

NEW CENTURY COMPANIES INC  
Form 10-Q  
August 14, 2009

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

FORM 10-Q

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

For the quarterly period ended June 30, 2009

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

Commission file number: 000-09459

NEW CENTURY COMPANIES, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

061034587  
(I.R.S. Employer  
Identification Number)

9831 Romandel Ave.  
Santa Fe Springs, CA 90670  
(Address of principal executive offices)

(562) 906-8455  
(Registrant's telephone number, including area code)

Not applicable  
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No x

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer  
Non-accelerated filer

Accelerated filer  
Smaller reporting company x

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

As of July 28, 2009, the Company had 15,344,654 shares of common stock, \$0.10 par value, issued and outstanding.

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NEW CENTURY COMPANIES, INC.

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### Forward-Looking Statements

This Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. For example, statements regarding the Company's financial position, business strategy and other plans and objectives for future operations, and assumptions and predictions about future product demand, supply, manufacturing, costs, marketing and pricing factors are all forward-looking statements. These statements are generally accompanied by words such as "intend," "anticipate," "believe," "estimate," "potential(ly)," "continue," "forecast," "predict," "plan," "may," "will," "could," "would," "shou negative of such terms or other comparable terminology. The Company believes that the assumptions and expectations reflected in such forward-looking statements are reasonable, based on information available to it on the date hereof, but the Company cannot provide assurances that these assumptions and expectations will prove to have been correct or that the Company will take any action that the Company may presently be planning. However, these forward-looking statements are inherently subject to known and unknown risks and uncertainties. Actual results or experience may differ materially from those expected or anticipated in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, regulatory policies, available cash, research results, competition from other similar businesses, and market and general economic factors. This discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto included in Item 1 of this Quarterly Report on Form 10-Q.

## Part I - Financial Information

## ITEM 1. FINANCIAL STATEMENTS

NEW CENTURY COMPANIES, INC. AND SUBSIDIARY  
CONDENSED CONSOLIDATED BALANCE SHEETS  
June 30, 2009 and December 31, 2008

	(Unaudited) June 30, 2009	December 31, 2008
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash	\$ -	\$ 31,889
Contract receivables, net of allowance of \$0 and \$24,000 for June 30, 2009 and December 31, 2008, respectively	11,906	237,787
Inventories	422,856	564,022
Costs and estimated earnings in excess of billings on uncompleted contracts	60,790	416,664
Deferred financing costs	283,433	252,305
Prepaid expenses and other current assets	160,182	168,668
<b>Total current assets</b>	<b>939,167</b>	<b>1,671,335</b>
Property and Equipment, net	152,225	186,906
Deferred Financing Costs, net	113,862	233,702
<b>Total Assets</b>	<b>\$ 1,205,254</b>	<b>\$ 2,091,943</b>
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>		
<b>Current Liabilities</b>		
Bank overdraft	\$ 44,553	\$ 15,329
Accounts payable and accrued liabilities	1,643,751	1,417,464
Dividends payable	500,550	459,275
Billings in excess of costs and estimated earnings on uncompleted contracts	84,402	1,388,348
Capital lease obligation, current portion	24,044	27,874
Derivative liability	4,080,953	1,975,298
CAMOFI Convertible note payable, net of discount of \$1,423,780 at June 30, 2009 and \$2,089,443 at December 31, 2008, respectively	1,403,501	737,838
CAMHZN Convertible note payable, net of discount of \$239,535 at June 30, 2009 and \$350,090 at December 31, 2008, respectively	510,465	399,910
CAMOFI Convertible Note, net of discount of \$96,039	605,161	-
CAMHZN Convertible Note, net of discount of \$23,896	149,904	-

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Total current liabilities	9,047,284	6,421,336
Long Term Liabilities		
Capital lease obligation, long term portion	-	9,804
Total liabilities	9,047,284	6,431,140
Commitments and Contingencies		
Stockholders' Deficit		
Cumulative, convertible, Series B preferred stock, \$1 par value, 15,000,000 shares authorized, no shares issued and outstanding (liquidation preference of \$25 per share)	-	-
Cumulative, convertible, Series C preferred stock, \$1 par value, 75,000 shares authorized, 26,880 shares issued and outstanding (liquidation preference of \$672,000)	26,880	26,880
Cumulative, convertible, Series D preferred stock, \$25 par value, 75,000 shares authorized, 11,640 shares issued and outstanding (liquidation preference of \$291,000)	291,000	291,000
Common stock, \$0.10 par value, 50,000,000 shares authorized; 15,344,654 shares issued and outstanding at June 30, 2009 and December 31, 2008	1,534,466	1,534,466
Notes receivable from stockholders	(564,928)	(564,928)
Deferred equity compensation	(64,167)	(101,667)
Additional paid-in capital	7,390,021	7,355,007
Accumulated deficit	(16,455,302)	(12,879,955)
Total stockholders' deficit	(7,842,030)	(4,339,197)
Total Liabilities and Stockholders' deficit	\$ 1,205,254	\$ 2,091,943

See accompanying notes to the condensed consolidated financial statements.

NEW CENTURY COMPANIES, INC. AND SUBSIDIARY  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
For the Three and Six Months Ended June 30, 2009 and 2008  
(Unaudited)

	For the Three Months Ended June 30		For the Six Months Ended June 30,	
	2009	As Restated 2008	2009	As Restated 2008
CONTRACT REVENUES	\$ 1,359,630	\$ 1,434,676	\$ 2,414,332	\$ 2,961,278
COST OF SALES	1,193,730	1,363,614	2,012,623	2,672,093
GROSS PROFIT	165,900	71,062	401,709	289,185
<b>OPERATING EXPENSES</b>				
Consulting and other compensation	77,158	73,998	139,773	345,382
Salaries and related	83,409	74,123	236,496	127,619
Selling, general and administrative	135,967	278,441	367,988	716,470
TOTAL OPERATING EXPENSES	296,534	426,562	744,257	1,189,471
OPERATING LOSS	(130,634)	(355,500)	(342,548)	(900,286)
<b>OTHER INCOME (EXPENSES)</b>				
Gain on writeoff of accounts payable	-	3,577	5,681	60,205
(Loss) / gain on valuation of derivative liabilities	225,075	1,287,654	(1,575,903)	2,588,416
Interest expense	(952,461)	(497,382)	(1,620,856)	(984,151)
TOTAL OTHER INCOME (EXPENSES)	(727,386)	793,849	(3,191,078)	1,664,470
INCOME (LOSS) BEFORE PROVISION FOR INCOME TAXES	(858,020)	438,349	(3,533,626)	764,184
PROVISION FOR INCOME TAXES	-	-	-	-
NET INCOME (LOSS)	\$ (858,020)	\$ 438,349	\$ (3,533,626)	\$ 764,184
Preferred Stock Dividends	\$ (41,275)	\$ (41,275)	\$ (41,275)	\$ (41,275)
NET INCOME (LOSS) APPLICABLE TO COMMON STOCKHOLDERS	\$ (899,295)	\$ 397,074	\$ (3,574,901)	\$ 722,909
Basic net income (loss) available to common stockholders per common share	\$ (0.06)	\$ 0.03	\$ (0.23)	\$ 0.05
	\$ (0.06)	0.01	(0.23)	\$ 0.02

Diluted net income (loss) available to common  
stockholders per common share

Basic weighted average common shares outstanding	15,344,654	15,344,656	15,344,654	15,344,656
Diluted weighted average common shares outstanding	15,344,654	45,450,838	15,344,654	45,450,838

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See accompanying notes to the condensed consolidated financial statements.

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NEW CENTURY COMPANIES, INC. AND SUBSIDIARY  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
For the Six Months Ended June 30, 2009 and 2008  
(Unaudited)

	2009	As Restated 2008
<b>Cash flows from operating activities:</b>		
Net (loss) income	\$ (3,533,626)	\$ 764,184
<b>Adjustments to reconcile net (loss) income to net cash used in operating activities:</b>		
Depreciation and amortization of property and equipment	34,681	41,232
Bad debt expense	-	27,259
Gain on write off of accounts payable	(5,681)	(60,205)
Amortization of deferred financing costs	233,712	180,960
Estimated fair value of options issued to employees	35,014	-
Amortization of stock-based consulting fees and employee compensation	37,500	251,165
Amortization of BCF and debt discount	1,136,035	503,788
(Gain) / loss on valuation of derivatives liabilities	1,575,903	(2,588,416)
<b>Changes in operating assets and liabilities:</b>		
Contracts receivable	225,881	20,717
Inventories	141,166	232,377
Costs and estimated earnings in excess of billings on uncompleted contracts	355,874	135,363
Prepaid expenses and other current assets	8,486	(264,416)
Accounts payable and accrued liabilities	281,520	202,406
Billings in excess of costs and estimated earnings on uncompleted contracts	(1,303,946)	241,013
<b>Net cash used in operating activities</b>	<b>(777,481)</b>	<b>(312,573)</b>
<b>Cash flows from financing activities:</b>		
Bank overdraft	29,224	47,665
Proceeds from issuance of convertible notes payable, net of financing costs	730,000	-
Principal payments on notes payable and capital lease	(13,632)	-
Deferred financing cost	-	(16,821)
<b>Net cash provided by financing activities</b>	<b>745,592</b>	<b>30,844</b>
<b>Net change in cash</b>	<b>(31,889)</b>	<b>(281,729)</b>
Cash at beginning of period	31,889	281,729
Cash at end of period	\$ -	\$ -
<b>Supplemental disclosure of non-cash financing and investing activities:</b>		
Accrued cumulative dividends on preferred stock	\$ 41,275	\$ 41,275

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Debt discount recorded on convertible notes payable	\$ 479,752	\$ 2,755,107
Stock and warrants Issued for Financing Costs	\$ -	\$ 102,500

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See accompanying notes to the condensed consolidated financial statements.

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NEW CENTURY COMPANIES, INC. AND SUBSIDIARY  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2009 AND 2008 (As Restated)

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## 1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

### Organization And Nature Of Operations

New Century Companies, Inc. and its wholly owned subsidiary, New Century Remanufacturing, Inc., (collectively, the "Company"), a California corporation, was incorporated March 1996 and is located in Southern California. The Company provides after-market services, including rebuilding, retrofitting and remanufacturing of metal cutting machinery. Once completed, a remanufactured machine is "like new" with state-of-the-art computers and the cost to the Company's customers is substantially less than the price of a new machine.

The Company currently sells its services by direct sales and through a network of machinery dealers primarily in the United States. Its customers are generally medium to large sized manufacturing companies in various industries where metal cutting is an integral part of their businesses. The Company grants credit to its customers who are predominately located in the western United States.

The Company trades on the OTC Bulletin Board under the symbol "NCNC."

### Principles Of Consolidation

The condensed consolidated financial statements include the accounts of New Century Companies, Inc. and its wholly owned subsidiary, New Century Remanufacturing, Inc. All significant intercompany accounts and transactions have been eliminated in consolidation.

### Basis Of Presentation

The accompanying unaudited interim condensed consolidated financial statements have been prepared by the Company, pursuant to the rules and regulations of the United States Securities and Exchange Commission (the "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 ("GAAP") have been omitted pursuant to such SEC rules and regulations; nevertheless, the Company believes that the disclosures are adequate to make the information presented not misleading. These financial statements and the notes hereto should be read in conjunction with the financial statements, accounting policies and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2008, filed with the SEC. In the opinion of management, all adjustments necessary to present fairly, in accordance with GAAP, the Company's financial position as of June 30, 2009, and the results of operations and cash flows for the interim periods presented, have been made. Such adjustments consist only of normal recurring adjustments. The results of operations for the three and six months ended June 30, 2009 are not necessarily indicative of the results for the full year ending December 31, 2009. Amounts related to disclosure of December 31, 2008 balances within these interim condensed consolidated financial statements were derived from the audited 2008 consolidated financial statements and notes thereto.

## Reclassifications

The Company has reclassified the presentation of prior-year information to conform to the current presentation.

## Going Concern

The accompanying condensed consolidated financial statements have been prepared assuming the Company will continue as a going concern, which contemplates, among other things, the realization of assets and satisfaction of liabilities in the normal course of business. As of June 30, 2009, the Company has an accumulated deficit of approximately \$16,455,000, had recurring losses, a working capital deficit of approximately \$8,108,000, and was also in default on its convertible notes. These factors raise substantial doubt about the Company's ability to continue as a going concern. The Company intends to fund operations through anticipated increased sales along with renegotiated or new debt and equity financing arrangements which management believes may be insufficient to fund its capital expenditures, working capital and other cash requirements for the year ending December 31, 2009. Therefore, the Company will be required to seek additional funds to finance its long-term operations. The successful outcome of future activities cannot be determined at this time and there is no assurance that if achieved, the Company will have sufficient funds to execute its intended business plan or generate positive operating results.

In response to these problems, management has taken the following actions:

- The Company continues its aggressive program for selling machines.
- The Company continues to implement plans to further reduce operating costs.
- The Company is seeking investment capital through the public and private markets.
- The Company is seeking strategic acquisition candidates.

The condensed consolidated financial statements do not include any adjustments related to recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

## Inventory

Inventories are stated at the lower of cost or net realizable value. Cost is determined under the first-in, first-out method. Inventories represent cost of work in process on units not yet under contract. Cost includes all direct material and labor, machinery, subcontractors and allocations of indirect overhead. At each balance sheet date, the Company evaluates its ending inventories for excess quantities and obsolescence. Among other factors, the Company considers historical demand and forecasted demand in relation to the inventory on hand and market conditions when determining obsolescence and net realizable value. Provisions are made to reduce excess or obsolete inventories to their estimated net realizable values. Once established, write-downs are considered permanent adjustments to the cost basis of the excess or obsolete inventories.

## Revenue Recognition

The Company's revenues consist primarily of contracts with customers. The Company uses the percentage-of-completion method of accounting to account for long-term contracts pursuant to Statements of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts", and, therefore, takes into account the cost, estimated earnings and revenue to date on fixed-fee contracts not yet completed. The percentage-of-completion method is used because management considers total cost to be the best available measure of progress on the contracts. Because of inherent uncertainties in estimating costs, it is at least reasonably possible that the estimates used will change within the near term.



For contracts, the amount of revenue recognized at the financial statement date is the portion of the total contract price that the cost expended to date bears to the anticipated final cost, based on current estimates of cost to complete. Contract costs include all materials, direct labor, machinery, subcontract costs and allocations of indirect overhead.

Because contracts may extend over a period of time, changes in job performance, changes in job conditions and revisions of estimates of cost and earnings during the course of the work are reflected in the accounting period in which the facts that require the revision become known. At the time a loss on a contract becomes known, the entire amount of the estimated ultimate loss is recognized in the financial statements.

Contracts that are substantially complete are considered closed for financial statement purposes. Costs incurred and revenue earned on contracts in progress in excess of billings (under billings) are classified as a current asset. Amounts billed in excess of costs and revenue earned (over billings) are classified as a current liability.

For revenues from stock inventory the Company follows Staff Accounting Bulletin ("SAB") No. 104, "Revenue Recognition", which outlines the basic criteria that must be met to recognize revenue other than revenue on contracts, and provides guidance for presentation of this revenue and for disclosure related to these revenue recognition policies in financial statements filed with the SEC.

The Company accounts for shipping and handling fees and costs in accordance with EITF Issue No. 00-10, "Accounting for Shipping and Handling Fees and Costs." Shipping and handling fees and costs incurred by the Company are immaterial to the operations of the Company and are included in cost of sales.

In accordance with Statements of Financial Accounting Standards ("SFAS") No. 48, "Revenue Recognition when Right of Return Exists," revenue is recorded net of an estimate for markdowns, price concessions and warranty costs. Such reserve is based on management's evaluation of historical experience, current industry trends and estimated costs. As of June 30, 2009, the Company estimated the markdowns, price concessions and warranty costs and concluded amounts are immaterial and did not record any adjustment to revenues.

#### Basic And Diluted Loss Per Common Share

Basic net earnings (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted net income (loss) per share is computed by dividing net loss by the weighted average number of common shares and dilutive common stock equivalents outstanding for each respective period.

Common stock equivalents, representing convertible Preferred Stock, convertible debt, options and warrants totaling approximately 74,320,847 shares at June 30, 2009 are not included in the diluted loss per share as they would be anti-dilutive. Common stock equivalents, representing convertible Preferred Stock, convertible debt, options and warrants totaling approximately 30,106,000 are included in the diluted income per share at June 30, 2008.

#### Stock Based Compensation

Effective January 1, 2006, we adopted the fair value method of accounting for employee stock compensation cost pursuant to SFAS No. 123(R), "Share-Based Payments." Under the fair value recognition provisions of SFAS 123(R), share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense on a straight-line basis over the requisite service period, which is the vesting period. For the three and six months ended June 30, 2009 and 2008, \$35,014 and \$0, respectively, of share-based compensation expense was recognized in the accompanying condensed consolidated statements of operations.



From time to time, the Company's Board of Directors grants common share purchase options or warrants to selected directors, officers, employees, consultants and advisors in payment of goods or services provided by such persons on a stand-alone basis outside of any of the Company's formal stock plans. The terms of these grants are individually negotiated and generally expire within five years from the grant date.

Under the terms of the Company's 2000 Stock Option Plan, options to purchase an aggregate of 5,000,000 shares of common stock may be issued to officers, key employees and consultants of the Company. The exercise price of any option generally may not be less than the fair market value of the shares on the date of grant. The term of each option generally may not be more than five years.

There is no share-based compensation resulting from the application of SFAS No. 123R to options granted outside of the Company's Stock Option Plan for the three and six months ended June 30, 2009 and 2008. Share-based compensation recognized as a result of the adoption of SFAS No. 123R use the Black Scholes option pricing model for estimating fair value of options granted.

In accordance with SFAS No. 123R, the Company's policy is to adjust share-based compensation on a quarterly basis for changes to the estimate of expected award forfeitures based on actual forfeiture experience.

The fair value of stock-based awards to employees and directors is calculated using the Black-Scholes option pricing model, even though the model was developed to estimate the fair value of freely tradable, fully transferable options without vesting restriction, which differ significantly from the Company's stock options. The Black-Scholes model also requires subjective assumptions regarding future stock price volatility and expected time to exercise, which greatly affect the calculated values. The expected term of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. The risk-free rate selected to value any particular grant is based on the U.S. Treasury rate that corresponds to the pricing term of the grant effective as of the date of the grant. The expected volatility is based on the historical volatility of our common stock. These factors could change in the future, affecting the determination of stock-based compensation expense in future periods.

There were no options granted, exercised or cancelled during the six months ended June 30, 2009. There are 900,000 shares available for grant at June 30, 2009.

All options outstanding have vested as of June 30, 2009 and are as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term in Years	Aggregate Intrinsic Value (1)
Vested	4,100,000	\$ 0.15	1.49	\$ —

(1) Represents the added value as difference between the exercise price and the closing market price of the Company's common stock at the end of the reporting period (as of June 30, 2009 and December 31, 2008, the market price of the Company's common stock was \$0.07 and \$0.05, respectively).



The Company follows SFAS No. 123(R) (as interpreted by EITF Issue No. 96-18, "Accounting for Equity Instruments That Are Issued To Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services") to account for transactions involving services provided by third parties where the Company issues equity instruments as part of the total consideration. Pursuant to paragraph 7 of SFAS No. 123 (R), the Company accounts for such transactions using the fair value of the consideration received (i.e. the value of the goods or services) or the fair value of the equity instruments issued, whichever is more reliably measurable. The Company applies EITF Issue No. 96-18 in transactions when the value of the goods and/or services are not readily determinable the fair value of the equity instruments is more reliably measurable and the counterparty receives equity instruments in full or partial settlement of the transactions, using the following methodology:

- a) For transactions where goods have already been delivered or services rendered, the equity instruments are issued on or about the date the performance is complete (and valued on the date of issuance).
- b) For transactions where the instruments are issued on a fully vested, non-forfeitable basis, the equity instruments are valued on or about the date of the contract.
- c) For any transactions not meeting the criteria in (a) or (b) above, the Company re-measures the consideration at each reporting date based on its then current stock value.

The following table summarizes information related to stock options outstanding and exercisable at June 30, 2009:

Exercise Price	Number of Options outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price
\$ 0.075-0.083	1,300,000	0.24	\$ 0.08
\$ 0.15-0.20	2,800,000	1.25	\$ 0.19
	4,100,000		\$ 0.15

From time to time, the Company issues warrants to employees and to third parties pursuant to various agreements, which are not approved by the shareholders.

The following is a status of the warrants outstanding at June 30, 2009 and December 31, 2008:

	Outstanding Warrants		
	Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value (1)
December 31, 2008	5,586,824	\$ 0.21	\$ —
Grants	—	—	—
Exercises	—	—	—
Cancellations/ Terminated	—	—	—
Outstanding and Exercisable at June 30, 2009	5,586,824	\$ 0.21	\$ —

(1) Represents the added value as difference between the exercise price and the closing market price of the Company's common stock at the end of the reporting period (as of June 30, 2009 and December 31, 2008, the market price of the Company's common stock was \$0.07 and \$0.05, respectively).

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The following table summarizes information related to warrants outstanding and exercisable at December 31, 2009:

Exercise Price	Number of Warrants outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price
\$ 0.60-0.70	1,372,538	0.72	\$ 0.64
\$ 0.07	4,214,286	3.39	\$ 0.07
	5,586,824		\$ 0.21

#### Deferred Financing Costs

Direct costs of securing debt financing are capitalized and amortized over the term of the related debt. When a loan is paid in full, any unamortized financing costs are removed from the related accounts and charged to interest expense. During the three months ended June 30, 2009 and 2008, the Company amortized approximately \$117,000 and \$90,000, respectively, to interest expense. During the six months ended June 30, 2009 and 2008, the Company amortized approximately \$234,000 and \$181,000, respectively, to interest expense.

#### Fair Value Measurements

The Company adopted SFAS No. 157, "Fair Value Measurements", in the first quarter of fiscal 2008. SFAS 157 was amended in February 2008 by the Financial Accounting Standards Board ("FASB") Staff Position ("FSP") FAS No. 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Its Related Interpretive Accounting Pronouncements That Address Leasing Transactions", and by FSP FAS 157-2, "Effective Date of FASB Statement No. 157", which delayed the Company's application of SFAS 157 for nonrecurring nonfinancial assets and liabilities until January 1, 2009. FAS 157 was further amended in October 2008 by FSP FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active", which clarifies the application of SFAS 157 to assets participating in inactive markets.

Implementation of SFAS 157 did not have a material effect on the Company's results of operations or financial position and had no effect on the Company's existing fair-value measurement practices. However, SFAS 157 requires disclosure of a fair-value hierarchy of inputs the Company uses to value an asset or a liability. The three levels of the fair-value hierarchy are described as follows:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities. For the Company, Level 1 inputs include quoted prices on the Company's securities that are actively traded.

Level 2: Inputs other than Level 1 that are observable, either directly or indirectly. For the Company, Level 2 inputs include assumptions such as estimated life, risk free rate and volatility estimates used in determining the fair values of the Company's option and warrant securities issued.

Level 3: Unobservable inputs for the asset or liability. Beginning January 1, 2009, Level 3 inputs may be required for the determination of fair value associated with certain nonrecurring measurements of nonfinancial assets and liabilities. The Company does not currently present any nonfinancial assets or liabilities at fair value.

Determining which category an asset or liability falls within the hierarchy requires significant judgment. The Company evaluates its hierarchy disclosures each quarter. Liabilities measured at fair value on a recurring basis are summarized as follows (unaudited):

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	Level 1	Level 2	Level 3	June 30, 2009
Fair value of derivative liability	—\$	—\$	4,080,953	\$ 4,080,953
Total	\$ —\$	—\$	4,080,953	\$ 4,080,953

The Company has no assets that are measured at fair value on a recurring basis. There were no assets or liabilities measured at fair value on a non-recurring basis during the six months ended June 30, 2009.

#### Accounting for Derivative Instruments

In connection with the issuance of certain convertible notes payable (see Note 3), the notes provided for a conversion into shares of the Company's common stock at a rate which was determined to be variable. The Company determined that the variable conversion feature was an embedded derivative instrument pursuant to SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. The accounting treatment of derivative financial instruments requires that the Company record the derivatives and related warrants at their fair values as of the inception date of the note agreements and at fair value as of each subsequent balance sheet date. In addition, under the provisions of Emerging Issues Task Force ("EITF") Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock," as a result of entering into the debenture agreements, the Company was required to classify all other non-employee options and warrants as derivative liabilities and record them at their fair values at each balance sheet date. Any change in fair value was recorded as non-operating, non-cash income or expense at each balance sheet date. If the fair value of the derivatives was higher at the subsequent balance sheet date, the Company recorded a non-operating, non-cash charge. If the fair value of the derivatives was lower at the subsequent balance sheet date, the Company recorded non-operating, non-cash income.

During the six months ended June 30, 2009 and 2008, the Company recognized other expense of \$1,575,903 and other income of \$2,588,416, respectively, related to recording the derivative liability at fair value. At June 30, 2009 and December 31, 2008, the derivative liability balance was \$4,080,953 and \$1,975,298, respectively.

Warrant-related and conversion-related derivatives were valued using the Black-Scholes Option Pricing Model with the following assumptions during the six months ended June 30, 2009 and 2008: dividend yield of 0%; volatility ranging from 178% to 670%(2009) and 160% to 187% (2008), respectively; and risk free interest rates ranging from 0.19% to 2.54% (2009) and 0.10% to 2.21% (2008).

The following table summarizes the activity related to the derivative liability during the six months ended June 30, 2009:

Derivative liability - December 31, 2008	\$ 2,025,298
Derivative liability added during the year	479,752
Change in fair value of derivative liability	1,575,903
Total derivative liability - June 30, 2009	\$ 4,080,953

#### Significant Recent Accounting Pronouncements

In June 2009, the FASB issued SFAS No. 168, The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles – a Replacement of FASB Statement No. 162 ("SFAS No. 168"). The Codification will become the source of authoritative U.S. GAAP. The statement is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Company expects to adopt this standard with the filing of its Quarterly Report on Form 10-Q for the period ended September 30, 2009 and does not expect the standard to have a material impact on the Company's consolidated financial statements.

In April 2009, the FASB issued FSP FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly ("FSP FAS 157-4"), which provides additional guidance for estimating fair value in accordance with Statement of Financial Accounting Standards No. 157, Fair Value Measurements, ("SFAS 157"). FSP FAS 157-4 states that a significant decrease in the volume and level of activity for the asset or liability when compared with normal market activity is an indication that transactions or quoted prices may not be determinative of fair value because there may be increased instances of transactions that are not orderly in such market conditions. The adoption of FSP FAS 157-4 did not have a material impact on the Company's consolidated financial position, results of operations or liquidity.

In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments ("FSP FAS 107-1 and APB 28-1"), which requires disclosures about the fair value of the Company's financial instruments for which it is practicable to estimate that value, whether recognized or not recognized in the balance sheets, in the interim reporting periods as well as in the annual reporting periods. In addition, FSP FAS 107-1 and APB 28-1 requires disclosures of the methods and significant assumptions used to estimate the fair value of those financial instruments. FSP FAS 107-1 and APB 28-1 became effective for the Company in its second quarter of fiscal 2009. The adoption of FSP FAS 107-1 and APB 28-1 did not have a material impact on the Company's consolidated financial position, results of operations or liquidity.

In April 2009, the FASB issued FSP FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments ("FSP FAS 115-2 and FAS 124-2"), which establishes a new method of recognizing and reporting other-than-temporary impairments of debt securities and requires additional disclosures related to debt and equity securities. FSP FAS 115-2 and FAS 124-2 does not change existing recognition and measurement guidance related to other-than-temporary impairments of equity securities. FSP FAS 115-2 and FAS 124-2 became effective for the Company in its second quarter of fiscal 2009. The adoption of FSP FAS 115-2 and FAS 124-2 did not have a material impact on the Company's consolidated financial position, results of operations or liquidity.



Other recent accounting pronouncements issued by the FASB (including the EITF) and the American Institute of Certified Public Accountants did not or are not believed by management to have a material impact on the Company's present or future consolidated financial statements.

## 2. CONTRACTS IN PROGRESS

Contracts in progress which include completed contracts not completely billed approximate the following as of June 30, 2009 and December 31, 2008:

	June 30, 2009	December 31, 2008
Cumulative costs to date	\$ 2,578,000	\$ 6,756,000
Cumulative gross profit to date	2,050,000	5,768,000
Cumulative revenue earned	4,628,000	12,524,000
Less progress billings to date	(4,651,000)	(13,495,000)
Net over billings	\$ (23,000)	\$ (971,000)

The following approximate amounts are included in the accompanying condensed consolidated balance sheets under these captions:

	June 30, 2009	December 31, 2008
Costs and estimated earnings in excess of billings on uncompleted contracts	\$ 61,000	\$ 417,000
Billings in excess of costs and estimated earnings on uncompleted contracts	(84,000)	(1,388,000)
Net over billings	\$ (23,000)	\$ (971,000)



## 3. CONVERTIBLE DEBT

## CAMOFI AND CAMHZN 12% AND 15% Senior Secured Convertible Debt

The Company's convertible debt financing, Amended 12% CAMOFI Convertible Note ("Amended 12% CAMOFI Note") and 15% CAMHZN Convertible Note ("15% CAMHZN Note"), are in default. The last monthly contractual payment on the CAMOFI note was made in October 2008 and no payments have made on the CAMHZN Note which were scheduled to begin on September 1, 2008. The Convertible Notes aggregate to \$3,897,213 principal and interest. As of June 30, 2009 and December 31, 2008, the principal balances, accrued interest and the debt discounts are presented in the table below.

CONV NOTES	June 30, 2009		December 31, 2008	
	CAMOFI	CAMHZN	CAMOFI	CAMHZN
Principal	\$ 2,827,281	\$ 750,000	\$ 2,827,281	\$ 750,000
Discount related to warrants liability	(81,340)	(33,541)	(119,369)	(48,890)
Discount related to convertible option liability	(1,301,502)	(205,994)	(1,909,996)	(301,200)
Discount related to stock issued with notes	(40,938)		(60,078)	
Notes presented net of debt discounts	\$ 1,403,501	\$ 510,465	\$ 737,838	\$ 399,910
Accrued Interest	\$ 226,182	\$ 93,750	\$ 56,546	\$ 37,500

During the three months ended June 30, 2009 and 2008, the Company amortized debt discounts of approximately \$751,000 and \$252,000, respectively, to interest expense related to the 12% and 15% Convertible Notes. During the six months ended June 30, 2009 and 2008, the Company amortized debt discounts of approximately \$776,000 and \$178,000, respectively, to interest expense related to the 12% and 15% Convertible Notes.

The Convertible Debt and Warrant Agreements include an anti-dilution feature and a buy-in clause which cause the embedded conversion option and the warrants to be treated as derivative liabilities which are valued on a quarterly basis and the resulting change in fair value of the derivative liabilities are recorded as a gain or loss upon valuation in the statement of operations.

In connection with the Amended 12% CAMOFI Note, the Company issued 725,000 five year warrants with an exercise price of \$0.10 per share and 725,000 five year warrants with an exercise price of \$0.20 per share. Due to the anti-dilution feature in the warrant agreements, the warrants have a reduced exercise price of \$0.07 and adjusted total warrants of 3,214,286 at June 30, 2009 and December 31, 2008. As of June 30, 2009 and December 31, 2008, the fair value of the warrant derivative liability was determined to be \$208,873 and \$151,400 respectively. Upon valuation, a gain of \$1,305 was recorded for the three months ended June 30, 2009. For the six months ended June 30, 2009, a total loss of \$57,473 was recorded.

In connection with the 15% CAMHZN Note, the Company issued 1,000,000 seven year warrants with an exercise price of \$0.07 per share. As of June 30, 2009 and December 31, 2008, the fair value of the warrant derivative liability was determined to be \$68,474 and \$50,000 respectively. Upon valuation, a loss of \$97 was recorded for the three months ended June 30, 2009. For the six months ended June 30, 2009, a total loss of \$18,474 was recorded.

The Amended 12% CAMOFI and 15% CAMHZN Notes are both convertible into shares of common stock at a conversion price of \$0.07 per share (subject to adjustment based on the anti-dilution feature). At June 30, 2009 and December 31, 2008, the aggregate fair value CAMOFI conversion option derivative liabilities was \$2,466,896 and \$1,515,634, respectively. Upon valuation, a gain of \$55,924 was recorded for the three months ended June 30, 2009. For the six months ended June 30, 2009, a total loss of \$951,262 was recorded. At June 30, 2009 and December 31,

2008, the aggregate fair value of the CAMHZN conversion option derivative liabilities was \$654,400 and \$308,264, respectively. Upon valuation, a gain of \$14,835 was recorded for the three months ended June 30, 2009. For the six months ended June 30, 2009, a loss of \$346,136 was recorded.

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#### CAMOFI AND CAMHZN Senior Secured Convertible Debt

On February 18, 2009, the Company entered into an agreement with CAMOFI Master LDC for the issuance of a Senior Secured Convertible Note for \$701,200, maturing on August 18, 2009. The Note can be converted at \$0.07 per share at any time during the term of the convertible note, subject to certain anti-dilution adjustments. The note is secured by all of the assets of the Company.

On February 18, 2009, the Company entered into an agreement with CAMHZN Master LDC for the issuance of a Senior Secured Convertible Note for \$173,800 maturing on August 18, 2009. The Note can be converted at \$0.07 per share at any time during the term of the convertible note, subject to certain anti-dilution adjustments.

The Notes are convertible into shares of common stock with a conversion price of \$0.07. Per FAS 133 "Accounting for Derivative Instruments and Hedging Activities", the conversion option is a derivative liability. The Company recorded at issuance a \$384,460 derivative liability for the CAMOFI Note, and a \$95,292 derivative liability for the CAMHZN Note. The conversion option liability is revalued each quarter. At June 30, 2009 the fair value was \$546,784 for the CAMOFI Note, and \$135,526 for CAMHZN Note. Upon valuation, a gain of \$122,696 and \$30,412, respectively, was recorded for the CAMOFI and CAMHZN notes for the three months ended June 30, 2009. For the six months ended June 30, 2009, a loss of \$162,324 and \$40,234, respectively, was recorded for the CAMOFI and CAMZHN notes.

The Company recorded deferred financing costs at issuance of \$116,200 on the CAMOFI Note and \$28,800 on the CAMHZN Note for the difference between the face amount of the notes and the net proceeds received. In addition, the discounts resulting from the conversion options of \$384,460 on the CAMOFI Note and \$95,292 on the CAMHZN Note are amortized into interest expense ratably over the life of the Notes. For the three months ended June 30, 2009, the Company recorded amortization expense on the conversion option and issuance costs of \$215,476 and \$74,985, respectively, on the CAMOFI Note and \$53,649 and 18,585, respectively, on the CAMHZN Note. For the six months ended June 30, 2009, the Company recorded amortization expense on the conversion option and issuance costs of \$288,421 and \$108,750, respectively, on the CAMOFI Note and \$71,396 and \$57,844, respectively, on the CAMHZN Note.

#### 4. EQUITY TRANSACTIONS

##### Equity Compensation

In February 2008, the Company entered into a year contract with a third party for public relations services valued at \$30,000. The fee was paid in the form of 150,000 shares of the Company's common stock based on the stock market price of the shares at the contract date. The value of the common stock on the date of the transaction was recorded as a deferred charge and is amortized to operating expense over the life of the agreement. Consulting fees under this contract of \$2,500 were amortized to expense during the three months ended June 30, 2008. Consulting fees under this contract of \$2,500 and \$5,000 were amortized to expense during the six months ended June 30, 2009 and June 30, 2008, respectively. As of June 30, 2009 the balance of deferred consulting fees was fully amortized.

In February 2008, the Company entered into a three month contract with a third party for public relations services valued at \$20,000. The fee was paid in the form of 100,000 shares of the Company's common stock based on the stock market price of the shares at the contract date. The value of the common stock on the date of the transaction was recorded as a deferred charge and is amortized to operating expense over the life of the agreement. Consulting fees under this contract of \$20,000 were amortized to expense during the six months ended June 30, 2008 and at June 30, 2008 the balance of deferred consulting fees was fully amortized.



In March 2008, the Company entered into a one month contract with a third party for public and financial communication services valued at \$25,000. The fee was paid in the form of 125,000 shares of the Company's common stock based on the stock market price of the shares at the contract date. The value of the common stock on the date of the transaction was recorded as a deferred charge and is amortized to operating expense over the life of the agreement. Consulting fees under this contract of \$25,000 were amortized to expense during the three and six months ended June 30, 2008 and at June 30, 2008 the balance of deferred consulting fees was fully amortized.

In June 2007, the Company entered into a three year contract with a third party for internet public investor relations services valued at \$210,000. The fee was paid in the form of 300,000 shares of the Company's common stock and valued based on the stock market price of the shares at the contract date. The value of the common stock on the date of the transaction was recorded as a deferred charge. \$18,000 was amortized to operating expense during the three months ended June 30, 2009 and 2008. \$35,000 was amortized to operating expense during the six months ended June 30, 2009 and 2008. At June 30, 2009 and December 31, 2008, the remaining deferred consulting fees totaled \$64,167 and \$101,667, respectively.

#### Dividends on preferred stock

The preferred shares Series C and preferred shares Series D shares have a mandatory cumulative dividend of \$1.25 per share, which is payable on a semi-annual basis in September and December each year to holders of record on November 30 and May 31. The preferred shareholders have certain liquidation preferences and do not have voting rights.

At June 30, 2009 and December 31, 2008, the Company had a total of 26,680 preferred shares Series C and 11,640 preferred shares Series D issued and outstanding. As of June 30, 2009 and December 31, 2008, the Company's accumulated dividends payable of \$500,550 and \$459,275, respectively. The Company declared dividends of \$41,275 during the three and six months ended June 30, 2009.

## 5. EARNINGS (LOSS) PER SHARE

The following is a reconciliation of the numerators and denominators of the basic and diluted earnings (loss) per share computations for the three and six months ended June 30, 2008:

	Three months ended June 30, 2008		
	Income (Loss)	Shares	Per Share Amount
Net income	\$ 438,349		
Less: Preferred stock dividends	(41,275)		
Basic income available to common shareholders	\$ 397,074	15,344,656	\$ 0.03
Add: Preferred dividends	41,275		
Add: Interest on convertible debt	148,382	-	
Add: Dilutive impact of convertible preferred stock	-	582,000	
Add: Dilutive impact of convertible debt	-	29,500,000	
Add: Dilutive impact of options and warrants	-	24,182	
Diluted income available to common shareholders	\$ 586,731	45,450,838	\$ 0.01
	Six months ended June 30, 2008		
	Income (Loss)	Shares	Per Share Amount
Net income	\$ 764,184		
Less: Preferred stock dividends	(41,275)		
Basic income available to common shareholders	\$ 722,909	15,344,656	\$ 0.05
Add: Preferred dividends	41,275		
Add: Interest on convertible debt	299,403	-	
Add: Dilutive impact of convertible preferred stock	-	582,000	
Add: Dilutive impact of convertible debt	-	29,500,000	
Add: Dilutive impact of options and warrants	-	2,343,000	
Diluted income available to common shareholders	\$ 1,063,587	47,769,656	\$ 0.02



The computation of diluted earnings per share does not assume conversion or exercise of securities that may have an anti-dilutive effect on earnings per share. Convertible preferred stock, convertible debt, stock options and warrants that have not been included in the diluted income per share computation totaled 76,073,976 for the period ended June 30, 2009.

## 6. RESTATEMENTS

June 30, 2008

The statement of operations and statement of cash flows for the three and six months ended June 30, 2008 included herein were restated to reflect the effect of changes to the original accounting for the CAMOFI Note issued in February 2006. The original accounting did not record the separate derivative for the conversion option and the warrants in accordance with FAS 133, "Accounting for Derivative Instruments and Hedging Activities" and EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled In, a Company's Own Stock".

The effect of these changes impacted the balance sheet and the statement of operations from February 2006 through December 31, 2008. The balance sheet effect is due to recording the conversion option and warrant liabilities and the effect on the statement of operations is due to the gains and losses from the quarterly fair value adjustments and an increase in interest expense. Accordingly, the statement of operations for the three and six months ended June 30, 2008 has been restated as summarized below:

Effect of Correction	As Previously Reported	Adjustment	As Restated
<b>Balance Sheet as of June 30, 2008</b>			
Conversion Option Liability	-	3,021,989	3,021,989
Warrant Liability	-	186,916	186,916
Accumulated Deficit	13,098,072	1,203,869	14,301,941
<b>Total Stockholders' Deficit (equity)</b>	<b>3,022,952</b>	<b>3,185,486</b>	<b>6,208,438</b>
<b>Statement of Operations for the three months ended June 30, 2008</b>			
Marked-to-Market Gain (Loss)	-	(515,057)	(515,057)
Net Income (Loss)	(849,305)	1,241,827	392,522
Net Income (Loss) Available to common shareholders	(890,580)	1,241,827	351,247
EPS - Basic	(0.06)	0.08	0.02
EPS - Diluted	(0.06)	0.08	0.02
<b>Statement of Operations for the six months ended June 30, 2008</b>			
Marked-to-Market Gain (Loss)	-	785,705	785,705
Net Income (Loss)	(1,824,232)	2,542,589	718,357
Net Income (Loss) Available to common shareholders	(1,865,507)	2,542,589	677,082
EPS - Basic	(0.13)	0.18	0.05
EPS - Diluted	(0.13)	0.18	0.05

March 31, 2009

The statement of operations and statement of cash flows for the three months ended June 30, 2009 included herein reflect the effect of changes to the original accounting for the CAMOFI and CAMZHN notes issued in February 2009, certain adjustments related to the Company's contract accounting, a misclassification error and for the valuation of the related derivative liabilities at March 31, 2009.





The effect of these changes impacted the balance sheet and the statement of operations from January 1, 2009 through March 31, 2009. The balance sheet effect is due to adjusting the conversion option discount that was originally recorded on the CAMOFI and CAMZHN notes issued in February 2009, the valuation of the related derivative liabilities certain adjustments related to the Company's contract accounting, a misclassification error and for the valuation of the related derivative liabilities at March 31, 2009 and the valuation of the derivative liabilities associated with the 12% CAMOFI and 15% CAMZHN notes. The effect on the statement of operations is due to the gains and losses from the revised quarterly fair value adjustments and an increase in interest expense from the increased amortization expense related to the adjustment of the conversion option discounts that were recorded on the CAMOFI and CAMZHN notes issued in February 2009. Accordingly, the effect of the restatements on the balance sheet at March 31, 2009 and statement of operations for the three months ended March 31, 2009 has been summarized below:

Effect of Correction	As Previously Reported	Adjustment	As Restated
<b>Balance Sheet as of March 31, 2009</b>			
(1) Costs in Excess of Billings	15,551	86,477	102,028
(2) Deferred financing costs	435,986	108,750	544,736
(3) Billings in Excess of Costs	823,478	(216,417)	607,061
(4) February 2009 Convertible Notes	464,984	49,798	514,782
(5) Derivative Liability	4,885,000	(578,972)	4,306,028
(6) Accumulated Deficit	16,701,824	(1,040,414)	15,661,410
<b>Statement of Operations for the three months ended March 31, 2009</b>			
(7) Sales	1,298,458	(243,756)	1,054,702
(8) Cost of sales	1,365,543	(546,650)	818,893
(9) Marked-to-Market Gain (Loss)	(2,738,436)	937,458	(1,800,978)
(10) Interest expense	(490,408)	(199,938)	(632,145)
(11) Net Loss	(3,821,869)	1,040,414	(2,781,455)
Net Loss Available to common shareholders	(3,821,869)	1,040,414	(2,781,455)
EPS – Basic	(0.25)	0.07	(0.18)
EPS - Diluted	(0.25)	0.07	(0.18)

- (1) Adjustment in order to reconcile the Company's balance sheet account to the Company's contract accounting worksheets.
  - (2) Represents the reclassification of \$145,000 of financing costs in connection with the February 2009 notes, less amortization of \$36,250.
  - (3) Adjustment in order to reconcile the Company's balance sheet account to the Company's contract accounting worksheets.
  - (4) Adjustment reflects an increase of \$278,486 of debt discount related to the valuation of the conversion options and an increase of \$119,938 of amortization of such options, net of reclassification of financing costs of \$108,750 noted in (1) above.
  - (5) Adjustment reflects an increase of \$278,486 related to the valuation of the conversion options of the February 2009 notes and a decrease in the loss on fair value of \$937,458 and corrections of \$80,000 of misclassifications between the change in fair value and interest expense.
  - (6) \_\_\_\_\_ and (11) The cumulative effect of adjustments (7) through (11).
  - (7) and (8) Adjustment in order to reconcile the Company's P&L accounts to the Company's contract accounting worksheets.
  - (9) Adjustment reflects an increase of \$278,466 in the valuation of the conversion options in connection with the February 2009 notes, a decrease in the valuation of all derivatives of \$578, 972 and a decrease in the loss on fair value of \$937,458.
  - (10) \_\_\_\_\_ See (2) and (4) above.
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## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the Company's condensed consolidated financial statements and the notes thereto appearing elsewhere in this Form 10-Q. Certain statements contained herein that are not related to historical results, including, without limitation, statements regarding the Company's business strategy and objectives, future financial position, expectations about pending litigation and estimated cost savings, are forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended (the "Securities Exchange Act") and involve risks and uncertainties. Although the Company believes that the assumptions on which these forward-looking statements are based are reasonable, there can be no assurance that such assumptions will prove to be accurate and actual results could differ materially from those discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, regulatory policies, and market and general policies, competition from other similar businesses, and market and general economic factors. All forward-looking statements contained in this Form 10-Q are qualified in their entirety by this statement.

### OVERVIEW

The Company is engaged in acquiring, re-manufacturing and selling pre-owned Computer Numerically Controlled ("CNC") machine tools to manufacturing customers. The Company provides rebuilt, retrofit and remanufacturing services for numerous brands of machine tools. The remanufacturing of a machine tool, typically consisting of replacing all components, realigning the machine, adding updated CNC capability and electrical and mechanical enhancements, generally takes two to four months to complete. Once completed, a remanufactured machine is a "like new," state-of-the-art machine with a price ranging from \$275,000 to \$1,000,000, which is substantially less than the price of an equivalent new machine. The Company also manufactures original equipment CNC large turning lathes and attachments under the trade name Century Turn.

CNC machines use commands from onboard computers to control the movements of cutting tools and rotation speeds of the parts being produced. Computer controls enable operators to program operations such as part rotation, tooling selection and tooling movement for specific parts and then store the programs in memory for future use. The machines are able to produce parts while left unattended. Because of this ability, as well as superior speed of operation, a CNC machine is able to produce the same amount of work as several manually controlled machines, as well as reduce the number of operators required; generating higher profits with less re-work and scrap. Since the introduction of CNC tooling machines, continual advances in computer control technology have allowed for easier programming and additional machine capabilities.

A vertical turning machine permits the production of larger, heavier and more oddly shaped parts on a machine, which uses less floor space when compared to the traditional horizontal turning machine because the spindle and cam are aligned on a vertical plane, with the spindle on the bottom.

The primary industry segments in which the Company's machines are utilized to make component parts are in aerospace, power generation turbines, military, component parts for the energy sector for natural gas and oil exploration and medical fields. The Company sells its products to customers located in United States, Canada and Mexico.

Over the last four years, the Company has designed and developed a large horizontal CNC turning lathe with productivity features new to the metalworking industry. The Company believes that a potential market for the Century Turn Lathe, in addition to the markets mentioned above, is aircraft landing gear.

We provide our manufactured and remanufactured machines as part of the machine tool industry. The machine tool industry worldwide is approximately a \$30 billion business annually. The industry is sensitive to market conditions and generally trends downward prior to poor economic conditions, and improves prior to an improvement in economic conditions.

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Our machines are utilized in a wide variety of industry segments as follows: aerospace, energy, valves, fittings, oil and gas, machinery and equipment, and transportation. With the recent downturn in the aerospace industry, we have seen an increase in orders from new industries such as defense and medical industries.

The Company's current strategy is to expand its customer sales base with its present line of machine products. The Company's growth strategy also includes strategic acquisitions in addition to growing the current business. Plans for expansion are funded through current working capital from ongoing sales. A significant acquisition will require additional financing.

**RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED JUNE 30, 2009 COMPARED TO JUNE 30, 2008.**

**Revenues.** The Company generated revenues of \$1,359,630 for the three months ended June 30, 2009, which was a \$75,046 or 5% decrease from \$1,434,676 for the three months ended June 30, 2008. The decrease is the result of lower than usual sales and a tighter credit market.

**Gross Profit.** Gross profit for the three months ended June 30, 2009, was \$165,900 or 12% of revenues, compared to \$71,062 or 5% of revenues for the three months ended June 30, 2008, a 133% increase. The increase in gross profit is due to management strategy to lower cost of sales through reduction of overhead expenses and cost of materials.

**Operating Expenses.** The Company incurred total operating expenses of \$296,534 for the three months ended June 30, 2009, which was a \$130,028 or 30% decrease from \$426,562 for the three months ended June 30, 2008. In the three months ended June 30, 2009, compared with the three months ended June 30, 2008, all the operating expenses increased (decreased) as follow:

	Increase/(Decrease) %
Consulting and other compensation	4
Salaries and related	13
Selling, general and administrative	(51)

The increase in salaries and related costs is due to the reclassification of certain costs to compensation. Selling, general and administrative expenses decreased due to management strategy to reduce operating expenses.

**Operating Loss.** Operating loss for the three months ended June 30, 2009, was \$130,634 compared to an operating loss of \$355,500 for the three months ended June 30, 2008. The decrease in loss of \$224,866 is primarily due to decreased cost of sales and decreased selling, general and administrative expenses for the quarter ended June 30, 2009.

**Interest Expense and Debt Discount Amortization.** Interest expense for the three months ended June 30, 2009, was \$952,461 compared with \$497,382 for the three months ended June 30, 2008. The increase of \$455,079, or 91%, in interest expenses is due to additional interest on new convertible loans.

**Change in Fair Value of Derivative Liabilities.** In connection with its convertible notes, the Company recorded conversion options and warrant derivative liabilities. The derivative liabilities are reevaluated each reporting period. During the three months ended June 30, 2009, we recorded a gain of \$225,075 on the change in fair value due to the decrease in our stock price from March 31, 2009.



RESULTS OF OPERATIONS FOR THE SIX MONTHS ENDED JUNE 30, 2009 COMPARED TO JUNE 30, 2008.

**Revenues.** The Company generated revenues of \$2,414,332 for the six months ended June 30, 2009, which was a \$546,946 or 18% decrease from \$2,961,278 for the six months ended June 30, 2008. The decrease is the result of lower than usual sales and a tighter credit market.

**Gross Profit.** Gross profit for the six months ended June 30, 2009, was 401,709 or 17% of revenues, compared to \$289,185 or 10% of revenues for the six months ended June 30, 2008.

**Operating Expenses.** The Company incurred total operating expenses of \$744,257 for the six months ended June 30, 2009, which was a \$445,214 or 37% decrease from \$1,189,471 for the six months ended June 30, 2008. In the six months ended June 30, 2009, compared with the six months ended June 30, 2008, all the operating expenses increased (decreased) as follows:

	Increase/(Decrease) %
Consulting and other compensation	(60)
Salaries and related	85
Selling, general and administrative	(49)

The decrease in consulting and other compensation is due to the reduction in the number of consulting contracts and the expiration of the existing contracts. The increase in salaries and related costs is due to the reclassification of certain costs to compensation. Selling, general and administrative expenses decreased due to management strategy to reduce operating expenses.

**Operating Loss.** Operating loss for the six months ended June 30, 2009, was \$342,548 compared to \$900,286 for the six months ended June 30, 2008. The decrease in loss of \$557,738 or 62% is primarily due to decreased consulting and other compensation expenses and selling, general and administrative expenses.

**Interest Expense and Debt Discount Amortization.** Interest expense for the six months ended June 30, 2009, was \$1,620,856 compared with \$984,151 for the six months ended June 30, 2008. The increase of \$636,705 in interest expenses is due to additional interest on new convertible loans.

**Change in Fair Value of Derivative Liabilities.** In connection with its convertible notes, the Company recorded conversion options and warrant derivative liabilities. The derivative liabilities are reevaluated each reporting period. During the six months ended June 30, 2009, we recorded a loss on the change in fair value of derivative liabilities due to the increase in our stock price during the period, in addition to recording \$479,752 of additional derivatives during the period.

FINANCIAL CONDITION, LIQUIDITY, CAPITAL RESOURCES

The net decrease in cash during the six months ended June 30, 2009 was \$31,889.

For the six months ended June 30, 2009, the cash provided by financing activities was \$745,592, compared with \$30,844 in the six months ended June 30, 2008. For the six months ended June 30, 2009, \$777,481 cash was used by operating activities.





## GOING CONCERN

The accompanying condensed consolidated financial statements have been prepared assuming the Company will continue as a going concern, which contemplates, among other things, the realization of assets and satisfaction of liabilities in the normal course of business. The Company has an accumulated deficit of approximately \$16,455,000, a net loss of approximately \$3,534,000, a working capital deficit of approximately \$8,108,000 and was also in default on two of its convertible notes. These factors raise substantial doubt about the Company's ability to continue as a going concern. The Company intends to fund operations through anticipated increased sales along with renegotiated or new debt and equity financing arrangements which management believes may be insufficient to fund its capital expenditures, working capital and other cash requirements for the year ending December 31, 2009. Therefore, the Company will be required to seek additional funds to finance its long-term operations. The successful outcome of future activities cannot be determined at this time and there is no assurance that if achieved, the Company will have sufficient funds to execute its intended business plan or generate positive operating results.

In response to these problems, management has taken the following actions:

- The Company continues its aggressive program for selling machines.
- The Company continues to implement plans to further reduce operating costs.
- The Company is seeking investment capital through the public and private markets.
- The Company is seeking strategic acquisition candidates

The condensed consolidated financial statements do not include any adjustments related to recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

## INFLATION AND CHANGING PRICES

The Company does not foresee any adverse effects on its earnings as a result of inflation or changing prices.

## CRITICAL ACCOUNTING POLICIES

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America requires management to make judgments, assumptions and estimates that affect the amounts reported in our consolidated financial statements and the accompanying notes. The amounts of assets and liabilities reported on our balance sheet and the amounts of revenues and expenses reported for each of our fiscal periods are affected by estimates and assumptions, which are used for, but not limited to, the accounting for revenue recognition, accounts receivable, doubtful accounts and inventories. Actual results could differ from these estimates. The accounting policies stated below are significantly affected by judgments, assumptions and estimates used in the preparation of the financial statements:

### Revenue Recognition

Service revenues are billed and recognized in the period the services are rendered.

The Company accounts for shipping and handling fees and costs in accordance with EITF 00-10 "Accounting for Shipping and Handling Fees and Costs." Such fees and costs incurred by the Company are recorded to cost of goods sold and are immaterial to the operations of the Company.

In accordance with SFAS 48, "Revenue Recognition when Right of Return Exists," revenue is recorded net of an estimate of markdowns, price concessions and warranty costs. Such reserve is based on management's evaluation of

historical experience, current industry trends and estimated costs.

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In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin 101 ("SAB 101"), "Revenue Recognition," as amended by SAB No. 104 which outlines the basic criteria that must be met to recognize revenue and provides guidance for presentation of revenue and for disclosure related to revenue recognition policies in financial statements filed with the Securities and Exchange Commission. Management believes that the Company's revenue recognition policy for services and product sales conforms to SAB 101 amended by SAB 104. The Company recognizes revenue of long-term contracts pursuant to SOP 81-1.

#### Method of Accounting for Long-Term Contracts

The Company uses the percentage-of-completion method of accounting to account for long-term contracts and, therefore, takes into account the cost, estimated earnings and revenue to date on fixed-fee contracts not yet completed. The percentage-of-completion method is used because management considers total cost to be the best available measure of progress on the contracts. Because of inherent uncertainties in estimating costs, it is at least reasonably possible that the estimates used will change within the near term.

The amount of revenue recognized at the statement date is the portion of the total contract price that the cost expended to date bears to the anticipated final cost, based on current estimates of cost to complete. It is not related to the progress billings to customers. Contract costs include all materials, direct labor, machinery, subcontract costs and allocations of indirect overhead.

Because long-term contracts may extend over a period of time, changes in job performance, changes in job conditions and revisions of estimates of cost and earnings during the course of the work are reflected in the accounting period in which the facts that require the revision become known. At the time a loss on a contract becomes known, the entire amount of the estimated ultimate loss is recognized in the consolidated financial statements.

Contracts that are substantially complete are considered closed for consolidated financial statement purposes. Revenue earned on contracts in progress in excess of billings (under billings) is classified as a current asset. Amounts billed in excess of revenue earned (over billings) are classified as a current liability. Inventories are stated at the lower of cost or net realizable value. Cost is determined under the first-in, first-out method. Inventories represent cost of work in process on units not yet under contract. Cost includes all direct material and labor, machinery, subcontractors and allocations of indirect overhead.

#### Other Significant Accounting Policies

Other significant accounting policies not involving the same level of measurement uncertainties as those discussed above, are nevertheless important to an understanding of the financial statements. The policies related to consolidation and loss contingencies require difficult judgments on complex matters that are often subject to multiple sources of authoritative guidance. Certain of these matters are among topics currently under reexamination by accounting standards setters and regulators. Although no specific conclusions reached by these standards setters appear likely to cause a material change in our accounting policies, outcomes cannot be predicted with confidence. Also see Note 1 of Notes to Condensed Consolidated Financial Statements, Summary of Significant Accounting Policies, which discusses accounting policies that must be selected by management when there are acceptable alternatives.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.



## ITEM 4. CONTROLS AND PROCEDURES

### Evaluation of Disclosure Controls and Procedures

We conducted an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer, who is also our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended (“Exchange Act”), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures also include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. Based on this evaluation, our Chief Executive Officer concluded as of June 30, 2009 that our disclosure controls and procedures were not effective at the reasonable assurance level due to the material weaknesses discussed immediately below.

### Material Weaknesses

(1) We had not effectively implemented comprehensive entity-level internal controls, as evidenced by the following deficiencies:

We did not establish an independent Audit Committee who are responsible for the oversight of the financial reporting process, nor was an Audit Committee Charter defined. At the current time we do not have any independent members of the Board who could comprise this committee.

We did not establish an adequate Whistle Blower program for the receipt, retention, and treatment of complaints received by the issuer regarding accounting, internal accounting controls, or auditing matters; and the confidential, anonymous submission by employees of the issuer of concerns regarding questionable accounting or auditing matters to the Audit Committee and Board of Directors.

We did not have an individual on our Board, nor on the Audit Committee, who meets the “Financial Expert” criteria.

We did not maintain documentation evidencing quarterly or other meetings between the Board, senior financial managers and our outside general counsel. Such meetings include reviewing and approving quarterly and annual filings with the Securities and Exchange Commission and reviewing on-going activities to determine if there are any potential audit related issues which may warrant involvement and follow-up action by the Board.

We did not follow a formal fraud assessment process to identify and design adequate internal controls to mitigate those risks not deemed to be acceptable.

We did not conduct annual performance reviews or evaluations of our management and staff employees.

(2) We did not have a sufficient complement of personnel with appropriate training and experience in GAAP, as evidenced by the following deficiencies:

We do not have a formally trained Chief Financial Officer who is responsible for the oversight of the accounting function. Currently the CEO is responsible for this function, but has not had formal accounting or auditing

experience.

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The Accountant is the only individual with technical accounting experience in our company but is limited in the exposure to SEC filings and disclosures.

We have not consulted with other outside parties with accounting experience to assist us in the SEC filings and disclosures prior to the December 31, 2008 10-K filing during 2009.

(3) We did not adequately segregate the duties of different personnel within our accounting group due to an insufficient complement of staff and inadequate management oversight.

(4) We did not adequately design internal controls as follows:

- The controls identified in the process documentation were not designed effectively and had no evidence of operating effectiveness for testing purposes.
- The controls identified in the process documentation did not cover all the risks for the specific process
- The controls identified in the process documentation did not cover all applicable assertions for the significant accounts.

(5) Due to the material weaknesses identified at our entity level we did not test whether our financial activity level controls or our information technology general controls were operating sufficiently to identify a deficiency, or combination of deficiencies, that may result in a reasonable possibility that a material misstatement of the financial statements would not be prevented or detected on a timely basis.

#### CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no significant changes in the Company's internal control over financial reporting during the Company's most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Inherent limitations exist in any system of internal control including the possibility of human error and the potential of overriding controls. Even effective internal controls can provide only reasonable assurance with respect to financial statement preparation. The effectiveness of an internal control system may also be affected by changes in conditions.



PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

Starting October 2008, the Company has been in default with all monthly payments on the 12% CAMOFI and 15% CAMHZN Convertible Note payable. As of June 30, 2009, the Company's default principal and interest aggregate to \$1,100,000.

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

None.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit 31.1 Certification required by Rule 13a-14(a) or Rule 15d-14(d) and under Section 302 of the Sarbanes-Oxley act of 2002

Exhibit 32.1 Certification required by Rule 13a-14(a) or Rule 15d-14(d) and under Section 906 of the Sarbanes-Oxley act of 2002

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the Company caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

August 14, 2009

NEW CENTURY COMPANIES, INC.

/s/ DAVID DUQUETTE

Name: David Duquette

Title: Chairman, President and Director

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated.

August 14, 2009

/s/ DAVID DUQUETTE

Name: David Duquette

Title: Chairman, President and Director

August 14, 2009

/s/ JOSEF CZIKMANTORI

Name: Josef Czikmantor

Title: Secretary and Director