently provide our customers with Internet access and enhanced products and services in the mid-Atlantic area of the United States. We have designed our comprehensive suite of enhanced products and services to meet the expanding needs of our customers and to increase our revenue per customer.

The products and services we provide include:

- o Internet access services;
- o Web design services;
- o Web hosting services;
- o End to end e-commerce solutions;
- o Online marketing consulting; and
- o Management of mission critical Internet applications.

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Our Internet service provider operating subsidiaries derive their income from the excess of the Internet service prices we charge our customers over the cost of service we pay our suppliers. Additionally, our retail customers pay for services by cash or credit card while we pay our suppliers on extended terms. As a result, we are able to increase our working capital between the time we receive payment for services and the time we are required to pay suppliers. We also generate income from the development of computer software for companies principally in the manufacturing industries and from sales from our retail computer store in Lynchburg, Virginia and Mt. Airy, North Carolina.

On July 1, 2001, we acquired 100% of the equity and voting interest of Advanced Internet Services, Inc., a North Carolina corporation which is a successor in interest to two sole proprietorships one having the same name as the corporation and the other with the name Professional Data Systems (collectively "ADVI"). ADVI is an Internet service provider located in Mt. Airy, North Carolina. The purchase price was \$965,980, which consisted of \$150,000 in cash, 6,021,818 of our common shares valued at \$301,091 a non-interest bearing promissory note for \$1,199,990 payable in 24 quarterly installments of \$49,995 and transaction costs of \$30,000. However, due to the non-interest bearing nature of the note, we imputed a discount rate of 36% to calculate the present value of the note. This discount rate is an estimate of our current cost of capital. Based on this calculation, the present value of the non-interest promissory note is \$484,889.

We believe the acquisition of ADVI, with about 3,000 subscribers, enhanced our primary strategy of consolidating small Internet service providers in the rural markets of the mid-Atlantic region by enlarging our service footprint. We also believe this transaction opened other acquisition opportunities for us to further increase our presence in the northern areas of North Carolina. This recent acquisition increases our Internet access customer base to over 15,000 subscribers. This acquisition included goodwill of \$702,642 that is the premium we paid to have the opportunity to generate revenues and earnings in this market. Furthermore, this acquisition generated us cost savings with the integration and consolidation of ADVI's corporate and administrative functions with our existing infrastructure. This estimated cost savings, along with the accretive nature of the transaction from an operating cash flow perspective, will further allow us to enhance our revenue streams and increase our operating cash flow.

### RESULTS OF OPERATIONS

The following tables show financial data for the six months ended June 30, 2002 and 2001. Operating results for any period are not necessarily

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indicative of results for any future period.

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FOR THE SIX MONTHS ENDED JUNE 30, 2002					
	CORPORATE	INTERNET	DEVELOPMENT	RETAIL	TOTAL
Revenue	\$ -	\$ 1,692,223	\$ 144,861	\$ 293,830	\$ 2,130,914
Cost of revenue	-	811,903	76,429	181,857	1,070,189
Gross profit	-	880,320	68,432	111,973	1,060,725
Operating expenses	415,863	630,593	58,859	60,749	1,166,064
Income (loss) from operations	(415,863)	249,727	9,573	51,224	(105,339)
Other income (expense)	(10,105)	(92,046)	(180)	41	(102,290)
Net income (loss)	\$ (425,968)	\$ 157,681	\$ 9,393	\$ 51,265	\$ (207,629)
EBITDA	\$ (413,224)	\$ 475,924	\$ 16,089	\$ 53,164	\$ 131,953
Corporate expenses paid with common stock	125,000	-	-	-	125,000
Actual cash generated	\$ (288,224)	\$ 475,924	\$ 16,089	\$ 53,164	\$ 256,953

FOR THE SIX MONTHS ENDED JUNE 30, 2001					
	CORPORATE	INTERNET	DEVELOPMENT	RETAIL	TOTAL
Revenue	\$ -	\$ 1,325,621	\$ 148,478	\$ 358,034	\$ 1,832,133
Cost of revenue	-	459,612	101,676	153,345	714,633
Gross profit	-	866,009	46,802	204,689	1,117,500
Operating expenses	770,000	812,845	81,355	149,579	1,813,779
Income (loss) from operations	(770,000)	53,164	(34,553)	55,110	(696,279)
Other income (expense)	91,634	(33,511)	-	708	58,831
Net income (loss)	\$ (678,366)	\$ 19,653	\$ (34,553)	\$ 55,818	\$ (637,448)
EBITDA	\$ (676,651)	\$ 616,606	\$ (34,553)	\$ 56,880	\$ (37,718)
Corporate expenses paid with common stock	450,377	-	-	-	450,377
Actual cash generated	\$ (226,274)	\$ 616,606	\$ (34,553)	\$ 56,880	\$ 412,659

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(1) EBITDA (earnings before interest, taxes, depreciation and amortization) consists of revenue less cost of revenue and operating expense. EBITDA is provided because it is a measure commonly used by investors to analyze and compare companies on the basis of operating performance. EBITDA is presented to enhance an understanding of our operating results and is not intended to represent cash flows or results of operations in accordance with GAAP for the periods indicated. EBITDA is not a measurement under GAAP and is not necessarily comparable with similarly titled measures for other companies. See Liquidity and Capital Resource section for further discussion of cash generated from operations.

### THREE MONTHS ENDED JUNE 30, 2002 COMPARED TO JUNE 30, 2001

REVENUE. Revenue for the three months ended June 30, 2002 increased by \$75,723 or 8.2% from \$919,959 for the three months ended June 30, 2001 to \$995,682 for the same period in 2002. The increase is attributed to the acquisition of Advance Internet in July 2001 that contributed revenue of \$201,278 for the three months ended June 30, 2002, offset by a decrease in revenue of \$125,555 principally as a result of increased competition in the high-speed internet access market.

COST OF REVENUE. Costs of revenue for the three months ended June 30, 2002 increased by \$155,371 or 40.2% from \$386,653 for the three months ended June 30, 2001 to \$542,024 for the same period in 2002. As a percentage of revenue cost of revenue has increased from 42.0% to 54.4%. The increase as a percentage of revenue is principally due higher internet access fees.

OPERATING EXPENSES. Operating expenses for the three months ended June 30, 2002 decreased by \$552,023 or 51.0% from \$1,081,634 for the three months ended June 30, 2001 to \$529,611 for the same period in 2002. The largest component of operating expense is depreciation and amortization that amounted to \$285,426 for the three months ended June 30, 2001 and \$50,051 for the same period in 2002. The decrease in depreciation and amortization is due to the adoption of SFAS No. 142 on January 1, 2002 which no longer requires us to amortize our goodwill balance.

OTHER INCOME. During the three months ended June 30, 2001, certain stockholders surrendered a total of 283,856 shares of common stock valued at \$13,313. We determined the value of the shares surrendered based on the market value of the common stock on the date of surrender. The surrendered shares were originally issued in connections with our acquisition of Sitestar, Inc. in July 1999. .

GAIN FROM MARKETABLE SECURITIES. During the three months ended June 30, 2001, we recognized \$89,446 in gains on the sale of marketable securities. During the three months ended June 30, 2002 we recognized no such gains. We have classified the marketable securities in our portfolio as trading securities.

INTEREST EXPENSE. Interest expense for the three months ended June 30, 2002 decreased by \$15,768 or 24.0% from \$65,601 for the three months ended June 30, 2001 to \$49,833 for the same period in 2002. This decrease was a result of no loan amortization charges related to the convertible debenture during the three months ended June 30, 2002.

### SIX MONTHS ENDED JUNE 30, 2002 COMPARED TO JUNE 30, 2001

REVENUE. Revenue for the six months ended June 30, 2002 increased by \$298,781 or

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16.3% from \$1,832,133 for the six months ended June 30, 2001 to \$2,130,914 for the same period in 2002. The increase is attributed to the acquisition of Advance Internet in July 2001 that contributed revenue of \$480,825 for the six months ended June 30, 2002, offset by a decrease in revenue of \$152,044 principally as a result of increased competition in the high-speed internet access market.

**COST OF REVENUE.** Costs of revenue for the six months ended June 30, 2002 increased by \$355,556 or 49.8% from \$714,633 for the six months ended June 30, 2001 to \$1,070,189 for the same period in 2002. As a percentage of revenue cost of revenue has increased from 39.0% to 50.2%. The increase as a percentage of revenue is principally due some rebates we received from our major supplier of Internet services during the 1st quarter of 2001.

**OPERATING EXPENSES.** Operating expenses for the six months ended June 30, 2002 decreased by \$647,715 or 35.7% from \$1,813,779 for the six months ended June 30, 2001 to \$1,166,064 for the same period in 2002. The largest component of operating expense is depreciation and amortization that amounted to \$566,928 for the six months ended June 30, 2001 and \$237,297 for the same period in 2002. The decrease in depreciation and amortization is due to the adoption of SFAS No. 142 on January 1, 2002 which no longer requires us to amortize our goodwill balance.

**OTHER INCOME.** During the six months ended June 30, 2001, certain stockholders surrendered a total of 1,741,418 shares of common stock valued at \$96,517. We determined the value of the shares surrendered based on the market value of the common stock on the date of surrender. The surrendered shares were originally issued in connections with our acquisition of Sitestar, Inc. in July 1999.

**GAIN FROM MARKETABLE SECURITIES.** During the six months ended June 30, 2001, we recognized \$130,688 in gains on the sale of marketable securities. During the six months ended June 30, 2002 we recognized no such gains. We have classified the marketable securities in our portfolio as trading securities.

**INTEREST EXPENSE.** Interest expense for the six months ended June 30, 2002 decreased by \$64,068 or 38.1% from \$168,374 for the six months ended June 30, 2001 to \$104,306 for the same period in 2002. This decrease was a result of no loan amortization charges related to the convertible debenture during the six months ended June 30, 2002.

### LIQUIDITY AND CAPITAL RESOURCES

For the six months ended June 30, 2002, we generated EBITDA at our operating subsidiary level of \$545,177. This amount was offset by EBITDA at the corporate level of \$(413,224). However, at the corporate level we paid for certain salaries of \$125,000 by issuing shares of our common stock rather than paying these expenses with cash. After taking into account these non-cash expenses at the corporate level the actual net cash spent at the corporate level was \$288,224. The following table illustrates the actual cash flow generated during the six months ended June 30, 2002:

EBITDA generated at the operating subsidiary level	\$	545,177
EBITDA generated at the corporate level		(413,224)
Corporate expenses paid with common stock		125,000
		-----
ACTUAL CASH GENERATED	\$	256,953
		=====

During the six months ended June 30, 2002, we paid down our convertible debenture by \$325,000. We also repaid notes payable and notes payable - stockholders of approximately \$59,000 and \$55,000 respectively.

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Our business plan has required, and is expected to continue to require, substantial capital to fund the growth of our operations, capital expenditures, and expansion of sales and marketing capabilities and acquisitions.

On May 11, 2000 we issued two convertible debentures aggregating \$500,000. The debentures bear interest at 12% per annum and were due on May 1, 2001. On August 14, 2000, we issued another two convertible debenture for an aggregate of \$500,000 to the holders of the above-mentioned debentures for the same terms described above. The debenture bears interest at 12% per annum and were due on August 14, 2001. These convertible debentures are currently callable at anytime since it is past its maturity date. The debenture holders can call these debentures upon sufficient written advance notice as agreed upon in the convertible debenture agreement.

As of June 30, 2002, the holder of the debentures converted \$513,388 in principal and \$90,822 of accrued interest into 13,100,906 and 5,176,365, respectively, shares of our common stock. Also as of June 30, 2002, we have repaid \$335,000 of this debenture in cash.

As of June 30, 2002, the convertible debentures are past their maturity and callable at anytime by the debenture holders. The debenture holder has also served notice to us that the convertible debentures are in default. We have not converted any of the outstanding balances into our common stock for the last 3 quarters. We also have not redeemed any of the convertible debentures since February 2002.

As of June 30, 2002, there is a discrepancy between the balance maintained by us and the balance calculated by the debenture holders. The balance we have disclosed in our financial statements is derived from all the conversion notices and confirmation received from our debenture holders as of the last fiscal year's audited financial statements. The representatives of the debenture holders and us are working to reconcile and resolve the balance discrepancies.

We believe that we have proper documentation to support our position in this matter; however, in the event we are not successful in reconciling and resolving this matter, the outstanding balance of the convertible debenture could increase significantly. As of June 30, 2002, we have disclosed that the outstanding principal balance is \$151,612. This outstanding balance could increase to over \$300,000 if the debenture holders are able to assert that their balance is the correct balance.

We believe that our existing cash and cash equivalents, and short-term investments and cash flow from operations, will be sufficient to meet our working capital and capital expenditure requirements for at least the next 12 months. Additional financing may not be available when needed or, if available, such financing may not be on terms favorable to our shareholders or us. If such sources of financing are insufficient or unavailable, or if we experience shortfalls in anticipated revenue or increases in anticipated expenses, we may need to slow down or stop the expansion of our Internet Service Providers and reduce our marketing and development efforts. Any of these events could harm our business, financial condition or results of operations.

### FORWARD LOOKING STATEMENTS

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Stockholders are cautioned that all

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forward-looking statements involve risks and uncertainty, including without limitation, our ability to expand our customer base, make strategic acquisitions, general market conditions, and competition and pricing. Although we believe the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate, and therefore, there can be no assurance that the forward-looking statements contained in the report will prove to be accurate.

### Part II. OTHER INFORMATION

#### Item 1. Legal Proceedings

None

#### Item 2. Change in Securities and Use of Proceeds

None

#### Item 3. Defaults Upon Senior Securities

None

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

Not applicable

#### Item 5. Other Information

Not applicable

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

##### (a) Exhibits

99.1 Certification of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

99.2 Certification of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

##### (b) 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.

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SITESTAR CORPORATION

By: /s/ Frederick T. Manlunas

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Frederick T. Manlunas  
Executive Chairman and  
Chief Financial Officer

Date: August 19, 2002