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ONSPAN NETWORKING INC  
Form 10QSB  
May 12, 2004

U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-QSB

Quarterly Report Pursuant to Section 13 or 15(d) of the  
Securities Exchange Act of 1934

For Quarter Ended: MARCH 31, 2004

Commission File Number: 0-22991

ONSPAN NETWORKING, INC.  
-----

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

NEVADA  
-----

(State of Incorporation)

87-0460247  
-----

(IRS Employer ID No)

6413 CONGRESS AVENUE, SUITE 230, BOCA RATON, FL 33487  
-----

(Address of principal executive office)

(561) 988-2334  
-----

(Issuer's telephone number)

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 .

The number of shares outstanding of registrant's common stock, par value \$.012 per share, as of March 31, 2004 was 1,090,677.

Transitional Small Business Disclosure Format (Check one): Yes  No .

ONSPAN NETWORKING, INC. AND SUBSIDIARY

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Part I. Unaudited Financial Information

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### ONSPAN NETWORKING, INC. AND SUBSIDIARY

#### CONDENSED CONSOLIDATED BALANCE SHEET MARCH 31, 2004

(UNAUDITED)

#### ASSETS

##### CURRENT ASSETS

Cash and cash equivalents .....	\$ 12,064
Deposits .....	3,635
Prepaid Insurance .....	328
Inventory - Home .....	1,503,344
	-----
Total current assets .....	1,519,371
Property and equipment, net .....	3,820
Website .....	20,000
	-----
	\$ 1,543,191
	=====

#### LIABILITIES AND STOCKHOLDERS' EQUITY

##### CURRENT LIABILITIES

Accounts payable .....	\$ 161,518
Accrued dividend .....	30,946

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Accrued wages .....	50,500
Accrued interest .....	28,856
Note Payable - Related party .....	175,000
Loan Payable .....	681,000
Amounts due to purchasers of discontinued operations .....	55,929
	-----
Total current liabilities .....	1,183,749
STOCKHOLDERS' EQUITY	
Preferred stock; \$.001 par value; authorized 12,500 shares; issued and outstanding 2,713 shares; liquidation preference \$271,300 .....	2
Common stock, \$.012 par value. Authorized 8,333,333 shares; issued and outstanding 1,090,677 shares .....	13,088
Paid-in capital .....	7,908,845
Accumulated deficit .....	(7,562,493)
	-----
Total stockholders' equity .....	359,442
	-----
	\$ 1,543,191
	=====

See accompanying notes to condensed consolidated financial statements.

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ONSPAN NETWORKING, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
THREE AND SIX MONTHS ENDED MARCH 31, 2004 AND 2003

(UNAUDITED)

	THREE MONTHS ENDED MARCH 31,		SIX MONTHS ENDED MARCH 31,	
	2004	2003	2004	2003
	-----	-----	-----	-----
COSTS AND EXPENSES:				
Salaries and wages .....	\$ 43,500	\$ 40,000	\$ 65,500	\$ 79,000
Other selling, general and administrative expenses .....	208,924	25,624	291,568	59,289
	-----	-----	-----	-----
	252,424	65,624	357,068	138,289
	-----	-----	-----	-----
Loss from operations .....	(252,424)	(65,624)	(357,068)	(138,289)
OTHER INCOME (EXPENSE):				
Interest income .....	-	3,208	3	7,321
Unrealized (loss) on marketable equity securities .....	-	(30,000)	-	(49,000)
Interest expense .....	(2,525)	-	(2,525)	-
Other expense .....	-	-	-	(30,000)
	-----	-----	-----	-----
Total other income (expense) .....	(2,525)	(26,792)	(2,522)	(71,679)
	-----	-----	-----	-----

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LOSS BEFORE INCOME TAXES .....	(254,949)	(92,416)	(359,590)	(209,968)
INCOME TAX (BENEFIT) EXPENSE .....	-	-	-	-
LOSS FROM CONTINUING OPERATIONS .....	(254,949)	(92,416)	(359,590)	(209,968)
DIVIDENDS ON PREFERRED SHARES .....	-	-	-	-
NET LOSS APPLICABLE TO COMMON SHARES .....	\$ (254,949)	\$ (92,416)	\$ (359,590)	\$ (209,968)
BASIC AND DILUTED NET LOSS PER SHARE				
CONTINUED OPERATIONS .....	\$ (0.24)	\$ (0.10)	\$ (0.36)	\$ (0.22)
WEIGHTED AVERAGE SHARES OUTSTANDING				
BASIC .....	1,055,820	968,677	1,012,010	964,552
DILUTED .....	1,058,533	968,677	1,014,723	964,552

See accompanying notes to condensed consolidated financial statements.

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ONSPAN NETWORKING, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY  
SIX MONTHS ENDED MARCH 31, 2004

(UNAUDITED)

	Preferred Stock		Common Stock			Paid-in	Acco
	Shares	Par Value	Shares	Par Value	Capital	Deficit	
BALANCE, September 30, 2003	2,713	\$ 2	968,677	\$11,624	\$7,873,709	\$(7,202,903)	\$
Exercise of Stock Options .	122,000	\$1,464	\$ 35,136	\$36,600			
Net (loss) .....	-	-	-	-	-	(359,590)	(
BALANCE, March 31, 2004 ...	2,713	\$ 2	1,090,677	\$13,088	\$7,908,845	\$(7,562,493)	\$

See accompanying notes to condensed consolidated financial statements.

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ONSPAN NETWORKING, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
SIX MONTHS ENDED MARCH 31, 2004 AND 2003

(UNAUDITED)

	2004	2003
	-----	-----

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CASH FLOWS FROM OPERATING ACTIVITIES

Net loss .....	\$ (359,590)	\$ (209,968)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation .....	470	454
Deferred income taxes .....	-	-
Unrealized loss from marketable securities .....	-	49,000
Change in assets and liabilities		
Income tax receivable .....	-	45,147
Inventory .....	(39,000)	-
Deposit .....	(51)	-
Prepaid expenses .....	10,077	11,833
Accounts payable .....	95,483	(378)
Accrued expenses .....	69,923	30,000
Net cash used in operating activities .....	(222,688)	(73,912)

CASH FLOWS FROM INVESTING ACTIVITIES

Escrow Deposit .....	-	(130,000)
Capital expenditures .....	(22,922)	-
Net cash used in investing activities .....	(22,922)	(130,000)

CASH FLOWS FROM FINANCING ACTIVITIES

Loan Payable .....	181,000	-
Exercise of Stock Option .....	36,600	-
Net cash provided by financing activities .....	217,600	-
NET DECREASE IN CASH AND CASH EQUIVALENTS .....	(28,010)	(203,912)
CASH AND CASH EQUIVALENTS, beginning of period ...	40,074	1,030,611
CASH AND CASH EQUIVALENTS, end of period .....	\$ 12,064	\$ 826,699

Continued

See accompanying notes to condensed consolidated financial statements.

ONSPAN NETWORKING, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
SIX MONTHS ENDED MARCH 31, 2004 AND 2003

(UNAUDITED)  
(CONTINUED)

	2004	2003
	-----	-----

SUPPLEMENTAL CASH FLOW INFORMATION

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Cash paid for interest and income taxes are as follows:

Interest .....	\$	28,856	\$	-
Income taxes .....	\$	-	\$	-
Financed insurance premiums .....	\$	-	\$	-

See accompanying notes to condensed consolidated financial statements.

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### ONSPAN NETWORKING, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS THREE MONTHS ENDED MARCH 31, 2004 AND 2003

(UNAUDITED)

##### A. ORGANIZATION

Onspan Networking, Inc. (the "Company" or "Onspan"), a Nevada corporation, is a holding company. Onspan changed its name from Network Systems International, Inc. effective February 10, 2001.

Originally incorporated in 1985, as Network Information Services, Inc., Network Systems International, Inc. ("NESI"), a Nevada corporation, was the surviving corporation of a reverse merger completed in April 1996. The Company became a publicly traded entity in connection with the re-organization.

On July 10, 1998, the Company's stock was officially approved for listing on the NASDAQ small cap market and the Company's common stock began trading on NASDAQ Small Cap under the symbol NESI. As of April 2, 2002, the securities were de-listed from the Nasdaq SmallCap market and now trade on the Over-The-Counter Bulletin Board under the symbol ONSP.

On November 10, 2000, Onspan completed the acquisition of 100% of the issued and outstanding common stock of InterLAN, a Virginia corporation.

On August 5, 2002, the Company sold and transferred the stock of its wholly-owned subsidiary, InterLAN Communications, Inc. to G. Anthony Munno, Martin Sainsbury Carter and Brian Ianniello, who were executives and employees of InterLAN. In exchange for the assignment of the InterLAN stock, Messrs. Munno, Carter and Ianniello transferred 21,168 shares of Onspan common shares, and Onspan was relieved of substantially all obligations and guarantees provided to third parties. Onspan also retained the right to a certain tax refund in amount of \$45,147 owing to InterLAN. These individuals also resigned in all capacities as directors, officers and/or employees of Onspan. Onspan retained the following assets of the corporation in cash of \$1,078,883, the marketable securities, the prepaid expenses, the entire income tax receivable, and \$2,611 in property. The liabilities Onspan retained include the dividend payable amount due to purchasers of discontinued operations, and the balance of the note payable.

On April 22, 2003 the Company created a new subsidiary, Coventry 1 Inc. which is a Nevada Corporation. The Company's other subsidiary Onspan SmartHouse, Inc., is a Florida Corporation.

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Prior to August 5, 2002, the Company, a Nevada corporation, was a holding Company, that through its wholly owned subsidiary, InterLAN Communications, Inc. ("InterLAN"), developed data communications and networking infrastructure solutions for business,

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government and education. Following August 5, 2002, the Company, announced a change in its strategy and subsequently sold its operating division InterLAN. In April of 2003, the Company changed its focus to investing in and revitalizing single family homes in established residential neighborhoods in suburban areas. The Company acquired its first property on June 19, 2003. The Company has entered into a contract with Garcia Brenner & Stromberg architects to design the project. The Company intends to renovate and expand the existing single-family home project on this site. This project, known as Coventry 1 Inc., has received its permits.

The financial statements included in this report have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission for interim reporting and include all adjustments (consisting only of normal recurring adjustments) that are, in the opinion of management, necessary for a fair presentation. These financial statements have not been audited.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations for interim reporting. The Company believes that the disclosures contained herein are adequate to make the information presented not misleading. However, these financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report for the year ended September 30, 2003, which is included in the Company's Form 10-KSB for the year ended September 30, 2003. The financial data for the interim periods presented may not necessarily reflect the results to be anticipated for the complete year.

### B. ACCOUNTING POLICIES

**PRINCIPLES OF CONSOLIDATION** - The accompanying consolidated financial statements for the period ended March 31, 2004 and 2003 include the accounts of Onspan Networking, Inc. and its subsidiaries, Coventry 1, Inc. and Onspan Smarthouse Inc. All significant intercompany accounts and transactions have been eliminated.

**CASH AND CASH EQUIVALENTS** - The Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

**FAIR VALUE OF FINANCIAL INSTRUMENTS** - The carrying values of cash and cash equivalents, accounts receivable, marketable equity securities, notes receivable, accounts payable, amounts due to purchasers of discontinued operations and note payable approximate fair value as of March 31, 2004, because of the short maturity of these instruments.

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**REVENUE RECOGNITION** - The Company recognizes revenue from all homebuilding activities at the closing of the sale using the deposit method. During construction, all direct material and labor costs and those indirect costs related to acquisition and construction are capitalized, and all customer deposits are treated as liabilities. Capitalized costs are charged to earnings upon closing. Costs incurred in connection with completed homes and selling,

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general, and administrative costs are charged to expense as incurred. Provision for estimated losses on uncompleted contracts and on speculative projects is made in the period in which such losses are determined

PREFERRED STOCK - At March 31, 2004, the Company had 2,713 shares outstanding of its Series A Convertible Preferred Stock ("Series A"). This issue has a stated liquidation preference value of \$100 per share redeemable at the Company's option, has no voting rights, and each preferred share is convertible into 4 shares of the Company's common stock as adjusted for the 1 for 12 reverse stock split. Dividends on the Series A were to be paid monthly in cash at a rate of 12% of the original issue. The Company's Board of Directors, elected that the payment of cash dividends on its Series A to be suspended. In particular, the Board took such actions as necessary to preserve the Company's working capital in order to ensure the continued viability of the Company. The Board of Directors is unable at this time to predict if the Company will resume the payment of cash dividends on its Series A 12% Cumulative Convertible Preferred Stock. However, the Company has accrued dividends on these shares in the amount of \$30,946 at March 31, 2004.

INCOME TAXES - The Company accounts for income taxes under the provisions of Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("SFAS 109"). Under SFAS 109, the liability method is used in accounting for income taxes and deferred tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

STOCK OPTION PLAN - The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations, in accounting for its stock option plan. As such, compensation expense would be recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price.

EARNINGS PER SHARE - The financial statements are presented in accordance with Statement of Financial Accounting Standards No. 128 ("SFAS 128"), "Earnings Per Share". Basic earnings per share is computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share reflect the potential dilution from the exercise or conversion of securities into common stock.

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USE OF ESTIMATES - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

PROPERTY AND EQUIPMENT - Property and equipment are stated at cost. Expenditures for significant renewals and improvements are capitalized. Repairs and maintenance are charged to expense as incurred. Depreciation is computed using an accelerated method for both financial and tax purposes based upon the useful lives of the assets.

OTHER ASSETS - Monies paid for acquisition of www.VOIS.com were \$20,000, were capitalized as a component of Other Assets on the Company's balance sheet. In accordance with Statement of Financial Accounting Standards No. 144,



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"Accounting for the Impairment or Disposal of Long-Lived Assets", the Company follows the policy of evaluating all qualifying assets as of the end of each reporting quarter. For the quarter ended March 31, 2004, no charges to operations were made for impairments in the future benefit of this asset. The Company will amortize the asset over three years .

### C. INVENTORY HOME

Inventory - home which is reflected at cost consists of the following at March 31, 2004 :

Home Basis .....	\$1,440,865
Improvements .....	62,479
	-----
Total Basis .....	\$1,503,344
	=====

### D. PROPERTY AND EQUIPMENT

Property and equipment, which are reflected at cost, consist of the following at March 31, 2004:

Computer equipment .....	\$ 6,613
	-----
Total property and equipment .	\$ 6,613
Less: accumulated depreciation	(2,791)
	-----
Property and equipment, net ..	\$ 3,820
	=====

Depreciation expense for the six months ended March 31, 2004 and 2003 is \$470 and \$454, respectively.

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### E. REVOLVING CREDIT NOTE

The Company has a demand line of credit with a related party (Evolve One Inc), totaling \$1,000,000, under which the Company may borrow on an unsecured basis at 5% annually. There was \$681,000 outstanding under this line of credit at March 31, 2004. Evolve One has deferred receiving the first payment of interest due under the Note at December 19, 2003. As of March 31, 2004 the Company has accrued \$26,331 in interest on this note. As of March 31, 2004, Evolve One, Inc did not have sufficient cash reserves to fully fund the available credit under the line of credit.

The terms of the demand line of credit state that the Company must issue options to purchase common stock equal to 10% of the dollar amount of the loan advance at an exercise price of \$0.10 per share, and options to purchase common stock equal to 90% of the dollar amount of the loan advance at the ten trading day average at the time of the draw (\$0.30 at June 30, 2003). Under these terms, the Company issued 675,000 stock options resulting in a charge to interest expense of \$110,008.

### F. NOTE PAYABLE - SHAREHOLDER

The Note Purchase agreement, a Convertible Promissory Note for \$100,000 was issued by the Company on October 24, 2003 to Mr. Tabin. This note is due on July 31, 2004, and accrues interest at a rate of 5.25% per annum payable at maturity. As of March 31, 2004 the Company has accrued \$2,281 in interest on this note. If the Company defaults on this note, the aggregate principle plus accrued interest

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will be eligible to be converted immediately into shares of common stock. If the note is not repaid or converted by the due date, then the company will issue to Mr. Tabin a three year warrant to purchase shares of the Company's common stock, par value \$.012 per share for the aggregate exercise price of \$5,000, at a price per share equal to \$0.01.

On February 27, 2004 the Company entered into a Secured Promissory Note with our President, Herbert Tabin. The Note Agreement, is a Secured Promissory Note for \$50,000 that was issued by the Company on February 27, 2004 to Mr. Tabin. This note is due on August 1, 2004, and accrues interest at a rate of 5.25% per annum payable at maturity. As of March 31, 2004 the Company has accrued \$244 in interest on this note. The note is secured by a security interest in property located at 3764 Coventry Lane, Boca Raton .

On March 31, 2004 the Company entered into a Secured Promissory Note with our President, Herbert Tabin. The Note Agreement, is a Secured Promissory Note for \$25,000 that was issued by the Company on March 31, 2004 to Mr. Tabin. This note is due on August 1, 2004, and accrues interest at a rate of 5.25% per annum payable at maturity. As of March 31, 2004 the Company has accrued \$0 in interest on this note. The note is secured by a security interest in property located at 3764 Coventry Lane, Boca Raton.

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### STOCKHOLDERS EQUITY

On January 26, 2004, Gary Schultheis exercised 122,000 employee stock options. These options had an exercisable price of .30 a share.

### G. EARNINGS PER SHARE

Basic earning (loss) per share is computed by dividing earnings available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflect per share amounts that would have resulted if dilutive potential common stock had been converted to common stock. The following reconciles amounts reported in the financial statements:

	2004 ----	2003 ----
Net loss from continuing operations .....	\$ (359,590)	\$ (209,968)
Denominator for basic earnings per share - Weighted average shares .....	1,012,010	964,552
Effect of dilutive securities - stock options .....	-	-
Denominator for diluted earnings per share - Weighted average shares adjusted for dilutive securities	1,012,010 =====	964,552 =====
Basic and diluted earnings (loss) per common share:		
Net (loss) .....	\$ (.36) =====	\$ (.22) =====

### H. LEGAL PROCEEDINGS

1. Network Systems International of North Carolina, Inc. v Network Systems International, Inc. and OnSpan Networking, Inc. (02-CvS-10154) (Complaint filed

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September 13, 2002). This action asserts a claim for breach of contract against the Company, seeking certain tax refunds obtained by the Company. The plaintiff, a former subsidiary of the Company, claims that these tax refunds belong to the plaintiff. The Company has filed an answer disputing the amounts claimed and seeking reimbursement for certain expenses incurred by the Company on behalf of the plaintiff. The parties have engaged in settlement discussions, which have been unsuccessful to date.

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### 2. Securities Actions:

a. Richard T. Clark and Joel C. Holt, individually, and derivatively, on behalf of OnSpan Networking, Inc. v. OnSpan Networking, Inc. and Herbert Tabin, Case No. 03-CV-298K (N.D. Okla.) (Removed from state court May 1, 2003); This action asserts claims for fraud, breach of contract, breach of fiduciary duties, and civil conspiracy. The action seeks damages in the amount of \$300,000, for each plaintiff, the plaintiffs' attorneys' fees and costs, and certain other relief. The case was filed in Oklahoma State court on March 28, 2003, and it was removed to federal court on May 1, 2003. The Company and Herb Tabin have filed a Motion to Dismiss all claims asserted. A special committee for the Board of OnSpan retained independent counsel to conduct an independent investigation into the derivative shareholder claims and an independent report has been issued

b. D. Mark White v OnSpan Networking, Inc. and Herbert Tabin, Case No. 352198686 03 (District Court, Tarrant County Texas) (Complaint filed May 2, 2003). This action asserts claims for violation of Texas securities law, fraud, and breach of fiduciary duties. The action seeks unspecified damages, restitution in the amount of \$300,000, treble damages, pre-judgment interest, the plaintiffs' attorneys' fees and costs, and certain other relief. The case was filed in Texas state court on May 2, 2003, and thereafter was removed to federal court in Ft. Worth. A mediation was conducted in February of 2004, although the case was not settled.

The company has conducted and answered extensive written discovery, though only one deposition has taken place so far (on grounds limited to jurisdiction). The company filed a motion to compel further discovery to substantiate plaintiff's contentions, which in large part was granted by the court in April of 2004. Plaintiff failed to provide the court ordered additional discovery, and thus, the company is seeking further relief pursuant to the court order. The company filed a third-party claim for breach of contract against RichMark Capital Corporation in February 2004, and will seek discovery from it in the near future.

The Company will vigorously defend all three of these actions.

### I. GOING CONCERN

The accompanying condensed financials were prepared assuming that the Company will continue as a going concern. The Company is currently a party to several legal proceedings and although the Company will vigorously defend all of these actions, the Company is unable to estimate with any reasonable certainty what liability it may have to these litigants. There are no assurances that the Company will be successful in defending these legal proceedings, or if successful the cost of defending these legal proceedings may significantly deplete the capital of the Company impairing the Company's ability to continue as a going concern. Accordingly, there are no assurances that the Company will

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be successful in achieving the above plans, or that such plans, if consummated, will enable the Company to obtain profitable operations or continue as a going concern, in addition the Company's lender does not have sufficient cash reserves to fund the available credit line.

### J. CONCENTRATIONS

#### GEOGRAPHICAL

Currently, all of the Company's material revenues to be derived in 2004 are from one house located in Palm Beach County within the State of Florida. Accordingly, the Company could be adversely affected by natural disasters, such as hurricanes or other tropical storms or events, economic downturns, significant unemployment, and other economic conditions that may occur from time to time in Florida, which may not have as much impact on more geographically diversified competitors.

#### FINANCIAL

The Company is currently reliant on construction/mortgage financing provided by one lender - Evolve One Inc. Any financial or legal impairment of this lender may have an impact on our current projects. An impairment of our lender may force the Company to cancel outstanding projects, may cause project delays or may ultimately force the Company to sell its projects.

### K. SUBSEQUENT EVENT

On April 16, 2004, the Company announced it will have to sell the real estate project it acquired in June 2003 in order to service mounting legal expenses associated with litigation. The Company, which had received engineering plans for the real estate project, had intended to renovate and expand the existing single-family home on this site.

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

### CRITICAL ACCOUNTING ESTIMATES AND POLICIES

The Company has identified the policies outlined below as critical to its business operations and an understanding of its results of operations. The listing is not intended to be a comprehensive list of all of the Company's accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by accounting principles generally accepted in the United States, with no need for management's judgment in their application. The impact and any associated risks related to these estimates and policies on the Company's business operations is discussed throughout Management's Discussion and Analysis or plan of operations where such policies affect the Company's reported and expected financial results. For a detailed discussion on the

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application of these and other accounting estimates or policies, see the Notes to Consolidated Financial Statements. The Company's preparation of the financial statements requires it to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the Company's financial statements, and the reported amounts of revenue and expenses during the reporting period. There can be no assurance that actual results will not differ from those estimates.

### PLAN OF OPERATION

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Prior to August 5, 2002, the Company, a Nevada corporation, was a holding Company, that through its wholly owned subsidiary, InterLAN Communications, Inc. ("InterLAN"), developed data communications and networking infrastructure solutions for business, government and education. Following August 5, 2002, the Company, announced a change in its strategy and subsequently sold its operating division InterLAN. In April of 2003, the Company changed its focus to investing in and revitalizing single family homes in established residential neighborhoods in suburban areas. The Company acquired its first property on June 19, 2003. The Company has entered into a contract with Garcia Brenner & Stromberg architects to design the project. The Company intends to renovate and expand the existing single-family home project on this site. This project, known as Coventry 1 Inc., has received its permits.

### RISK FACTORS

#### REAL ESTATE DEVELOPMENT INDUSTRY

Ownership of properties in the categories of which the Company invests is highly fragmented among individuals, partnerships, public and private corporations, and REITs. No single entity or person dominates the market for such properties. At any given time, a significant number of home properties as well as individual lots and tracts suitable for single-family homes are available for purchase in the various markets where the Company may seek additional acquisitions. Industry risks include environmental hazards; changes in general or local economic conditions; changes in interest rates and the availability of permanent mortgage financing which may render the acquisition, sale, or refinancing of a property difficult or unattractive and which may make debt service burdensome; changes in real estate and zoning laws; changes in income taxes, real estate taxes, or federal or local economic or rent controls; floods, earthquakes, and other acts of nature; and other factors beyond the control of any firm involved in the real estate development industry. Further, the Company, as other companies its size, will in all probability continue to encounter problems in obtaining contractors who, in turn, are able to obtain performance bonds for building contracts; obtaining bank financing for construction; and obtaining financing without personal guarantees of its officers and directors, all of which materially adversely affect its ability to carry on its business. The illiquidity of real estate investments generally may impair an industry participant's ability to respond promptly to changing circumstances. See "Risk Factors," below.

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#### CERTAIN RISK FACTORS ASSOCIATED WITH REAL ESTATE AND RELATED INVESTMENTS.

The Company is subject to the risks associated with ownership, operation, and financing of real estate. These risks include, but are not limited to, liability for environmental hazards; changes in general or local economic conditions; changes in interest rates and the availability of construction and permanent mortgage financing which may render the acquisition, sale, or refinancing of a property difficult or unattractive and which may make debt service burdensome; changes in real estate and zoning laws; bonding requirements; permitting requirements, changes in income taxes, real estate taxes, or federal or local economic or rent controls; floods, earthquakes, and other acts of nature; and other factors beyond the company's control. The illiquidity of real estate investments generally may impair the Company's ability to respond promptly to changing circumstances. Under federal, state, and local environmental laws, ordinances, and regulations, the Company may be liable for removal or remediation costs, as well as other costs (such as fines or injuries to persons and property) where our employees may have arranged for removal, disposal, or treatment of hazardous or toxic substances. In addition, environmental laws impose liability for release of asbestos-containing materials into the air, and

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third parties can seek recovery from the Company for personal injury associated with those materials.

LIMITED REVENUES; LIMITED RELEVANT OPERATING HISTORY; SIGNIFICANT AND CONTINUING OPERATING LOSSES; NEGATIVE CASH FLOW; ACCUMULATED DEFICIT.

Since its change in focus the Company has not had any revenues from sales of its properties. Accordingly, the Company has a limited relevant operating history upon which an evaluation of its prospects can be made. Such prospects must be considered in light of the risks, expenses and difficulties frequently encountered in the establishment of a relatively new business in the real estate development industry, which is a continually evolving industry characterized by an increasing number of market entrants and intense competition, as well as the risks, expenses and difficulties encountered in the real estate development and building construction business. The Company prior to its change has incurred operating losses and has an accumulated deficit of approximately \$7,562,493. There can be no assurance that the Company will be successful in generating revenues at a sufficient quantity or margin or that the Company will ever achieve profitable operations.

SIGNIFICANT CAPITAL REQUIREMENTS; NEED FOR ADDITIONAL CAPITAL.

The Company's capital requirements have been and will continue to be significant. The Company has been dependent primarily on existing capital and a credit line. Future capital needs may be satisfied by either the private placement of equity securities and/or debt financings. The Company based on its cash requirements and exposure to liability from shareholder lawsuits is unsure

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if existing capital will be sufficient for the next twelve months. In the event that the Company's plans (due to unanticipated expenses, delays, problems, or otherwise), the Company would be required to seek additional funding. Any such additional funding could be in the form of additional equity capital. The Company is currently, contemplating, pursuing potential funding opportunities. However, there can be no assurance that any of such opportunities will result in actual funding or that additional financing will be available to the Company when needed, on commercially reasonable terms, or at all. If the Company is unable to obtain additional financing if needed, it will likely be required to curtail its real estate development plans and may possibly cease its operations. Any additional equity financings may involve substantial dilution to the Company's then-existing shareholders.

MANAGEMENT OF GROWTH AND ATTRACTION AND RETENTION OF KEY PERSONNEL.

Management of the Company's growth may place a considerable strain on the Company's management, operations and systems. The Company's ability to execute any future business strategy will depend in part upon its ability to manage the demands of a growing business. Any failure of the Company's management team to effectively manage growth could have a material adverse affect on the Company's business, financial condition or results of operations. The Company's future success depends in large part on the continued service of its key management personnel. The Company believes that its future success also depends on its ability to attract and retain skilled technical, managerial and marketing personnel. Competition for qualified personnel is intense. The Company has from time to time experienced difficulties in recruiting qualified personnel. Failure by the Company to attract and retain the personnel it requires could have a material adverse affect on the financial condition and results of operations of the Company.

VOLATILITY OF MARKET PRICE; ISSUANCE OF SUBSTANTIAL NUMBER OF SHARES; AUTHORIZED

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### SHARES; PROXY RULES.

The Company's Common Stock has been traded since 1994. The Company believes that factors such as (but not limited to) the sale of common stock issued on conversion of the Company's debentures, announcements of developments related to the Company's business, fluctuations in the Company's quarterly or annual operating results, failure to meet expectations, general economic conditions, interest rate changes or money supply fluctuations and developments in the Company's relationships with clients and suppliers will cause the price of the Company's Common Stock to fluctuate substantially. In recent years the stock market has experienced extreme price fluctuations, which have often been unrelated to the operating performance of affected companies. Such fluctuations could adversely affect the market price of the Company's Common Stock.

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### PENNY STOCK REGULATIONS AND REQUIREMENTS FOR LOW PRICED STOCK.

The Commission adopted regulations which generally define a "penny stock" to be any non-Nasdaq equity security that has a market price of less than \$5.00 per share, subject to certain exceptions. Based upon the price of the Company's Common Stock as currently traded on the OTC Bulletin Board, the Company's stock is subject to Rule 15c-9 under the Exchange Act which imposes additional sales practice requirements on broker-dealers which sell securities to persons other than established customers and "accredited investors." For transactions covered by this Rule, a broker-dealer must make a special suitability determination for the purchaser and have received a purchaser's written consent to the transaction prior to sale. Consequently, the Rule may have a negative effect on the ability of shareholders to sell common shares of the Company in the secondary market.

### MANAGEMENT CONTROLS THE COMPANY'S FUNDS.

Management has broad discretion over how to spend the funds held by the Company. Although management will endeavor to act in the best interests of the shareholders, there can be no assurance that the decision to utilize proceeds will prove profitable to the Company.

### THE COMPANY MAY NOT BE SUCCESSFUL.

The Company is to compete in the competitive market of real estate development and housing construction. The Company's prospects for success will depend on management's ability to successfully market its lots or houses to buyers and its apartment projects to renters. As a result, demand and market acceptance for our projects is subject to a high level of uncertainty. The Company currently has limited resources to undertake the activities that will be necessary to acquire property and build real estate projects. If the Company is unable to expand its efforts, it will not generate substantial additional revenues. Investors should be aware that if the Company is not successful in the operation of its current business, or any future acquisition endeavors, each investor's entire investment in the Common Stock of the Company could become worthless. Even if the Company is successful in our operations and potential acquisitions, it is not certain that investors will derive a profit from investment in the Company.

### THE COMPANY RELIES ON ITS MANAGEMENT.

The Company is dependent upon the members of management set forth herein. If the current management is no longer able to provide services to the Company, its business will be negatively affected.

### ADDITIONAL DEBT, OR EQUITY FINANCING MAY AFFECT INVESTOR'S ABILITY TO SELL COMMON STOCK.

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The Company's common stock currently trades on the OTC Bulletin Board under the symbol ONSP. Stocks trading on the OTC Bulletin Board generally attract a smaller

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number of market makers and a less active public market and may be subject to significant volatility. If the Company raises additional money from the sale of its Common Stock, the market price could drop and investor's ability to sell stock could be diminished. Further, even if the Company is able to increase its authorized shares, there can be no assurance that it will be able to obtain sufficient shareholder votes in the future for any such increase, which votes are required by Nevada law.

THE COMPANYS STRATEGY INCLUDES PURSUING STRATEGIC ACQUISITIONS THAT MAY NOT BE SUCCESSFUL

The Company will consider acquiring businesses that are intended to add products and or services. Acquisitions involve a number of operational risks that the acquired business may not be successfully integrated, may distract management attention, may involve unforeseen costs and liabilities, and possible regulatory costs, some or all of which could have a materially adverse effect on the Company's financial condition or results of operations. Additionally, the Company may make acquisitions with cash or with stock, or a combination thereof. If the Company does make any such acquisitions, various associated risks may be encountered, including potential dilution to the Company's then current shareholders, as a result of additional shares of common stock being issued in connection with the acquisitions.

THE COMPANY'S STOCK PRICE WILL FLUCTUATE AND MAY FALL BELOW EXPECTATIONS OF SECURITIES ANALYSTS AND INVESTORS, WHICH COULD SUBJECT THE COMPANY TO LITIGATION

The market price of the Company's common stock may fluctuate significantly in response to a number of factors, some of which are beyond its control. These factors include:

- quarterly variations in operating results;
- changes in accounting treatments or principles;
- existing litigation;
- announcements by the Company or its competitors of new products and services offerings, significant contracts, acquisitions or strategic relationships;
- additions or departures of key personnel;
- any future sales of the Company's common stock or other securities;

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- stock market price and volume fluctuations of publicly-traded companies in general and Internet-related companies in particular; and
- general political, economic and market conditions.

It is likely that in some future quarter the Company's operating results may fall below the expectations of securities analysts and investors, which could



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result in a decrease in the trading price of the Company's common stock. In the past, securities class action litigation has often been brought against a company following periods of volatility in the market price of its securities. The Company may be the target of similar litigation in the future. Securities litigation could result in substantial costs and divert management's attention and resources, which could seriously harm the Company's business and operating results.

THERE IS A LIMITED PUBLIC MARKET FOR THE COMPANY'S COMMON STOCK AND THERE ARE NO ASSURANCES OF A CONTINUED TRADING MARKET FOR THE COMPANY'S COMMON STOCK

The Company's common stock is currently quoted on the OTC Bulletin Board (R) Market (OTCBB) under the symbol "ONSP". The Company's common stock is thinly traded. There are no assurances the Company will maintain its OTC Bulletin Board (R) listing. If the Company's common stock should be delisted from the OTC Bulletin Board(R) Market, it is likely that the stock would then be quoted on the Pink Sheets Market, which could materially and / or adversely effect any future liquidity in the Company's common stock.

INABILITY TO SECURE AN INDEPENDENT AUDIT COMMITTEE MEMBER

Due to the potential exposure to litigation and small compensation, it may be difficult to secure an Independent Audit Committee Member. If the Company is unable to secure an Independent Audit Committee Member, it may be in violation of current audit standards and may be subject to possible de-listing of which could have a materially adverse affect on the Company's financial condition or results of operations.

HISTORY OF BUSINESS

Originally incorporated in 1985, as Network Information Services, Inc., Network Systems International, Inc. ("NESI"), a Nevada corporation, was the surviving corporation of a reverse merger completed in April 1996. The Company became a publicly traded entity in connection with the re-organization. On July 10, 1998, the Company's stock was officially approved for listing on the NASDAQ Small Cap market and the Company's common stock began trading on NASDAQ Small Cap under the symbol NESI. As of April 2, 2002, the securities were de-listed from the NASDAQ Small Cap market and now trade on the Over-The-Counter Bulletin Board under the symbol ONSP. Effective February 10, 2001, the Company changed its name

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from Network Systems International, Inc., to Onspan Networking, Inc. (the "Company" or "Onspan"). On October 9, 2001, the Company effected a 1 for 12 reverse stock split of its issued and outstanding common stock. Prior to August 5, 2002, the Company, a Nevada corporation, was a holding company, that through its wholly owned subsidiary, InterLAN Communications, Inc. ("InterLAN"), developed data communications and networking infrastructure solutions for business, government and education. On August 5, 2002, the Company completed the sale of its operating division InterLAN and a changed its strategy of business. On April 22, 2003 the Company created a new subsidiary, Coventry 1 Inc. that is a Nevada Corporation. The Company's other subsidiary Onspan SmartHouse, Inc., is a Florida Corporation.

FORWARD LOOKING STATEMENTS

From time to time, the Company may publish forward-looking statements relative to such matters as anticipated financial performance, business prospects, technological developments and similar matters. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. All statements other than statements of historical fact included in

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this section or elsewhere in this report are, or may be deemed to be, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Exchange Act of 1934. Important factors that could cause actual results to differ materially from those discussed in such forward-looking statements include: 1. General economic factors including, but not limited to, changes in interest rates and trends in disposable income; 2. Information and technological advances; 3. Cost of products sold; 4. Competition; and 5. Success of marketing, advertising and promotional campaigns.

### A. LIQUIDITY AND CAPITAL RESOURCES

The Company based on its cash requirements and exposure to liability from shareholder lawsuits is unsure if existing capital will be sufficient for the next twelve months. The Company will be required to seek additional funding during the next twelve months. The Company is currently, contemplating, pursuing potential funding opportunities which may include additional equity capital. However, there can be no assurance that any of such opportunities will result in actual funding or that additional financing will be available to the Company when needed, on commercially reasonable terms, or at all. Any additional equity financings may involve substantial dilution to the Company's then-existing shareholders.

On April 16, 2004, the Company announced it will have to sell the real estate project it acquired in June 2003 in order to service mounting legal expenses associated with litigation. The Company, which had received engineering plans for the real estate project, had intended to renovate and expand the existing single-family home on this site.

During the six months ended March 31, 2004, working capital decreased \$345,443 to \$335,622 from \$681,065. During this same period, stockholders' equity decreased \$322,990 to \$359,442 from \$682,432. The decrease in stockholders' equity is

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due mainly to the net loss for the period (\$359,590) and the exercise of employee stock options \$36,600. The Company has budgeted significant capital expenditures for the current fiscal year to make improvements on the house. The Company is currently reliant on construction/mortgage financing provided by one lender - Evolve One Inc. As of March 31, 2004, Evolve One, Inc did not have sufficient cash reserves to fully fund the available credit under the line of credit. Any financial or legal impairment of this lender may have an impact on our current project. An impairment of our lender may force the Company to cancel outstanding project, may cause project delays or may ultimately force the Company to sell its project.

The Company is currently a party to several legal proceedings and although the Company will vigorously defend all of these actions, the Company is unable to estimate with any reasonable certainty what liability it may have to these litigants. There are no assurances that the Company will be successful in defending these legal proceedings, or if successful the cost of defending these legal proceedings may significantly deplete the capital of the Company impairing the Company's ability to continue as a going concern. Accordingly, there are no assurances that the Company will be successful in achieving the above plans, or that such plans, if consummated, will enable the Company to obtain profitable operations or continue as a going concern.

### B. RESULTS OF OPERATIONS

SELLING, GENERAL AND ADMINISTRATIVE EXPENSE - The Company's selling, general and administrative expenses, including salaries and wages amounted to \$357,068

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during the six months ended March 31, 2004 as compared to \$138,289 during the six months ended March 31, 2003. The increase of \$218,779 includes primarily a decrease of (\$13,500) for salaries , and (\$11,883) for D & O insurance , off set by a increase of \$203,700 for legal fees due to the three ongoing lawsuits , \$2,475 in stock transfer fees, \$13,000 for travel for the meeting with potential investment opportunities, and \$20,598 in rent and related utilities.

INCOME TAXES - The Company recorded \$136,500 in deferred income tax expense for the six-month period ended March 31, 2004, a 100% valuation allowance was taken against this amount as of March 31, 2004. The Company recorded \$78,374 in deferred income tax expense for the six-month period ended March 31, 2003, a 100% valuation allowance was taken against this amount as of March 31, 2003

The North Carolina Department of Revenue has contacted the Company with regard to state income taxes for the tax year ended September 30, 1999.

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Upon investigation, the Company has determined that former management did not file a state income tax return in North Carolina for that year although a return was filed in Florida for that year. The Company is in the process of investigating the situation and of evaluating what action should be taken as a result of the inquiry by the North Carolina Department of Revenue. The Company has been unable to estimate with any reasonable certainty what liability it may have to the State of North Carolina.

MARKETABLE EQUITY SECURITIES - As of March 31, 2003, the Company held 100,000 shares of eResource Capital Group (AMEX:RCG) ("eResource") with a cost basis of \$504,000 (\$5.04 per share). For the six months ended March 31, 2003, the Company recorded an unrealized loss from trading securities of (\$49,000) on the Company's stock and had a quoted market value of \$31,000 or \$0.31 (thirty one cents) per share.

### PART II - OTHER INFORMATION

#### ITEM 1.

##### LEGAL PROCEEDINGS

1. Network Systems International of North Carolina, Inc. v Network Systems International, Inc. and OnSpan Networking, Inc. (02-CvS-10154) (Complaint filed September 13, 2002). This action asserts a claim for breach of contract against the Company, seeking certain tax refunds obtained by the Company. The plaintiff, a former subsidiary of the Company, claims that these tax refunds belong to the plaintiff. The Company has filed an answer disputing the amounts claimed and seeking reimbursement for certain expenses incurred by the Company on behalf of the plaintiff. The parties have engaged in settlement discussions, which have been unsuccessful to date.

#### 2. Securities Actions:

a. Richard T. Clark and Joel C. Holt, individually, and derivatively, on behalf of OnSpan Networking, Inc. v. OnSpan Networking, Inc. and Herbert Tabin, Case No. 03-CV-298K (N.D. Okla.) (Removed from state court May 1, 2003); This action asserts claims for fraud, breach of contract, breach of fiduciary duties, and civil conspiracy. The action seeks damages in the amount of \$300,000, for each plaintiff, the plaintiffs' attorneys' fees and costs, and certain other relief. The case was filed in Oklahoma State court on March 28, 2003, and it was removed to federal court on May 1, 2003. The Company and Herb Tabin have filed a Motion to Dismiss all claims asserted. A special committee for the Board of OnSpan retained independent counsel to conduct an independent investigation into the

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derivative shareholder claims and an independent report has been issued.

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b. D. Mark White v OnSpan Networking, Inc. and Herbert Tabin, Case No. 352198686 03 (District Court, Tarrant County Texas) (Complaint filed May 2, 2003). This action asserts claims for violation of Texas securities law, fraud, and breach of fiduciary duties. The action seeks unspecified damages, restitution in the amount of \$300,000, treble damages, pre-judgment interest, the plaintiffs' attorneys' fees and costs, and certain other relief. The case was filed in Texas state court on May 2, 2003, and thereafter was removed to federal court in Ft. Worth. A mediation was conducted in February of 2004, although the case was not settled.

The company has conducted and answered extensive written discovery, though only one deposition has taken place so far (on grounds limited to jurisdiction). The company filed a motion to compel further discovery to substantiate plaintiff's contentions, which in large part was granted by the court in April of 2004. Plaintiff failed to provide the court ordered additional discovery, and thus, the company is seeking further relief pursuant to the court order. The company filed a third-party claim for breach of contract against RichMark Capital Corporation in February 2004, and will seek discovery from it in the near future.

ITEM 2.

### CHANGE IN SECURITIES

On January 26, 2004, Gary Schultheis exercised 122,000 employee stock options. These options had an exercisable price of .30 a share.

ITEM 5.

### OTHER INFORMATION

There is no immediate family relationship between or among any of the Directors and Executive Officers, except Ms. Dermer who is the sister-in-law of Mr. Tabin.

### Evaluation of disclosure controls and procedures

Within the 90 days prior to the filing date of this report, the Company carried out an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. This evaluation was done under the supervision and with the participation of the Company's President and Chief Financial Officer. Based upon that evaluation, they concluded that the Company's disclosure controls and procedures are effective in gathering, analyzing and disclosing information needed to satisfy the Company's disclosure obligations under the Exchange Act.

### Changes in internal controls

There were no significant changes in the Company's internal controls or in other factors that could significantly affect those controls since the most recent evaluation of such controls.

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ITEM 6.

### EXHIBITS AND REPORTS ON FORM 8-K

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a. Exhibits

- 4.0 Long Term Incentive Stock Options Plan (1)
- 31.1 Certification of President Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of President Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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(1) Incorporated by reference to the company's report on form S-8 dated July 27, 2001

b. Reports on Form 8-K

- 1. Form 8-K filed with the Securities and Exchange Commission October 16, 2001 announcing the Onspan Networking, Inc. (the "Company"), filed a Certificate pursuant to Section 78.207 of the Nevada Statutes whereby the Company decreasing the number of issued and outstanding shares of common stock, par value \$.012, at a rate of one for twelve (1:12), and proportionately decreasing the number of authorized shares of common stock at a rate of one for twelve (1:12). As a result, the Company's authorized common stock has been reduced from 100,000,000 shares to 8,333,333 shares, and the number of issued and outstanding shares of common stock were reduced from 11,574,619 to approximately 964,552 shares.
- 2. Form 8-K filed with the Securities and Exchange Commission August 8, 2002 announcing on August 5, 2002, the Company sold and transferred the stock of its wholly-owned subsidiary, InterLAN Communications, Inc. to G. Anthony Munno, Martin Sainsbury Carter and Brian Ianniello, who were executives and employees of InterLAN. In exchange for the assignment of the InterLAN stock, Messrs. Munno, Carter and Ianniello transferred 21,168 shares of Onspan common shares, and Onspan was relieved of substantially all obligations and guarantees provided to third parties. Onspan also retained the right to a certain tax refund owing to InterLAN. These individuals also resigned in all capacities as directors, officers and/or employees of Onspan. InterLAN provides data communications and network solutions and consulting services.

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SIGNATURE

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.

ONSPAN NETWORKING, INC.

Date: May 12, 2004

By: /s/ Herbert Tabin  
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Herbert Tabin, President

Date: May 12, 2004

By: /s/ Marissa Dermer

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Marissa Dermer, Chief Financial  
and Principal Accounting Officer

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