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VICOM INC
Form 10-Q
November 14, 2001

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

FORM 10-Q

(MARK ONE)

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

FOR THE PERIOD ENDING SEPTEMBER 30, 2001

OR

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

FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER 0 - 1325

VICOM, INCORPORATED

(Exact name of registrant as specified in its charter)

MINNESOTA

(State or other jurisdiction of incorporation or organization)

41 - 1255001

(IRS Employer Identification No.)

9449 SCIENCE CENTER DRIVE, NEW HOPE, MINNESOTA 55428

(Address of principal executive offices)

TELEPHONE (763) 504-3000 FAX (763) 504-3060

www.vicominc.net Internet

(Registrant's telephone number, facsimile number, and Internet address)

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 and 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

On November 9, 2001 there were 9,904,249 shares outstanding of the registrant's common stock, par value \$.01 per share, and 260,118 outstanding shares of the registrant's convertible preferred stock.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

VICOM, INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)

	Three Months Ended		Nine Months Ended	
	September 30, 2001	September 30, 2000	September 30, 2001	September 30, 2000
REVENUES	\$ 7,678,534	\$ 10,219,008	\$ 26,191,582	\$ 28,111,000
COSTS AND EXPENSES				
Cost of products and services	6,110,861	7,868,109	20,714,309	22,111,000
Selling, general and administrative	2,040,043	2,501,869	7,078,249	8,111,000
	8,150,904	10,369,978	27,792,558	30,222,000
LOSS FROM OPERATIONS	(472,370)	(150,970)	(1,600,976)	(1,111,000)
OTHER EXPENSES				
Interest expense	(271,641)	(133,669)	(796,386)	(1,111,000)
Miscellaneous income (expense)	(480,955)	169,834	(1,144,435)	(1,111,000)
	(752,596)	36,165	(1,940,821)	(1,111,000)
LOSS BEFORE INCOME TAXES	(1,224,966)	(114,805)	(3,541,797)	(2,222,000)
INCOME TAX PROVISION	--	--	--	--
NET LOSS	\$ (1,224,966)	\$ (114,805)	\$ (3,541,797)	\$ (2,222,000)
LOSS ATTRIBUTABLE TO COMMON STOCK				
Net loss	\$ (1,224,966)	\$ (114,805)	\$ (3,541,797)	\$ (2,222,000)
Preferred dividends	(72,817)	(5,971)	(248,425)	(1,111,000)
	\$ (1,297,783)	\$ (120,776)	\$ (3,790,222)	\$ (3,333,000)
LOSS PER COMMON SHARE- BASIC AND DILUTED	\$ (.15)	\$ (.01)	\$ (.46)	\$ (.15)

WEIGHTED AVERAGE COMMON SHARES

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OUTSTANDING-BASIC AND DILUTED 8,939,847 7,738,599 8,317,954 6

See notes to condensed consolidated financial statements

VICOM, INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	SEPTEMBER 30 2001
	----- (UNAUDITED)
ASSETS	
CURRENT ASSETS	
Cash	\$ 1,026,17
Accounts receivable, net allowance of \$132,407 and \$159,000	3,210,31
Inventories, net allowance of \$285,000 and \$200,000	2,000,79
Other	310,96
Costs and estimated earnings in excess of billings	(17,96)

TOTAL CURRENT ASSETS	6,530,27

PROPERTY AND EQUIPMENT	\$ 4,096,59
NONCURRENT ASSETS	
Goodwill, net of accumulated amortization of \$694,000 and \$436,678	2,835,52
Other	185,90

	3,021,43

	\$ 13,648,30

LIABILITIES AND STOCKHOLDERS' EQUITY	
CURRENT LIABILITIES	
Wholesale financing arrangement	\$ 1,058,69
Notes and installment obligations payable-current maturities	573,00
Accounts payable	2,452,64
Other liabilities	702,65
Deferred service obligations and revenue	440,24

TOTAL CURRENT LIABILITIES	5,227,23

NOTES AND INSTALLMENT OBLIGATIONS PAYABLE	3,913,50

COMMITMENTS AND CONTINGENCIES	-
STOCKHOLDERS' EQUITY	
Preferred Stock	
10% Class A cumulative convertible-no par value	

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(issued and outstanding - 50,972 and 0 shares)	479,04
10% Class B cumulative convertible-no par value	
(issued and outstanding-22,836 and 22,836 shares)	218,86
10% Class C cumulative convertible-no par value	
(issued and outstanding-147,310 and 150,810 shares)	1,909,00
14% Class D cumulative convertible-no par value (issued and outstanding	
39,000 and 72,500 shares)	407,50
Common stock-no par value (issued 9,767,771 and 8,137,181 shares; outstanding	
9,671,777 and 8,023,352 share	3,118,68
Subscription receivable	(510,00)
Options and warrants	16,503,66
Unamortized compensation	(1,390,18)
Accumulated deficit	(16,229,01)

	4,507,56

	\$ 13,648,30

See notes to condensed consolidated financial statements.

VICOM, INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	NINE M

	20

OPERATING ACTIVITIES	
Net loss	\$ (3,5
Adjustments to reconcile net loss to net cash used by operating activities	
Depreciation	7
Amortization	6
Gain on sales of property and equipment	
Changes in operating assets and liabilities:	
Accounts receivable	2,4
Inventories	3
Costs, estimated earnings, and billings	
Other assets	(1
Accounts payable	(1
Other liabilities	(1
Wholesale line of credit	(9
Deferred service obligations and revenue	1

Net cash used by operating activities	(5

INVESTING ACTIVITIES	
Purchases of property and equipment	(1,5
Proceeds from sales of property and equipment	
Purchase acquisition	(
Issuance of note receivable	
Collections on notes receivable	

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Net cash used by investing activities	(1,5

FINANCING ACTIVITIES	
Decrease in checks issued in excess of deposits	
Net borrowings under credit arrangements	
Proceeds from long-term debt and warrants	1,6
Proceeds from notes and installment obligations payable	1
Payments on notes and installment obligations payable	(3
Collections on subscription receivable	
Proceeds from issuance of stock and warrants	1,3
Stock issuance costs	(1
Redemption of preferred stock	(4
Preferred stock dividends	(2

Net cash provided by financing activities	2,0

INCREASE (DECREASE) IN CASH	(1
CASH	
Beginning of period	1,1

End of period	\$ 1,0

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION	
Interest paid	4
SUPPLEMENTAL DISCLOSURES OF NON-CASH INVESTING AND FINANCING ACTIVITIES	
Notes payable converted to preferred stock	2
Accounts payable converted to preferred stock	1
Notes payable converted to stock and warrants issued	
Subscriptions receivable on common stock	5
Warrant dividends	
Refinancing of debt	
Conversion of preferred to common stock	
Purchase acquisition	
Assets acquired	3
Liabilities assumed	
Equity securities consideration	3
Employee stock options issued with unamortized compensation	1,2

See notes to condensed consolidated financial statements

VICOM, INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

The information furnished in this report is unaudited and reflects all adjustments which are normal recurring adjustments and, which in the opinion of management, are necessary to fairly present the operating results for the interim periods. The operating results for the interim periods presented are not necessarily indicative of the operating results to be expected for the full fiscal year.

CERTAIN FINANCING ACTIVITIES

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In September 2001, Vicom received an investment of \$500,000 in exchange for Vicom Common Shares and Warrants. The transaction for the common shares was completed at the then trading market price for Vicom Common Stock. The investment was made by the Crestview Capital Fund 1, a Chicago based fund, which invests in undervalued publicly traded and medical companies. Proceeds were used primarily to fund original MultiBand construction.

LOSS PER SHARE

Loss per share-basic is determined by dividing net loss plus the preferred stock dividends by the weighted average common shares outstanding. Net loss per common share-diluted is computed by dividing net loss plus the preferred stock dividends by the weighted average common shares outstanding and the common share equivalents (stock options, stock warrants, convertible preferred shares, and issued but not outstanding restricted stock). Common share equivalents are not included in the computations as their effects were anti-dilutive. Options, convertible preferred stock and warrants together totaling 10,554,288 were excluded from the computation of dilutive loss per share for the periods ended September 30, 2001.

IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2001, the FASB issued SFAS No. 141 "Business Combinations." SFAS 141 eliminates the pooling-of-interests method of accounting for business combinations except for qualifying business combinations that were initiated prior to July 1, 2001. In addition, SFAS 141 further clarifies the criteria to recognize intangible assets separately from goodwill. The requirements of Statement 141 are effective for any business combination accounted for by the purchase method that is completed after June 30, 2001. The adoption of SFAS No. 141 will not have a material effect on the Company's financial position or results or operations.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets." Under SFAS 142, goodwill and indefinite lived intangible assets are no longer amortized but are reviewed annually (or more frequently if impairment indicators arise) for impairment. Separable intangible assets that are not deemed to have an indefinite life will continue to be amortized over their useful lives (but with no maximum life). The amortization provisions of SFAS 142 apply to goodwill and intangible assets acquired after June 30, 2001. The adoption of SFAS No. 142 will decrease the amount of goodwill amortization the Company is recording in the statement of operations. The amount of goodwill amortization recorded for the nine months ended September 30, 2001 was \$258,953.

FORWARD-LOOKING STATEMENTS

From time to time, the Company may publish forward-looking statements relating to such matters as anticipated financial performance, business prospects, product pricing, management for growth, integration of acquisitions, technological developments, new products, and similar matters. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements including those made in this statement. In order to comply with the terms of the Private Securities Litigation Reform Act, the Company notes that a variety of factors could cause the Company's actual results and experience to differ materially from the anticipated results or Company's forward-looking statements.

The risks and uncertainties that may affect the operations, performance, developments and results of the Company's business include the following: national and regional economic conditions; pending and future legislation affecting IT and telecommunications industries; market acceptance of the Company's products and services; the Company's products and services; the

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Company's continued ability to provide integrated communication solutions for customers in a dynamic industry; and other competitive factors.

Because these and other factors could affect the Company's operating results, past financial performance should not necessarily be considered as a reliable indicator of future performance and anticipated future period results.

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

GENERAL

Vicom is the parent corporation of three wholly-owned subsidiaries, Corporate Technologies USA, Inc. (CTU), MultiBand, Inc. (MultiBand) and Vicom Midwest Telecommunications Systems, Inc. (VMTS) (collectively the "company"). VMTS was not active as of September 30, 2001. Vicom incorporated MultiBand in February 2000 to provide voice, data and video services to residential multi-dwelling units (MDUs).

Vicom has provided clients with telecommunications products and services since its inception in 1975. As of September 30, 2001, Vicom was providing telephone equipment and service to approximately 1,000 customers, with approximately 10,000 telephones in service. In addition, CTU provides computer products and services to approximately 3,500 customers. The telecommunications systems we distribute are intended to provide customers with flexible, cost-effective alternatives as compared to systems available from major telephone companies, including those formerly comprising the Bell System, and from other interconnected telephone companies. As of September 30, 2001, MultiBand provided services to approximately 406 customers.

Vicom and CTU provide a full range of voice, data and video communications systems and service, system integration, training and related communication sales and support activities for commercial, professional and institutional customers, most of which are located in Minnesota, North Dakota, South Dakota and Nebraska. Vicom purchases products and equipment from NEC America, Inc. ("NEC"), Cisco Systems, Inc., Nortel Networks Corp., ECI Telecommunications, Inc. ("ECI"), and other manufacturers of communications and electronic products and equipment. We use these products to design telecommunications systems to fit our customers' specific needs and demands.

SELECTED CONSOLIDATED FINANCIAL DATA AS A PERCENTAGE OF REVENUES

	THREE MONTHS ENDED		NINE MONTHS ENDED	
	SEPTEMBER 30,	SEPTEMBER 30,	SEPTEMBER 30,	SEPTEMBER 30
	2001	2000	2001	2000
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
REVENUES	100.0%	100.0%	100.0%	100.0%
COST OF PRODUCTS AND SERVICES	79.6%	76.9%	79.1%	77.4%

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GROSS MARGIN	20.4%	23.1%	20.9%	22.6%
SELLING, GENERAL & ADMINISTRATIVE EXPENSES	26.6%	24.5%	27.0%	28.5%
	-----	-----	-----	-----
LOSS FROM OPERATIONS	(6.2)%	(1.5)%	(6.1)%	(5.9)%
OTHER EXPENSES, NET	(9.8)%	(.4)%	(7.4)%	(1.5)%
	-----	-----	-----	-----
LOSS BEFORE INCOME TAXES	(16.0)%	(1.1)%	(13.5)%	(7.5)%
INCOME TAX PROVISION	0.0%	0.0%	0.0%	0.0%
	-----	-----	-----	-----
NET LOSS	(16.0)%	(1.1)%	(13.5)%	(7.5)%
	=====	=====	=====	=====

The following table sets forth, for the period indicated, the gross margin percentages for Vicom, Incorporated, CTU and MultiBand.

	THREE MONTHS ENDED		NINE MONTHS ENDED	
	SEPTEMBER 30, 2001 (unaudited)	SEPTEMBER 30, 2000 (unaudited)	SEPTEMBER 30, 2001 (unaudited)	SEPTEMBER 30, 2000 (unaudited)
VICOM, INCORPORATED	0.0%	1.7%	54.7%	24.2%
CTU	20%	23.5%	20.9%	21.9%
MULTIBAND	76.3%	1.9%	6.5%	59.7%

RESULTS OF OPERATIONS

REVENUES

Revenues decreased 24.8% to \$7,678,534 in the quarter ended September 30, 2001, as compared to \$10,219,008 for the quarter ended September 30, 2000.

Revenues for Vicom, Incorporated decreased 100% to \$0.00 in the third quarter of fiscal 2001, as compared to \$119,037 in the third quarter of fiscal 2000. This decrease is due to the fact that all sales operations have been transferred to CTU.

Revenues for Corporate Technologies decreased 28.4% to \$7,618,442 as compared to \$10,651,245 in the third quarter of fiscal 2000. These results are reflective, in the Company's opinion, of current general economic conditions.

MultiBand revenues in the quarter ended September 30, 2001 were \$60,092 as compared to \$22,299 in the third quarter of fiscal 2000. MultiBand recorded its first revenues in the third quarter of 2000.

Revenues for the nine-month period ended September 30, 2001 decreased 8.5% to \$26,191,582 from \$28,624,886 for the comparable nine-month period of fiscal 2000. The Company believes the decrease in revenues for the quarter and year to date primarily resulted from a slowing economy.

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GROSS MARGIN

The Company's gross margin decreased 33.3% or \$783,226 to \$1,567,673 for the quarter ended September 30, 2001, as compared to \$2,350,899 for the similar quarter last year. Decrease in gross margin percentage is largely due to decreased sales of telephone equipment, which generally have a higher margin than sales of data equipment. For the quarter ended September 30, 2001, as a percent of total revenues, gross margin was 20.4% as compared to 23.1% for the similar period last year.

Gross margin for Vicom, Inc. for the quarter ended September 30, 2001, was \$0 as compared to gross margin of \$(51,932) for the quarter ended September 30, 2000. This decrease is a result of sales operations transferred to CTU.

Gross margin for CTU decreased by 39.3%, or \$983,624, to \$1,521,816 for the quarter ended September 30, 2001, as compared to \$2,505,440 in the third quarter of fiscal 2000, reflecting a drop in revenues.

Gross margin for MultiBand for the quarter ended September 30, 2001 was \$45,857 as compared to \$43,981 in the third quarter of 2000.

For the nine-month period ended September 30, 2001, the Company's gross margin decreased 15.0% or \$966,561 to \$5,477,273, as compared to \$6,443,834 for the similar period last year. The decrease in gross margin is directly attributable to the Company's decrease in revenues.

For the nine-month period ended September 30, 2001, as a percent of total revenues, gross margin was 20.9% as compared to 22.6% for the similar period last year. Decrease in gross margin percentage is largely due to decreased sales of telephone equipment, which generally have a higher margin than sales of data equipment.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses decreased 18.45% to \$2,040,043 in the quarter ended September 30, 2001, compared to \$2,501,869 in the prior year quarter. This decrease in selling, general and administrative expenses was, as a percentage of revenues, 26.6% for the quarter ended September 30, 2001 and 24.5% for the similar period a year ago. This decrease in expenses is primarily attributable to reductions in payroll and other corporate expenses.

For the nine-month period ended September 30, 2001, these expenses decreased 13.2% to \$7,078,249, as compared to \$8,154,184 for the same period in 2000. As a percentage of revenues, selling, general and administrative expenses are 26.6% for the period ended September 30, 2001, as compared to 28.5% for the same period last year. This percentage decrease is primarily attributable to reductions in payroll and other corporate expenses.

INTEREST EXPENSE

Interest expense was \$271,641 for the quarter ended September 30, 2001, versus \$133,669 for the similar period a year ago, reflecting an increased Company debt load due to acquisition related debt and increased borrowings.

Interest expense was \$796,386 for the nine months ended September 30, 2001, and \$446,820 for the same period last year.

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NET LOSS

In the third quarter of fiscal 2001, the Company incurred a net loss of \$1,224,966 compared to a net loss of \$114,805 for the third fiscal quarter of 2000. The nine-month period ended September 30, 2001, resulted in a net loss of \$3,541,797 compared to a net loss of \$2,157,170 for the same period last year.

IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2001, the FASB issued SFAS No. 141 "Business Combinations." SFAS 141 eliminates the pooling-of-interests method of accounting for business combinations except for qualifying business combinations that were initiated prior to July 1, 2001. In addition, SFAS 141 further clarifies the criteria to recognize intangible assets separately from goodwill. The requirements of Statement 141 are effective for any business combination accounted for by the purchase method that is completed after June 30, 2001. The adoption of SFAS No. 141 will not have a material effect on the Company's financial position or results or operations.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets." Under SFAS 142, goodwill and indefinite lived intangible assets are no longer amortized but are reviewed annually (or more frequently if impairment indicators arise) for impairment. Separable intangible assets that are not deemed to have an indefinite life will continue to be amortized over their useful lives (but with no maximum life). The amortization provisions of SFAS 142 apply to goodwill and intangible assets acquired after June 30, 2001. The adoption of SFAS No. 142 will decrease the amount of goodwill amortization the Company is recording in the statement of operations. The amount of goodwill amortization recorded for the nine months ended September 30, 2001 was \$258,953.

LIQUIDITY AND CAPITAL RESOURCES

Available working capital at September 30, 2001 increased approximately \$542,207 over September 30, 2000. This increase is primarily due to the investment from Crestview Capital Fund I.

The Company also experienced a significant decrease in accounts payable and other payables related to wholesale financing at September 30, 2001 versus September 30, 2000, reflecting lower revenues.

Inventories and accounts receivable at September 30, 2001 decreased from September 30, 2000, also due to lower revenues.

Current maturities of notes and installment obligations payable at September 30, 2001 decreased materially from September 30, 2000 generally due to replacement with longer-term debt.

Management of Vicom believes that, for the next 12 months, cash generated by sales of stock, and existing credit facilities, in aggregate, are adequate to meet the anticipated liquidity and capital resource requirements of its CTU business. Significant continuation of the Company's MultiBand's build-out is highly dependent on securing additional financing for future projects. Management believes that while future build-out

financing is available, there is no guarantee that said financing will be obtained or on terms acceptable to the Company.

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CAPITAL EXPENDITURES

The Company used \$1,585,278 for capital expenditures during the nine months ended September 30, 2001, as compared to \$1,409,830 in the similar period last year. Of the total year-to-date expenditures \$1,194,657 were incurred during the first quarter of 2001. These year-to-date 2001 expenditures were primarily for construction-in-process items, which totaled \$1,548,072 and related to the continued build-out of MultiBand (see Liquidity and Capital Resources). For the similar period last year, substantially all capital expenditures consisted of equipment acquired for internal use.

IMPACT OF YEAR 2000

The Company has experienced no significant system problems since January 1, 2000. In addition, the Company is not aware of any material problems being experienced by its suppliers and business partners. The Company believes it has adequately addressed the Year 2000 issue related to its internal systems and that it did not and will not have a material impact on its business, financial condition or its results of operations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Vicom is not subject to any material interest rate risk as any current lending agreements are at a fixed rate of interest.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

As of September 30, 2001, the Company was not engaged in any legal proceedings whose anticipated results would have a material adverse impact.

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

(a) An Annual Meeting of Vicom shareholders was held on May 20, 2001.

(b) The meeting resulted in the re-election for one year of the following individuals as follows:

Nominee	For	Against
Steven Bell	5,330,724	70,000
Jonathan Dodge	5,400,724	0
David Ekman	5,400,724	0
Marvin Frieman	5,400,724	0
Paul Knapp	5,400,724	0
James L. Mandel	5,330,724	70,000
Pierce McNally	5,400,724	0
Mark Mekler	5,400,724	0
Manuel A. Villafana	5,400,724	0

(c) Voting to ratify Lurie, Besikof, Lapidus & Co., LLP as independent auditors of Vicom for the fiscal year ended December 31, 2000:

For	Against	Abstain
-----	---------	---------

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5,400,724

0

2,500

ITEM 2. CHANGES IN SECURITIES

In September 2001, Vicom received an investment of \$500,000 in exchange for Vicom Common Shares and Warrants. The transaction for the common shares was completed at the then trading market price for Vicom Common Stock. The investment was made by the Crestview Capital Fund 1, a Chicago based fund, which invests in undervalued publicly traded and medical companies. Proceeds were used primarily to fund original MultiBand construction.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

- (a) Exhibits
None.
- (b) Reports on Form 8-K.
None.

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.

VICOM, INCORPORATED
Registrant

Date: November 14, 2001

By: /s/ James L. Mandel

James L. Mandel
CHIEF EXECUTIVE OFFICER

Date: November 14, 2001

By: /s/ Steven M. Bell

Steven M. Bell
CHIEF EXECUTIVE OFFICER
(PRINCIPAL FINANCIAL AND ACCOUNTING OFFICER)