APPIANT TECHNOLOGIES INC
Form 10-Q
May 20, 2002

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2002

[ ] 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 0-21999

APPIANT TECHNOLOGIES INC.
(Exact name of registrant as specified in its charter)

DELAWARE	84-1360852
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

6663 OWENS DRIVE
PLEASANTON, CALIFORNIA 94588
(Address of principal executive offices)

(925) 251-3200
(Registrant's telephone number)

Check 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 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 [X] NO [ ]

As of April 30, 2002, there were 16,229,901 shares of Common Stock outstanding.

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ITEM 1. Condensed Consolidated Financial Statements

APPIANT TECHNOLOGIES INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	March 31, 2002	September 30, 2001
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents.	$ 1,225,000	$ 3,379,000
Restricted cash.	113,000	117,000
Accounts receivable, less allowance for doubtful accounts of $250,000 and $328,000	478,000	1,123,000
Inventory.	799,000	890,000
Equipment at customers under integration	127,000	206,000
Prepaid expenses and other	1,358,000	418,000
TOTAL CURRENT ASSETS	4,100,000	6,133,000
Property and equipment, net.	3,870,000	5,381,000
Capitalized software, net.	17,269,000	16,664,000
Goodwill and other intangible assets, net.	8,340,000	10,255,000
Other assets	540,000	1,933,000

TOTAL ASSETS	$ 34,119,000	$ 40,366,000
LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Lines of credit	$ 300,000	$ 300,000
Accounts payable	6,733,000	8,834,000
Accrued liabilities	2,908,000	3,209,000
Deferred revenue	502,000	1,041,000
Income tax payable	141,000	302,000
Accrued liability related to warrants	370,000	1,818,000
Convertible promissory notes payable, net of Discounts	3,830,000	2,700,000
Notes payable	7,286,000	5,726,000
Capital lease obligations, current portion	286,000	4,085,000
TOTAL CURRENT LIABILITIES	22,356,000	28,015,000
Long term notes payable, net of current portion	419,000	379,000
Capital lease obligations, net of current portion	98,000	93,000
Other	26,000	39,000
TOTAL LIABILITIES	22,899,000	28,526,000
REDEEMABLE CONVERTIBLE PREFERRED STOCK	253,000	253,000
STOCKHOLDERS' EQUITY		
Common stock	159,000	157,000
Additional paid-in capital	85,142,000	80,657,000
Unearned stock-based compensation	(292,000)	(401,000)
Accumulated deficit	(73,730,000)	(68,364,000)
Accumulated other comprehensive loss	(312,000)	(462,000)
TOTAL STOCKHOLDERS' EQUITY	10,967,000	11,587,000
TOTAL LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND STOCKHOLDERS' EQUITY	$ 34,119,000	$ 40,366,000

The accompanying notes are an integral part of these condensed consolidated financial statements.

APPIANT TECHNOLOGIES INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(unaudited)

	Three Months Ended March 31,		Six Months Ende	
	2002	2001	2002	2
NET REVENUES:				

Products and integration services. .	$ 380,000	$ 2,111,000	$ 687,000	$ 3
Other services	2,056,000	4,389,000	5,132,000	9
TOTAL NET REVENUES	2,436,000	6,500,000	5,819,000	12
COST OF REVENUES:				
Products and integration services. .	157,000	1,691,000	352,000	3
Other services	2,854,000	3,383,000	4,927,000	6
TOTAL COST OF REVENUES	3,011,000	5,074,000	5,279,000	9
GROSS (LOSS) PROFIT.	(575,000)	1,426,000	540,000	3
OPERATING EXPENSES:				
Selling, general and administrative.	1,730,000	5,537,000	2,827,000	10
Research and development	521,000	526,000	1,138,000	1
Amortization of goodwill and other intangibles	994,000	201,000	2,013,000	
Release of capitalized lease obligation.	--	--	(2,839,000)	
TOTAL OPERATING EXPENSES	3,245,000	6,264,000	3,139,000	11
LOSS FROM OPERATIONS	(3,820,000)	(4,838,000)	(2,599,000)	(8
OTHER INCOME (EXPENSE):				
Interest income.	18,000	72,000	409,000	
Interest expense	(1,762,000)	(889,000)	(3,318,000)	(1
Other.	(10,000)	(145,000)	162,000	
Total other expense.	(1,754,000)	(962,000)	(2,747,000)	(1
Loss from operations before income tax.	(5,574,000)	(5,800,000)	(5,346,000)	(9
(Benefit) Provision for income tax .	(4,000)	111,000	20,000	
NET LOSS	(5,570,000)	(5,911,000)	(5,366,000)	(9
Preferred stock dividends.	--	--	--	(7
NET LOSS APPLICABLE TO COMMON STOCKHOLDERS	$ (5,570,000)	$ (5,911,000)	$ (5,366,000)	$ (17
BASIC AND DILUTED NET LOSS PER COMMON SHARE	$ (0.35)	$ (0.43)	$ (0.34)	$
COMPREHENSIVE LOSS				
Net loss	$ (5,570,000)	$ (5,911,000)	$ (5,366,000)	$ (9
Other comprehensive income Translation gain (loss)	12,000	(163,000)	150,000	
COMPREHENSIVE LOSS	$ (5,558,000)	$ (6,074,000)	$ (5,216,000)	$ (9

The accompanying notes are an integral part of these condensed consolidated financial statements.

APPIANT TECHNOLOGIES INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Six Month Ended March 31, 2002	Six Month Ended March 31, 2001
CASH FLOWS FROM OPERATING ACTIVITES:		
Net loss	$ (5,366,000)	$ (9,892,000)
Reduction in allowance for doubtful accounts	(78,000)	(26,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,618,000	964,000
Accretion of discounts on notes payable	3,338,000	147,000
Amortization of goodwill and other intangible assets	2,013,000	402,000
Provision for excess and obsolete inventory	--	197,000
Stock-based compensation relating to stock options and warrants	64,000	(1,794,000)
Release of capitalized lease obligation	(2,839,000)	--
Changes in operating assets and liabilities:		
Accounts receivable	782,000	(1,723,000)
Inventory	169,000	(31,000)
Prepaid expenses and other	(727,000)	(475,000)
Other assets	1,230,000	(458,000)
Accounts payable and other current liabilities	(3,660,000)	2,980,000
Accrued liability related to warrants	370,000	--
Income tax payable	(163,000)	44,000
Deferred revenue	(539,000)	551,000
CASH USED IN OPERATING ACTIVITIES	(3,788,000)	(9,114,000)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Restricted cash	5,000	3,000
Cash acquired in connection with acquisition	89,000	--
Capitalization of software development costs	(1,800,000)	(1,571,000)
Purchase of property and equipment	(151,000)	(1,164,000)
NET CASH USED IN INVESTING ACTIVITIES	(1,857,000)	(2,732,000)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment under line of credit	--	(343,000)
Proceeds from draw on equity line	--	1,745,000
Proceeds from issuance of notes, convertible notes and warrants	3,415,000	2,500,000
Proceeds from issuance of Series B preferred Stock, net of issuance costs	--	4,959,000
Proceeds from warrants and options exercised for common stock	--	1,640,000
Principal payments on capital lease obligations	(22,000)	(2,671,000)
Principal payment on notes payable to stockholders	(50,000)	--
NET CASH PROVIDED BY FINANCING ACTIVITIES	3,343,000	7,830,000
Effect of exchange rate changes on cash	148,000	(62,000)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(2,154,000)	(4,078,000)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	3,379,000	5,603,000
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 1,225,000	$ 1,525,000

The accompanying notes are an integral part of these condensed consolidated financial statements.

APPIANT TECHNOLOGIES INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Six Months Ended March 31, 2002	2001
Supplemental disclosures for cash flow information:		
Cash paid during the period for:		
Interest.	$ 22,000	$ 623,000
Income taxes.	24,000	177,000
NONCASH TRANSACTIONS:		
Beneficial conversion feature on convertible promissory Notes payable.	2,752,000	1,274,000
Reclassification of warrant liability to equity. . .	670,000	950,000
Write-off of assets related to release of capital lease liability	682,000	--
Property and equipment and software acquired under capital leases.	--	4,217,000
Preferred dividend on beneficial conversion feature of Series B Preferred Stock	--	7,626,000
Issuance of warrants to underwriters in conjunction with sale of Series B Preferred Stock	--	1,107,000
Modification of warrant exercise price in conjunction with sale of Series B Preferred Stock .	--	1,847,000
Liability for future issuance of common stock to underwriters in conjunction with sale of Series B Preferred Stock.	--	573,000
Payable for purchases of property and equipment and software.	--	4,913,000
Costs of borrowings on equity line	--	1,745,000
Conversion of Series B Preferred Stock into Common Stock	--	4,678,000
TOTAL NONCASH TRANSACTIONS	$ 4,104,000	$ 28,930,000

The accompanying notes are an integral part of these condensed consolidated financial statements.

APPIANT TECHNOLOGIES INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. BASIS OF PRESENTATION

The condensed consolidated financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures are adequate to make the information presented not misleading. The balance sheet as of September 30, 2001 is derived from the Company's audited financial statements included in its Form 10-K for the fiscal year ended September 30, 2001 but does not include all disclosures required by generally accepted accounting principles in the United States. These condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2001.

The unaudited condensed consolidated financial statements included herein reflect all adjustments (which include only normal recurring adjustments) which are, in the opinion of management, necessary to state fairly the results for the interim periods presented. The results of operations for the interim periods presented are not necessarily indicative of the operating results to be expected for any subsequent interim period or for the fiscal year ending September 30, 2002.

The consolidated financial statements include our results as well as the results of our significant operating subsidiaries: Appiant Technologies North America, Inc. ("Appiant NA") and Infotel Technologies (Pte) Ltd ("Infotel").

Appiant NA revenues were 28% and 41% of consolidated net revenues for the six months ended March 31, 2002 and 2001, respectively. Infotel revenues were 72% and 59% of consolidated net revenues for the six months ended March 31, 2002 and 2001, respectively.

LIQUIDITY

The condensed consolidated financial statements of the Company and its subsidiaries contemplate the realization of assets and satisfaction of liabilities in the normal course of business. The Company recorded a net loss of $5.4 million on net revenues of $5.8 million for the six months ended March 31, 2002 and sustained significant losses for the fiscal years ended 2001 and 2000. At March 31, 2002, the Company had an accumulative deficit of $73.7 million. As a result, the Company will need to generate significantly higher revenue to reach profitability as the organization of the new inUnison(SM) portal business is built. In addition, the amortization of capitalized software and other assets that the Company has purchased or developed for the new inUnison(SM) portal commenced on December 17, 2001. The Company is developing other technologies and amortization of the costs associated with these technologies will commence upon the completion of development.

Management's plans to reverse the recent trend of losses are to increase revenues and gross margins while controlling costs, primarily based on expected revenues for the Company's inUnison(SM) portal services applications. Continued existence of the Company is dependent on the Company's ability to obtain adequate funding and eventually establish profitable operations. The Company intends to obtain additional equity and/or debt financing in order to further finance the market introduction of its in Unison(SM) portal services and to meet working capital requirements. There remains significant uncertainly, however, about the Company's ability to continue as a going concern. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

2. NET LOSS PER SHARE

Net loss per share for both basic net loss per share, which is the weighted-average number of common shares outstanding, and diluted net loss per share, which includes the weighted-average number of common shares outstanding and all dilutive potential common shares outstanding, is calculated using the treasury stock method. For the three and six months ended March 31, 2002 and

2001, dilutive potential common shares outstanding reflects convertible promissory notes payable, convertible preferred stock, and shares and warrants to purchase the Company's common stock. The following table summarizes the Company's net loss per share computations for the three and six months ended March 31, 2002 and 2001 (in thousands, except per share amounts):

	Three Months Ended March 31,		Six Month Ended March	
	2002	2001	2002	2001
Net loss	$ (5,570)	$ (5,911)	$ (5,366)	$ (
Preferred stock dividends	--	--	--	(
Net loss applicable to common stock	$ (5,570)	$ (5,911)	$ (5,366)	$ (1
Weighted average shares used in net loss per share - basic and diluted	16,147	13,701	16,063	1
Net loss per share - basic and diluted	$ (0.35)	$ (0.43)	$ (0.34)	$
Antidilutive Securities:				
Shares issuable under employee common stock plans and warrants exercisable	9,266	5,969	9,266	
Convertible promissory notes	4,110	--	4,110	
Shares issuable for convertible referred shares	69	36	69	
Antidilutive securities not included in net loss per share calculation	13,445	6,005	13,445	

3. INVENTORY

Inventory consists of systems and system components and is valued at the lower of cost (first-in, first-out method) or market.

4. SOFTWARE DEVELOPMENT COSTS

The Company has adopted SOP 98-1 "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" as it intends to offer its software applications in a hosted service model. Software development costs, including costs incurred to purchase third party software, are capitalized beginning when the Company has determined factors are present, including among others, that technology exists to achieve the performance requirements, buy versus internal development decisions have been made and the Company's management has authorized the funding for the project. Capitalization of software costs ceases when the software is substantially complete and is ready for its intended use and is amortized over its estimated useful life of two to seven years using the straight-line method. To the extent that the Company were to license software, any revenues net of any direct incremental costs such as marketing, commissions, software reproduction costs, warranty, and service obligations, would be applied against the capitalized cost of software, and no profit would be recognized from such transactions unless and until net proceeds from licenses and amortization have reduced the capitalized carrying amount of the software to zero. Subsequent proceeds from licensing the software would be recognized as revenue.

When events or circumstances indicate the carrying value of internal use software might not be recoverable, the Company will assess the recoverability of these assets by determining whether the amortization of the asset balance over its remaining life can be recovered through undiscounted future operating cash flows. The amount of impairment, if any, is recognized to the extent that the carrying value exceeds the projected discounted future operating cash flows and is recognized as a write down of the asset. In addition, when it is no longer probable that computer software being developed will be placed in service, the asset will be recorded at the lower of its carrying value or fair value, if any, less direct selling costs.

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Our capitalized software costs were $1.5 million for the six months ended March 31, 2002 and $1.2 million in the six months ended March 31, 2001. On December 17, 2001 the Company began amortizing $10.4 million of these costs as the product was substantially complete and ready for its intended use. Amortization for the quarter ended March 31, 2002 was $782,000. Unamortized, capitalized costs of $7.3 million relate to those projects that are not as yet ready for their intended use.

5. RECENT ACCOUNTING PRONOUNCMENTS

In July 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141 ("SFAS 141"), "Business Combinations." SFAS 141 requires the purchase method of accounting for business combinations initiated after June 30, 2001 and eliminates the pooling-of-interests method. The Company believes that the adoption of SFAS 141 did not have a significant impact on its financial statements.

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 142 ("SFAS 142"), "Goodwill and Other Intangible Assets," which is effective for fiscal years beginning after March 15, 2001. SFAS 142 requires, among other things, the discontinuance of goodwill amortization. In addition, the Standard includes provisions upon adoption for the reclassification of certain existing recognized intangibles as goodwill, reassessment of the useful lives of existing recognized intangibles, reclassification of certain intangibles out of previously reported goodwill and the testing for impairment of existing goodwill and other intangibles. The Company is currently assessing but has not yet determined the impact of SFAS 142 on its financial position and results of operations.

In October 2001, the FASB issued SFAS 144 Accounting for the Impairment or Disposal of Long-Lived Assets, which is required to be applied in fiscal years beginning after December 15, 2001. SFAS 144 requires, among other things, the application of one accounting model for long-lived assets that are impaired or to be disposed of by sale. The Company believes that the adoption of SFAS 144 will not have a significant impact on its financial position or results of operations.

In May 2000, the Emerging Issues Task Force (EITF) issued EITF Issue No. 00-14, Accounting for Certain Sales Incentives. EITF Issue No. 00-14 addresses the recognition, measurement, and income statement classification for sales incentives that a vendor voluntarily offers to customers (without charge), which the customer can use in, or exercise as a result of, a single exchange transaction. Sales incentives that fall within the scope of EITF Issue No. 00-14 include offers that a customer can use to receive a reduction in the price of a product or service at the point of sale. The EITF changed the transition date for Issue 00-14, concluding that a company should apply this consensus no later than the company s annual or interim financial statements for the periods beginning after December 15, 2001. In June 2001, the EITF issued EITF Issue No. 00-25, Vendor Income Statement Characterization of Consideration Paid to a Reseller of the Vendor s Products, effective for periods beginning after December 15, 2001. EITF Issue No. 00-25 addresses whether consideration from a vendor to a reseller is (a) an adjustment of the selling prices of the vendor s products and, therefore, should be deducted from revenue when recognized in the vendor s statement of operations or (b) a cost incurred by the vendor for assets or services received from the reseller and, therefore, should be included as a cost or expense when recognized in the vendor s statement of operations. Upon application of these EITFs, financial statements for prior periods presented for comparative purposes should be reclassified to comply with the income statement display requirements under these Issues. In September of 2001, the EITF issued EITF Issue No. 01-09, Accounting for Consideration Given by Vendor to a Customer or a Reseller of the Vendor s Products, which is a codification of EITF Issues No. 00-14, No. 00-25 and No. 00-22 Accounting for Points and Certain Other Time-or Volume-Based Sales Incentive Offers and Offers for Free Products or Services to be Delivered in the Future. The Company has adopted these pronouncements in fiscal year 2002 and has recorded an offset to revenues of $28,000 in the second quarter of fiscal 2002.

6. COMMITMENTS AND CONTINGENCIES

CAPITAL LEASES

In December 2001, the Company reached an agreement with a vendor under which the vendor agreed to release the Company from capital lease obligations of $3.5 million. The agreement also provided for the return of equipment capitalized under the capital lease obligations of $0.7 million. In June 2001, the Company charged to operating expenses $3.7 million of consulting services related to its

first data center in Atlanta, Georgia, when its data center was relocated to Sunnyvale, California, as such costs had no future value following the relocation. According, the Company has recorded a gain of $2.8 million within operating expenses equal to the difference between the capital lease obligation and the book value of the capitalized equipment returned to the vendor.

At March 31, 2002, the Company leased other computer equipment and software under capital leases. These leases extend for varying periods through 2004.

Equipment and software under capital leases included in property and equipment are as follows:

	March 31, 2002	December 31, 2001
Equipment and software	$ 958,000	$ 958,000
Less: accumulated amortization	(472,000)	(414,000)
	$ 486,000	$ 544,000

Future capital lease payments are as follows:

	March 31, 2001
Fiscal Year	
2002	$ 200,000
2003	203,000
2004	31,000
	434,000
Less amount representing interest	(50,000)
Present value of minimum future payments	384,000
Less current portion	(286,000)
	$ 98,000

CONTINGENCIES

In January 2002, a default judgment was issued against the Company in favor of an equipment vendor in the amount of $123,000, which is recorded in accounts payable as of March 31, 2002. The Company was successful in having that default judgment set aside on February 6, 2002. The Company is in discussions to establish a mutually agreed upon payment plan and expects to settle this issue.

In October 2001, a software vendor filed suit against the Company for breach of contract totaling approximately $703,000, which is recorded in accounts payable as of March 31, 2002, plus interest and attorney's fees. On December 28, 2001, Appiant filed an answer denying this general demand, and is preparing a counter-suit for return of over $600,000 paid to this vendor. The Company will continue to otherwise vigorously pursue this matter.

In December 2001, a major customer tendered its internal defense costs and expenses arising from its defense of a lawsuit involving claims of infringement of certain patents. It is seeking reimbursement from Company of approximately $53,000. As the Company is only a distributor of these systems, any liability suffered by us is reimbursable by the supplier of these systems. The Company will continue to vigorously defend this matter.

In January 2002, a note holder filed suit demanding payment on a Note in the amount of $1.2 million. The Company and note holder have negotiated an agreed resolution of these notes involving a repayment plan of a minimum of $100,000 per month until the outstanding balance plus accrued interest is paid in full.

In January 2002, a services and equipment provider filed suit in Texas for breach of contract totaling $117,000 which is recorded in accounts payable as of March 31, 2002. The Company is currently in negotiations to resolve this claim.

In February 2002, two former owners of an acquired entity filed suit for breach of contract regarding the calculation of additional compensation due to them on the second anniversary of the acquisition. The lawsuit seeks approximately

$450,000 in damages, interest and attorney's fees. The Company successfully defeated plaintiff's application for a writ of attachment in March 2002. The Company will continue to vigorously defend this matter.

While management intends to defend these matters vigorously, there can be no assurance that any of these complaints or other third party assertions will be resolved without costly litigation, or in a manner that is not adverse to our financial position, results of operations or cash flow. No estimate can be made of the possible loss or possible range of loss associated with the resolution of these matters in excess of amounts accrued.

7. CONVERTIBLE PROMISSORY NOTES PAYABLE AND WARRANTS

During the three months ended March 31, 2002, the Company entered into several Convertible Promissory Notes Payable (the "Convertible Notes") with certain investors in the aggregate principal amount of $2,025,000, of which $1,550,000 was with members of the board of directors or shareholders. The Convertible Notes accrue interest at 10% per annum, which is payable in common stock at the time of conversion and are collateralized by the Company's legacy business accounts receivables, and the assets of the Infotel subsidiary, and mature on various dates from April 30, 2002 through October 15, 2002. The conversion price is equal to the lower of 90% of the closing price of the Company's common stock on the trading day immediately preceding the maturity date, or 90% of any subsequent interim financing that occurs between the issuance date of the notes and the maturity date. Upon conversion, the Convertible Notes have no specific registration rights.

In connection with these Convertible Notes, the Company issued warrants to purchase 1,315,000 shares of the Company's common stock at an exercise price of ranging from $1.32 per share to $1.80 per share. The estimated value of the warrants of $1,878,000 was determined using the Black-Scholes option pricing model and the following assumptions: contractual term of 5 years, a risk free interest rate of 3.375%, a dividend yield of 0% and volatility of 145%. The allocation of the Convertible Notes proceeds to the fair value of the warrants of $974,000 was recorded as a discount on the Convertible Notes and as additional paid-in capital. Upon exercise of the warrants, the holder has no specific registration rights. In addition, as a result of the beneficial conversion feature described above for the Convertible Notes, the Company recorded $1,051,000 additional paid-in capital, and a discount on the notes payable which is accreted over the note maturity period to interest expense. As a result, these discounts are accreted over the note maturity period and $498,000 was recorded as non-cash interest expense for the three months ended March 31, 2002.

Between October 31, 2001 and December 20, 2001, the Company entered into several Convertible Promissory Notes Payable (the "Convertible Notes") with certain investors in the aggregate principal amount of $1,390,000, of which $400,000 was with members of the board of directors or shareholders. The Notes accrue interest at 8% per annum, which is payable in common stock at the time of conversion and are collateralized by the Company's legacy business accounts receivables, and the assets of the Infotel subsidiary, and mature on various dates from December 27, 2001 to November 16, 2003. The conversion price is equal to the lower of 90% of the closing price of the Company's common stock on the trading day immediately preceding the maturity date, or 90% of any subsequent interim financing that occurs between the issuance date of the notes and the maturity date. Upon conversion, the Convertible Notes have no specific registration rights.

In connection with these Convertible Notes, the Company issued warrants to purchase 945,000 shares of the Company's common stock at an exercise price of ranging from $1.20 per share to $1.77 per share. The estimated value of the warrants of $1,269,000 was determined using the Black-Scholes option pricing model and the following assumptions: contractual term of 5 years, a risk free interest rate of 3.92%, a dividend yield of 0% and volatility of 148%. The allocation of the Convertible Notes proceeds to the fair value of the warrants of $663,000 was recorded as a discount on the Convertible Notes and as additional paid in capital. Upon exercise of the warrants, the holder has no specific registration rights.

The discount on the Convertible Notes related to the warrants is accreted over the note maturity period and $310,000 and $881,000 was recorded as non-cash interest expense for the three and six months ended March 31, 2002, resectively. In addition, as a result of the beneficial conversion feature described above for the Convertible Notes, the Company recorded $726,000 additional paid-in capital, and a discount on the notes payable which is accreted over the note maturity period to interest expense. As a result, $361,000 was recorded as interest expense for the six months ended March 31, 2002.

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Under the June 8, 2001 Convertible Notes Payable purchase agreement, the common stock issuable pursuant to the conversion of the notes and exercise of the related warrants were to be registered within 30 days after the next round of financing. Due to the registration requirement, the warrants were classified as liabilities and are remeasured to current estimated value at each reporting date using the Black-Scholes option pricing model. The change in estimated value is reported in the statement of operations. On December 1, 2001, certain of the warrant agreements were amended to remove the requirement to register the common stock under these warrants. Accordingly, the liability related to these warrants on December 1, 2001 of $670,000 was reclassified to stockholders' equity, additional paid-in capital. The Company recognized a reduction in interest expense of $442,000 and $778,000 for the three and six months ended March 31, 2002 due to the change in the estimated value of these warrants.

8. SEGMENT REPORTING

The Company defines operating segments as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. The operating segments disclosed are managed separately, and each represents a strategic business unit that offers different products and serves different markets.

The Company's reportable operating segments include Appiant Technologies Inc. (Appiant NA) and Infotel. Appiant NA includes the Company's enterprise operations in the US. Appiant NA enterprise operations include systems integration and distribution of voice processing and multimedia messaging equipment, technical support, ongoing maintenance and product development.

Infotel is a distributor and integrator of telecommunications and other electronics products operating in Singapore and provides radar system integration, turnkey project management, networking and test instrumentation services. Infotel derives substantially all of its revenue from sales in Singapore. There are no intersegment revenues.

The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies in the Company's Annual Report on Form 10-K for fiscal year ended September 30, 2001.

	APPIANT NA(1)	INFOTEL	TOTAL
THREE MONTHS ENDED March 31, 2002			
Net revenues to external customers	$ 688,000	$1,748,000	$ 2,436,000
Loss from operations	(3,510,000)	(310,000)	(3,820,000)
Non-current assets	29,678,000	341,000	30,019,000
THREE MONTHS ENDED March 31, 2001			
Net revenues to external customers	$ 2,817,000	$3,683,000	$ 6,500,000
Loss (income) from operations	(5,387,000)	549,000	(4,838,000)
Non-current assets	32,214,000	2,092,000	34,306,000
SIX MONTHS ENDED March 31, 2002			
Net revenues to external customers	$ 1,643,000	$4,176,000	$ 5,819,000
Loss from operations	(2,356,000)	(243,000)	(2,599,000)
Non-current assets	29,678,000	341,000	30,019,000
SIX MONTHS ENDED March 31, 2001			
Net revenues to external customers	$ 5,180,000	$7,435,000	$12,615,000
Loss (income) from operations	(9,500,000)	958,000	(8,542,000)
Non-current assets	32,214,000	2,092,000	34,306,000