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PORTA SYSTEMS CORP
Form 10-Q
November 14, 2003

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 September 30, 2003

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 1-8191

PORTA SYSTEMS CORP.

(Exact name of registrant as specified in its charter)

Delaware

11-2203988

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

6851 Jericho Turnpike, Suite 170, Syosset, New York

(Address of principal executive offices)

11791

(Zip Code)

516-364-9300

(Company'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 No

Indicate by a check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date:

Common stock (par value \$0.01) 9,972,284 shares as of November 7, 2003

PART I.- FINANCIAL INFORMATION
Item 1- Financial Statements

PORTA SYSTEMS CORP. AND SUBSIDIARIES

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Consolidated Balance Sheets (Dollars in thousands)

	September 30, 2003
Assets	(Unaudited)
-----	-----
Current assets:	
Cash and cash equivalents	\$ 184
Accounts receivable - trade, less allowance for doubtful accounts	4,568
Inventories	2,707
Prepaid expenses and other current assets	433
Total current assets	----- 7,892
Property, plant and equipment, net	1,530
Goodwill, net	2,961
Other assets	103
Total assets	----- \$ 12,486 =====
Liabilities and Stockholders' Deficit	

Current liabilities:	
Senior debt	\$ 25,303
Subordinated notes	6,144
6% convertible subordinated debentures	385
Accounts payable	5,773
Accrued expenses	2,546
Accrued interest payable	3,332
Accrued commissions	414
Accrued deferred compensation	72
Income taxes payable	18
Short-term loan	5
Total current liabilities	----- 43,992 -----
Deferred compensation	1,124
Total long-term liabilities	----- 1,124 -----
Total liabilities	----- 45,116 -----
Stockholders' deficit:	
Preferred stock, no par value; authorized 1,000,000 shares, none issued	--
Common stock, par value \$.01; authorized 20,000,000 shares, issued 10,003,224 and 10,003,224 shares at September 30, 2003 and December 31, 2002	100
Additional paid-in capital	76,059
Accumulated deficit	(102,704)
Accumulated other comprehensive loss:	
Foreign currency translation adjustment	(4,147)

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Treasury stock, at cost	(30,692)
	(1,938)

Total stockholders' deficit	(32,630)

Total liabilities and stockholders' deficit	\$ 12,486
	=====

See accompanying notes to consolidated financial statements.

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PORTA SYSTEMS CORP. AND SUBSIDIARIES
 Unaudited Consolidated Statements of Operations and Comprehensive Loss
 (In thousands, except per share data)

	Nine Months Ended	
	September 30, 2003	September 30, 2002
	-----	-----
Sales	\$ 14,125	\$ 16,329
Cost of sales	10,006	11,308
	-----	-----
Gross profit	4,119	5,021
	-----	-----
Selling, general and administrative expenses	4,559	5,448
Research and development expenses	1,553	1,998
Impairment loss	--	800
	-----	-----
Total expenses	6,112	8,246
	-----	-----
Operating loss	(1,993)	(3,225)
Interest expense	(940)	(1,488)
Interest income	1	5
Gain on sale of investment in joint venture	--	450
Other income (expense), net	(26)	60
	-----	-----
Loss before income taxes	(2,958)	(4,198)
Income tax (expense) benefit	277	(23)
	-----	-----
Net loss	\$ (2,681)	\$ (4,221)
	=====	=====
Other comprehensive loss:		
Foreign currency translation adjustments	(14)	(32)
	-----	-----
Comprehensive loss	\$ (2,695)	\$ (4,253)
	=====	=====

Per share data:

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Basic per share amounts:

Net loss per share of common stock	\$ (0.27)	\$ (0.42)
	=====	=====
Weighted average shares outstanding	9,972	9,961
	=====	=====

Diluted per share amounts:

Net loss per share of common stock	\$ (0.27)	\$ (0.42)
	=====	=====
Weighted average shares outstanding	9,972	9,961
	=====	=====

See accompanying notes to unaudited consolidated financial statements.

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PORTA SYSTEMS CORP. AND SUBSIDIARIES
 Unaudited Consolidated Statements of Operations and Comprehensive Loss
 (In thousands, except per share data)

	Three Months Ended	
	September 30, 2003	September 30, 2002
	-----	-----
Sales	\$ 5,787	\$ 5,093
Cost of sales	3,728	3,068
	-----	-----
Gross profit	2,059	2,025
	-----	-----
Selling, general and administrative expenses	1,435	1,818
Research and development expenses	520	611
	-----	-----
Total expenses	1,955	2,429
	-----	-----
Operating income (loss)	104	(404)
Interest expense	(313)	(310)
Interest income	--	1
Other income (expense), net	--	30
	-----	-----
Loss before income taxes	(209)	(683)
Income tax expense	(5)	(13)
	-----	-----
Net loss	\$ (214)	\$ (696)
	=====	=====
Other comprehensive loss:		
Foreign currency translation adjustments	36	(27)

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	-----	-----
Comprehensive loss	\$ (178)	\$ (723)
	=====	=====
Per share data:		
Basic per share amounts:		
Net loss per share of common stock	\$ (0.02)	\$ (0.07)
	=====	=====
Weighted average shares outstanding	9,972	9,972
	=====	=====
Diluted per share amounts:		
Net loss per share of common stock	\$ (0.02)	\$ (0.07)
	=====	=====
Weighted average shares outstanding	9,972	9,972
	=====	=====

See accompanying notes to unaudited consolidated financial statements.

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PORTA SYSTEMS CORP. AND SUBSIDIARIES
 Unaudited Consolidated Statements of Cash Flows
 (In thousands)

	Nine Months Ended	
	September 30, 2003	September 30, 2002
	-----	-----
Cash flows from operating activities:		
Net loss	\$ (2,681)	\$ (4,221)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	402	498
Amortization of debt discounts	--	3
Impairment loss	--	800
Gain on sale of investment in joint venture	--	(450)
Changes in operating assets and liabilities:		
Accounts receivable	86	(1,712)
Inventories	656	1,777
Prepaid expenses	(104)	207
Other assets	237	(304)
Accounts payable, accrued expenses and other liabilities	735	316
	-----	-----
Net cash used in operating activities	(669)	(3,086)
	-----	-----
Cash flows from investing activities:		
Capital expenditures, net	(77)	(50)
	-----	-----
Net cash used in investing activities	(77)	(50)

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	-----	-----
Cash flows from financing activities:		
Proceeds from senior debt	233	2,901
Proceeds from exercised options and warrants	--	4
Repayments of short term loans	(3)	(2)
	-----	-----
Net cash provided by financing activities	230	2,903
	-----	-----
Effect of exchange rate changes on cash	(79)	(80)
	-----	-----
Decrease in cash and cash equivalents	(595)	(313)
Cash and equivalents - beginning of the year	779	1,204
	-----	-----
Cash and equivalents - end of the period	\$ 184	\$ 891
	=====	=====
Supplemental cash flow disclosure:		
Cash paid for interest expense	\$ 4	\$ 9
	=====	=====
Cash paid for income taxes	\$ 8	\$ 15
	=====	=====

See accompanying notes to unaudited consolidated financial statements.

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PORTA SYSTEMS CORP. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1: Management's Responsibility For Interim Financial Statements
Including All Adjustments Necessary For Fair Presentation

Management acknowledges its responsibility for the preparation of the accompanying interim consolidated financial statements which reflect all adjustments, consisting of normal recurring adjustments, considered necessary in its opinion for a fair statement of its consolidated financial position and the results of its operations for the interim period presented. These consolidated financial statements should be read in conjunction with the summary of significant accounting policies and notes to consolidated financial statements included in the Company's Form 10-K annual report for the year ended December 31, 2002. These financial statements have been prepared assuming that the Company will continue as a going concern and, accordingly, do not include any adjustments that might result from the outcome of the uncertainties described in these financial statements. The audit opinion included in the December 31, 2002 Form 10-K annual report contained an explanatory paragraph regarding the Company's ability to continue as a going concern. Results for the third quarter or the first nine months of 2003 are not necessarily indicative of results for the year. See Note 3.

Note 2: Inventories

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Inventories are stated at the lower of cost (on the average or first-in, first-out method) or market. The composition of inventories at the end of the respective periods is as follows:

	September 30, 2003	December 31, 2002
	-----	-----
	(in thousands)	
Parts and components	\$ 1,224	\$ 1,767
Work-in-process	541	208
Finished goods	942	1,388
	-----	-----
	\$ 2,707	\$ 3,363
	=====	=====

Note 3: Senior and Subordinated Debt

On September 30, 2003, the Company's debt to its senior lender was \$25,303,000. Under a prior amendment, the loan became due and payable on December 31, 2002. On November 13, 2003, the senior lender granted an extension to January 15, 2004. As a result, the entire balance of the Company's obligations to its senior lender becomes due and payable on that date. The Company does not have the ability to pay the senior debt or the subordinated debt described in the following paragraph. If the maturity of the senior debt is not extended beyond January 15, 2004, and if the senior lender demands payment of all or a significant portion of the loan when due, the Company will not be able to continue in business and may seek protection under the Bankruptcy Code.

Our senior lender has not required us to pay interest on approximately \$23,000,000 of senior debt since March 1, 2002. Accordingly, the financial statements do not reflect any interest charges on that amount which would have been payable but for the senior lender's waiver of interest.

As of September 30, 2003, the Company's short-term debt also included \$6,144,000 of subordinated debt that became due on July 3, 2001 and \$385,000 of 6% debentures which became due on July 2, 2002.

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Accrued interest on the subordinated notes was approximately \$2,974,000, which represents interest from July 2000 through September 30, 2003, and accrued interest on the 6% debentures was \$58,000. The Company's senior lender has precluded it from paying any principal or interest on the subordinated debt.

Note 4: Accounting for Stock Based Compensation

The Company applies the intrinsic value method as outlined in APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for stock options. Under the intrinsic value method, no compensation expense is recognized if the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of the grant. Accordingly, no compensation cost has been recognized. SFAS No. 123, "Accounting for Stock-based Compensation," requires the Company to provide pro forma information regarding net loss and net loss per share of common stock as if compensation cost for the Company's stock option programs had been determined in accordance with the fair value method prescribed therein. Since there was no stock-based compensation in the nine months ended September 30, 2003 and 2002, pro forma loss is the same as the reported net loss.

Note 5: Segment Data

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The Company has three reportable segments: Line Connection and Protection Equipment ("Line") whose products interconnect copper telephone lines to switching equipment and provide fuse elements that protect telephone equipment and personnel from electrical surges; Operating Support Systems ("OSS") whose products automate the testing, provisioning, maintenance and administration of communication networks and the management of support personnel and equipment; and Signal Processing ("Signal") whose products are used in data communication devices that employ high frequency transformer technology.

The factors used to determine the above segments focused primarily on the types of products and services provided, and the type of customer served. Each of these segments is managed separately from the others, and management evaluates segment performance based on operating income.

There has been no significant change from December 31, 2002 in the basis of measurement of segment revenues and profit or loss, and no significant change in the Company's assets.

	Nine Months Ended		Three Months Ended	
	September 30, 2003	September 30, 2002	September 30, 2003	September 30, 2002
Sales:				
Line	\$ 7,944,000	\$ 7,126,000	\$ 3,712,000	\$ 2,126,000
OSS	2,450,000	5,240,000	860,000	1,126,000
Signal	3,023,000	3,368,000	952,000	1,126,000
	-----	-----	-----	-----
	\$ 13,417,000	\$ 15,734,000	\$ 5,524,000	\$ 4,378,000
	=====	=====	=====	=====
Segment profit (loss):				
Line	\$ 806,000	\$ (524,000)	\$ 821,000	\$ 1,126,000
OSS	(1,648,000)	(7,000)	(315,000)	(1,126,000)
Signal	814,000	(122,000)	255,000	(1,126,000)
	-----	-----	-----	-----
	\$ (28,000)	\$ (653,000)	\$ 761,000	\$ (1,126,000)
	=====	=====	=====	=====

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The following table reconciles segment totals to consolidated totals:

	Nine Months Ended		Three Months Ended	
	September 30, 2003	September 30, 2002	September 30, 2003	September 30, 2002
Sales:				
Total revenue for reportable segments	\$ 13,417,000	\$ 15,734,000	\$ 5,524,000	\$ 4,378,000
Other revenue	708,000	595,000	263,000	1,126,000
	-----	-----	-----	-----
Consolidated total revenue	\$ 14,125,000	\$ 16,329,000	\$ 5,787,000	\$ 5,504,000

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	=====	=====	=====
Operating loss:			
Total segment profit (loss)			
for reportable segments	\$ (28,000)	\$ (653,000)	\$ 761,000
Corporate and unallocated	(1,965,000)	(2,572,000)	(657,000)
	-----	-----	-----
Consolidated total			
Operating income (loss)	\$ (1,993,000)	\$ (3,225,000)	\$ 104,000
	=====	=====	=====

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

Introduction

Reference is made to the information provided under "Critical Accounting Policies and Estimates" in our Form 10-K for the year ended December 31, 2002. Although our orders and sales for Line equipment increased in the third quarter of 2003, our business continues to be impaired by our financial position, and we cannot assure you that the increase in orders and sales will continue for any significant period. We are continuing to encounter delays in shipping a portion of backlog in a timely manner, as key suppliers are reluctant to provide us with credit. In addition, there have been periods during the three and nine months ended September 30, 2003 that we did not have the funds either to prepay suppliers or to make purchases on a COD basis. Our business will be impaired if, and to the extent that, we are not able to make purchases necessary to fill our orders. Our senior lender is not providing us with any additional funds, and our obligations to the senior lender, which are described below and in Note 3, become due on January 15, 2004.

Our senior lender has not required us to pay or accrue interest on approximately \$23,000,000 of senior debt since March 1, 2002. Accordingly, the financial statements do not reflect any interest charges on that amount which would have been payable but for the senior lender's waiver of interest.

We have been seeking to raise funds from the sale of one or more of our divisions, and were engaged in negotiations with respect to the potential sale of certain assets of one of our divisions. In the past, we have engaged in negotiations with respect to sales of our divisions, and none of such negotiations resulted in an agreement. In the event that we are not able to sell any of our divisions, we will evaluate alternatives available to us, which may include the discontinuation of unprofitable operations and it may be necessary for us to seek protection under the Bankruptcy Code.

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The Company's consolidated statements of operations for the periods indicated below, shown as a percentage of sales, are as follows:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	-----	-----	-----	-----
	2003	2002	2003	2002
	----	----	----	----
Sales	100%	100%	100%	100%
Cost of sales	71%	69%	64%	60%

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Gross profit	29%	31%	36%	40%
Selling, general and administrative expenses	32%	33%	25%	36%
Research and development expenses	11%	12%	9%	12%
Impairment loss	0%	5%	0%	0%
Operating Income/(loss)	(14%)	(20%)	2%	(8%)
Interest expense - net	(7%)	(9%)	(6%)	(6%)
Gain on sale of joint venture	0%	3%	0%	0%
Other	2%	0%	0%	0%
Net loss	(19%)	(26%)	(4%)	(14%)

The Company's sales by product line for the periods ended September 30, 2003 and 2002 are as follows:

	Nine Months Ended September 30,			

	\$ (000)			
	2003		2002	
	----		----	
Line connection/protection equipment	\$ 7,944	56%	\$ 7,126	44%
OSS equipment	2,450	17%	5,240	32%
Signal Processing	3,023	22%	3,368	20%
Other	708	5%	595	4%
	-----		-----	
	\$14,125	100%	\$16,329	100%
	=====		=====	
	Three Months Ended September 30,			

	\$ (000)			
	2003		2002	
	----		----	
Line connection/protection equipment	\$3,712	64%	\$2,894	57%
OSS equipment	860	15%	1,004	20%
Signal Processing	952	16%	956	19%
Other	263	5%	239	4%
	-----		-----	
	\$5,787	100%	\$5,093	100%
	=====		=====	

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Results of Operations

Our sales for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002 decreased by \$2,204,000 (13%) from \$16,329,000 in 2002 to \$14,125,000 in 2003. Sales for the quarter ended September 30, 2003 of \$5,787,000 increased by \$694,000 (14%) compared to \$5,093,000 for the quarter ended September 30, 2002. The decrease in sales for the nine months is primarily attributed to a 53% decline in sales from our OSS business. The increase in sales for the three month period results from a 28% increase in the Line equipment offset by a 14% decline in sales from our OSS business unit and no material change in the Signal revenue.

Line equipment sales for the nine months ended September 30, were \$7,944,000 compared to \$7,126,000 in the same period of 2002, an increase of \$818,000 (11%). Sales for the three months ended September 30 increased by

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\$818,000 (28%) from \$2,894,000 in 2002 to \$3,712,000 in 2003. The increase for the three months ended September 30, 2003 reflects significant increased sales primarily to customers in the United Kingdom.

OSS sales for the nine months ended September 30, 2003 were \$2,450,000 compared to \$5,240,000 in the same period of 2002, a decrease of \$2,790,000 (53%). OSS sales for the three months ended September 30, 2003 were \$860,000 compared to \$1,004,000 in the same period of 2002, a decrease of \$144,000 (14%). The decrease in sales for the nine and three months resulted from our inability to secure new orders attributable to the slowdown in the telecommunications market and the effects of our financial condition, and from lower levels of contract completion compared to the similar period of the prior year.

Signal sales for the nine months ended September 30, 2003 were \$3,023,000 compared to \$3,368,000 in the same period of 2002, a decrease of \$345,000 (10%). Sales for the three months ended September 30, 2003 compared to 2002, decreased \$4,000 from \$956,000 to \$952,000. These decreases in sales were primarily due to shortages of materials resulting from the refusal of several of our suppliers to ship us on credit due to our financial condition.

Gross margin for the nine months ended September 30, 2003 was 29% compared to 31% for the nine months ended September 30, 2002. Gross margin for the quarter ended September 30, 2003 was 36% compared to 40% for the quarter ended September 30, 2002. Line equipment margins rose during the quarter and nine months ended September 30, 2003, as compared to 2002, due to increased revenue, as noted above, which enabled us to better absorb manufacturing overhead. These gains were offset by lower margins from the OSS business unit during the three and nine months ended September 30, 2003 as compared to 2002, resulting in part from the underabsorption of fixed expenses of this business unit due to the low revenue levels. The Signal margins also increased, primarily from the better absorption of overhead.

Selling, general and administrative expenses decreased by \$889,000 (16%) from \$5,448,000 to \$4,559,000 for the nine months ended September 30, 2003 compared to 2002. For the quarter ended September 30, 2003 selling general and administrative expenses decreased by \$383,000 (21%) from 2002. This decrease relates primarily to our ongoing efforts to reduce personnel and consulting services, and reduced OSS sales commissions reflecting our current OSS level of business.

Research and development expenses decreased by \$445,000 (22%) and by \$91,000 (15%) for the nine and three months ended September 30, 2003 from the comparable periods in 2002. These decreases

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resulted from our efforts to reduce expenses primarily related to the OSS business. Our failure to fund research and development could adversely affect our capability to offer products based on developing technologies, which could affect both our efforts to sell product in future years and our attractiveness to potential buyers.

At June 30, 2002, we determined that goodwill related to our Signal division was impaired based upon attaining a fair market value estimate during discussions with respect to the proposed sale of the Signal division. Based on those discussions, we estimated that the impairment loss was approximately \$800,000. This amount was charged to operations in the quarter ended June 30, 2002 reducing the carrying value of the goodwill to \$2,961,000. Furthermore, we cannot give assurance that further write-downs will not be necessary. The

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goodwill for our Line and OSS divisions had previously been written off.

As a result of the above, for the nine months ended September 30, 2003 vs. the nine months of 2002 our operating loss decreased from \$3,225,000 to \$1,993,000 (38%). We recorded an operating income of \$104,000 for the quarter ended September 30, 2003 as compared to an operating loss of \$404,000 for the quarter ended September 30, 2002, a 126% improvement.

Interest expense for the nine months ended September 30, 2003 compared to September 30, 2002 decreased by \$548,000 (37%) from \$1,488,000 in 2002 to \$940,000 in 2003. Interest expense for the three-month period ending September 30, 2003 compared to the same three months of 2002, increased by \$3,000 (1%) from \$310,000 in 2002 to \$313,000 in 2003. This increase is attributable to our amended agreement with our senior lender, which provides that the old term loan, in the principal amount of approximately \$23,000,000, bears no interest commencing March 1, 2002 until such time as the lender, in its sole discretion, resumes interest charges. The senior lender has not resumed interest charges.

The tax benefit for the nine months ended September 30, 2003 resulted principally from the settlement of an outstanding tax obligation of \$274,000 of one of our subsidiaries for \$30,000.

As a result of the foregoing, we incurred a net loss of \$2,681,000, \$0.27 per share (basic and diluted), for the nine months ended September 30, 2003, compared with a net loss of \$4,221,000, \$0.42 per share (basic and diluted), for the nine months ended September 30, 2002. The net loss for the three months ended September 30, 2003 was \$214,000, \$0.02 per share (basic and diluted), compared with a net loss for the three months ended September 30, 2002 of \$696,000, \$0.07 per share (basic and diluted).

Liquidity and Capital Resources

At September 30, 2003, we had cash and cash equivalents of \$184,000 compared with \$779,000 at December 31, 2002. Our working capital deficit at September 30, 2003 was \$36,100,000 compared to a working capital deficit of \$34,199,000 at December 31, 2002. Our outstanding senior and subordinated debt, with the reduced level of cash on hand and inventory, and the increased level of accounts payable, resulted in the increase in the working capital deficiency. During the nine months of 2003, the net cash used by us in operations was \$669,000 and we are continuing to operate with a negative cash flow.

As of September 30, 2003, our debt includes \$25,303,000 of senior debt which matures on January 15, 2004, \$6,144,000 of subordinated debt that became due on July 3, 2001, and \$385,000 of 6% debentures, which became due on July 2, 2002. The maturity date of the senior debt reflects an extension

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of the maturity of our senior debt. On August 29, 2003, the senior lender granted an extension to November 15, 2003, and on November 13, 2003, the senior lender granted a further extension to January 15, 2004. Interest on the subordinated notes was approximately \$2,974,000, which represents interest from July 2000 through September 30, 2003, and interest on the 6% debentures was \$58,000. We do not have sufficient resources to pay either the senior lender or the subordinated lenders, we are unable to generate such cash from our operations, and our senior lender is not making any further advances to us and has precluded us from making any payments on the subordinated debt. We also do not have any prospects of obtaining an alternate senior lender to replace our present lender.

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Our financial condition and stock price effectively preclude us from raising funds through the issuance of debt or equity securities, we have no other source of funds other than operations, and we are generating a negative cash flow. We have in the past sought to raise funds through the sale of one or more of our divisions, but our efforts to date have been unsuccessful. Even if we were able to sell all of our divisions, it is unlikely that we would generate sufficient cash to pay our senior lender in full.

If the senior lender does not extend the maturity date of our obligations beyond January 15, 2004 and demands payment of all or a significant portion of our obligations to the senior lender, we will not be able to continue in business and we may seek protection under the Bankruptcy Code. We cannot assure you that our senior lender will not demand payment of all or a significant portion of our obligations. Furthermore, even if our senior lender grants us additional extensions, it may nonetheless be necessary for us to seek protection under the Bankruptcy Code.

As a result of our continuing financial difficulties:

- o we are having and we may continue to have difficulty performing our obligations under our OSS contracts, which could result in the cancellation of contracts or the loss of future business and penalties for non-performance;
- o we are continuing to have difficulty in obtaining new business from either existing customers or new customers, although, as noted above, our orders and sales for Line products increased during the three months ended September 30, 2003; and
- o a number of creditors have engaged attorneys or collection agencies, or commenced legal actions against us.

We are seeking to address our need for liquidity by exploring alternatives, including the possible sale of one or more of our divisions. Even if a sale is completed, we may still be unable to operate profitably and it may be necessary for us to seek protection under the Bankruptcy Code.

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Forward Looking Statements

Statements contained in this Form 10-Q include forward-looking statements that are subject to risks and uncertainties. In particular, statements in this Form 10-Q that state the Company's intentions, beliefs, expectations, strategies, predictions or any other statements relating to our future activities or other future events or conditions are "forward-looking statements." Forward-looking statements are subject to risks, uncertainties and other factors, including, but not limited to, those identified under "Risk Factors," in our Form 10-K for the year ended December 31, 2002 and those described in Management's Discussion and Analysis of Financial Conditions and Results of Operations" in our Form 10-K and this Form 10-Q, and those described in any other filings by us with the Securities and Exchange Commission, as well as general economic conditions and economic conditions affecting the telecommunications industry, any one or more of which could cause actual results to differ materially from those stated in such statements.

Item 3. Quantitative and Qualitative Disclosure About Market Risk.

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Although we conduct operations outside of the United States, most of our contracts and sales are dollar denominated. A portion of the revenue from our United Kingdom operations and the majority of our United Kingdom expenses are denominated in Sterling. Any Sterling-denominated receipts are promptly converted into United States dollars. We do not engage in any hedging or other currency transactions. For the nine months ended September 30, 2003 and 2002, the currency translation adjustment was not significant in relation to our total revenue.

Item 4. Controls and Procedures

Our chief executive officer and chief financial officer have supervised and participated in an evaluation of the effectiveness of our disclosure controls and procedures as of a date within 90 days of the date of this report, and based on their evaluations, they believe that our disclosure controls and procedures (as defined in Rule 13a-14(c) of the Securities Exchange Act of 1934, as amended) are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms. As a result of the evaluation, there were no significant changes in our internal controls or other factors that could significantly affect these controls subsequent to the date of their evaluation.

PART II - OTHER INFORMATION

Item 3. Defaults Upon Senior Securities.

See Note 3 of Notes to Unaudited Consolidated Financial Statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources" for information concerning defaults on our subordinated debt.

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Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

- 31.1 Certificate of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certificate of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certificate of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certificate of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K

On August 14, 2003, the Company reported its results of operations for the quarter ended June 30, 2003 under Item 9.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the

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Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PORTA SYSTEMS CORP.

Dated November 14, 2003

By /s/William V. Carney

William V. Carney
Chairman of the Board
and Chief Executive Officer

Dated November 14, 2003

By /s/Edward B. Kornfeld

Edward B. Kornfeld
Senior Vice President
and Chief Financial Officer