ION NETWORKS INC
Form 10KSB/A
August 21, 2002

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB/A

Amendment No. 3

[X] ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended March 31, 2002

OR

[_] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____________ to ____________

Commission File No.: 0-13117

ION NETWORKS, INC.
(Name of Small Business Issuer in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	22-2413505 (IRS Employer Identification Number)
1551 South Washington Avenue, Piscataway (Address of Principal Executive Offices)	08854 (Zip Code)

Issuer's telephone number, including area code: (732) 529-0100

Securities registered under Section 12(b) of the Exchange Act: None

Securities registered under Section 12(g) of the Exchange Act: Common Stock, $.001 par value

[X] 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.

[_] Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

The issuer's revenues for its most recent fiscal year totaled $7,312,235.

The aggregate market value of voting stock held by non-affiliates, based on the closing price of the Common Stock, par value $0.001 (the "Common Stock") on June 19, 2002 of $0.40, as reported on the NASDAQ National Market was approximately $6,701,419. Shares of Common Stock held by each officer and director and by each

person who owns 5% or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for any other purpose.

There were 25,138,001 shares of Common Stock outstanding as of June 19, 2002.

DOCUMENTS INCORPORATED BY REFERENCE: None.

Information Regarding Forward-Looking Statements

A number of statements contained in this report are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties that could cause actual results to differ materially from those expressed or implied in the applicable statements. These risks and uncertainties include, but are not limited to, the recent introduction and the costs associated with, a new family of products; dependence on the acceptance of this new family of products; uncertainty as to the acceptance of the Company's products generally; risks related to technological factors; potential manufacturing difficulties; uncertainty of product development; uncertainty of adequate financing; dependence on third parties; dependence on key personnel; competition; a limited customer base; risk of system failure, security risks and liability risks; risk of requirements to comply with government regulations; vulnerability to rapid industry change and technological obsolescence; and general economic conditions. In some cases, you can identify forward-looking statements by our use of words such as "may," "will," "should," "could," "expects," "plans," "intends," "anticipates," "believes," "estimates," "predicts," "potential," or "continue" or the negative or other variations of these words, or other comparable words or phrases. Unless otherwise required by applicable securities laws, the Company assumes no obligation to update any such forward-looking statements, or to update the reasons why actual results could differ from those projected in the forward-looking statements.

PART I

Item 1: Description of Business

Overview

ION Networks, Inc ("ION" or the "Company") designs, develops, manufactures and sells infrastructure security and management products to corporations, service providers and government agencies. The Company's hardware and software products are designed to form a secure auditable portal to protect IT and network infrastructure from internal and external security threats. ION's infrastructure security solution operates in the IP, data center, telecommunications and transport, and telephony environments and is sold by a direct sales force and indirect channel partners mainly throughout North America and Europe.

As organizations become more interconnected and dependent on networks such as the Internet, they are increasingly being exposed to a widening range of cyber-threats. These attacks occur despite the wide spread deployment of information security technologies, suggesting that it is not sufficient to only protect the electronic perimeter of an organization. With the most damaging security breaches increasingly appearing within the boundaries of organizations, Infrastructure Security has become one of the newest components of electronic security strategies. Infrastructure Security focuses on protecting the critical infrastructure devices that support the transfer, storage, and processing of business applications and information. Infrastructure security also provides a method by which the tools used to manage these devices, and the administrators

who keep these devices running smoothly, are protected against the threat of attack from the outside.

The ION Secure /TM/ product suite provides ION customers with comprehensive infrastructure security including secure access, authentication, authorization, audit and administrative functions that we believe form a highly scalable, robust, reliable, easy-to-use and cost-effective secure management portal. ION solutions include ION Secure PRIISMS centralized management software, 3000 and 5000 series security appliances, and 500 series security tokens. These solutions are based on ION proprietary software and hardware developed and maintained by the Company. ION infrastructure security solutions use the same single-purpose embedded ION Secure Operating System (ISOS) software on all security appliance models, with the goal of simplifying the management of thousands of IT and telecommunications infrastructure devices such as servers, routers, LAN switches, PBXs, messaging systems and multiplexers. ION solutions are designed to enable administrators to securely configure, troubleshoot and manage geographically dispersed infrastructure devices from central operations centers, reducing costly on-site visits, service disruptions and skilled personnel requirements. ION infrastructure security solutions can be used in a variety of networks including TCP/IP-data, PBX-telephony, telecommunications and data centers ranging in size from one to thousands of infrastructure devices. ION solutions are designed to be fully compatible with information security solutions offered by, among others, Cisco, Checkpoint and Nortel Networks.

ION's infrastructure security solutions are distributed via three distinct channels: (i) a direct sales force, (ii) indirect channels, such as Value Added Resellers (VARs) and (iii) Original Equipment Manufacturers (OEMs). Services revenue is typically generated from integration and maintenance services in conjunction with the sale of ION solutions. As of March 31, 2002, ION has sold more than 40,000 infrastructure security appliances worldwide.

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ION Networks, Inc. is a Delaware corporation founded in 1999 through the combination of two companies, MicroFrame, Inc. (originally founded in 1982), a New Jersey corporation and SolCom Systems Limited (originally founded in 1994), a Scottish corporation located in Livingston, Scotland. In 1999, the Company expanded its technology base through the purchase of certain assets of LeeMAH DataCom Securities Corporation. References in this document to "we," "our," "us," and "the Company" refer to ION Networks, Inc. Our principal executive offices are located at 1551 South Washington Avenue, Piscataway, New Jersey 08854, and our telephone number is (732) 529-0100.

Industry Background

Pervasive Use of Corporate Security to Protect Employees and Business Assets

ION believes that a key factor to the long-term success and competitive advantage of any business is its ability to protect its people and assets from all types of security threats. Many businesses have implemented some type of corporate security strategy that physically protects employees and business assets from outsiders who may seek to harm individuals, steal proprietary information, or disrupt the operations of an organization.

Wide Acceptance of Information Security to Protect Business Applications and Information

As organizations become more interconnected and dependent on networks such as the Internet, they are increasingly being exposed to a widening range of cyber-threats -- threats that we believe transcend the need for physical access

in order to cause damage to a business. We believe that computer crime is projected to grow by an estimated 230% in 2002, based on estimates from publications by research firms that analyze IT security and related costs. To counter these cyber-threats, organizations are seeking to secure corporate user access, business applications and information with information security strategies designed to protect the electronic doorways into an organization. Increasingly, businesses are deploying information security solutions that protect against outsiders -- people such as hackers without any legitimate access -- through the use of security tokens for user authentication, intrusion detection systems to identify attackers and firewalls to restrict remote access to corporate networks and systems.

Growing Impact of Insider Security Threats

While outsider threats present a significant challenge to organizations, the Computer Security Institute and the FBI have reported that outsiders account for fewer than half of the reported information security incidents in the United States, although the number of such incidents continues to rise. These reports estimated the average cost of successful attacks by outsiders to be $56,000. By contrast, the average cost of malicious acts by insiders was estimated to be $2.7 million. Interestingly, these attacks occurred despite the wide spread deployment of information security technologies, suggesting that simply protecting the electronic perimeter of an organization has not slowed the pace of real losses from security threats.

Increasing Need to Protect the "Electronic Interior" of Businesses -- Infrastructure Security

According to a survey by the American Society for Industrial Security (ASIS) and Price Waterhouse Coopers, the majority of serious security breaches occur at the hands of people with some degree of legitimate access, ranging from current employees to former employees, customers, and contractors. Much of the focus on information security solutions has revolved around policing the general user population. We believe that the users with the greatest potential to cause harm are IT administrators themselves, because they know where the most critical information is kept and how to bypass safeguards. Administrators (and intruders who gain administrator privileges) likely have the access, authorization and knowledge necessary to cause significant damage to any organization.

We believe that there is a growing trend of outsourcing IT professionals for services that are not core to a business, thereby creating an ever-changing climate where organizations know less and less about the backgrounds and intentions of their IT administrators. Therefore, organizations are increasingly exposed to potentially significant financial and productivity losses unless the most empowered users and access to administrative functions are adequately restricted and monitored. Information security strategies cannot be effective unless administrative services are protected through the implementation of infrastructure security strategies that safeguard infrastructure devices such as servers, routers, LAN switches, PBXs, messaging systems and multiplexers.

We believe that many of today's most damaging security threats are appearing within the boundaries of organizations, forcing organizations to extend their security protection inward from the perimeter. Infrastructure Security, a new component in the electronic security domain, focuses on protecting the critical infrastructure devices that support the transfer, storage, and processing of business applications and information.

We estimate the number of potentially vulnerable infrastructure devices

that may require protection by an infrastructure security solution across our addressable markets to be in excess of 100 million worldwide. This largely untapped need to protect infrastructure devices provides ION with what we estimate to be a significant market opportunity.

The ION Networks Solution

The ION infrastructure security solution consists of ION Secure PRIISMS software and ION Secure 3000 and 5000 series appliances for centralized security policy management and distributed security policy enforcement. Together, PRIISMS centralized management software and the security appliances form a secure management portal to critical infrastructure devices. ION solutions also provide a variety of management features for improving administrator productivity and mediating alarms from these infrastructure devices. ION has refined its infrastructure security solution by adding custom features specific to a wide range of infrastructure devices. ION Secure 3000 and 5000 series security appliances also support management of discrete alarms for the physical environment surrounding infrastructure devices such as doors, lighting, air conditioners or diesel generators and monitoring environmental conditions including temperature, humidity, fire and water conditions.

The ION Secure product suite is intended to provide our customers with the following key benefits:

A Complete Infrastructure Security Solution. We believe ION offers one of the most complete, commercially available solutions in our industry for securely managing infrastructure devices. We have taken a broad approach to infrastructure security and developed a product suite that protects administrative services with one unified solution by providing secure:

.. Access -- ION solutions are designed so that administrators can only gain access to infrastructure devices through the network connectivity provided by ION Secure PRIISMS software and ION Secure 3000 and 5000 series security appliances that together form a secure management portal. PRIISMS provides a single point of entry into the secure management portal for administrators utilizing Secure Shell (SSH), Point-to-Point Tunneling Protocol (PPTP) and Telnet. Access to PRIISMS is only granted based on strong multi-factor authentication of administrators. PRIISMS servers are typically colocated in Network Operations Centers along with enterprise management and operational support systems. ION Secure 3000 and/or 5000 series security appliances are deployed throughout an organization's network to protect against unauthorized access to infrastructure devices. ION Secure PRIISMS software and ION Secure 3000 and 5000 series security appliances provide infrastructure access protection by forcing all administrative traffic through a secure management network using one or both of the following methods: (i) TCP/IP based Virtual Private Networks (IP-VPNs) with firewall services and encrypted VPN IPSec tunnels and (ii) Virtual Private Dial-up Networks (VPDNs) over public switched telephone networks.

.. Authentication -- ION infrastructure security solutions combine strong multi-factor authentication with "single sign-on" to the secure management portal. Administrative sessions require the use of ION hardware or software security tokens that use two-factor authentication. PRIISMS provides a single sign-on environment for all administrative applications. Single sign-on means that administrators need only log into PRIISMS once to easily gain secure access to the infrastructure devices they are tasked with managing. ION 3000 and 5000 series security appliances support the same strong authentication mechanisms as PRIISMS. Whether connecting through an IP-VPN or VPDN, multi-factor authentication is required for administrators to communicate with every ION security appliance. Private key management services are integrated into ION infrastructure security solutions in order

to ease deployment of PRIISMS and security appliances.

.. Authorization -- ION infrastructure security solutions provide extensive security policy management capabilities for controlling administrator actions. Policies are centrally managed via ION Secure PRIISMS software at the user or group level with distributed policy enforcement handled by the 3000 and 5000 series security appliances. ION Secure PRIISMS multi-level authorization restricts administrator access to specific infrastructure devices, as well as prohibits the issuing of specific commands. Multi-level authorization services are intended to provide tight control over the specific commands that can be issued by administrators via command filtering.

.. Audit -- ION Secure PRIISMS software and 3000 and 5000 series security appliances are designed to maintain detailed audit trails on administrator activities, infrastructure devices and security appliance health. ION security appliances maintain extensive logs on administrative sessions including administrator authentication success, failure and connection histories. The entire history of each administrative session can be captured down to the characters entered by an administrator. Command filters can be utilized to restrict which commands an administrator may enter to control an infrastructure device. ION security appliance logs are protected from tampering and can maintain the history of administrative sessions.

.. Administration -- ION Secure PRIISMS software provides directory services for assigning authentication methods and privileges to users and groups and the logical partitioning of authorized infrastructure device views. Once authenticated into PRIISMS, administrators can only see and manage assigned infrastructure devices. In addition, centralized management of ION security appliances via PRIISMS simplifies the installation, configuration and upgrade of the ION Secure Operating System (ISOS) on remote ION security appliancesThe ION Secure 3000 and 5000 series appliances provide a wide range of management services such as alarm mediation, remote diagnostics, and task automation. In addition, messages from non-standard managed infrastructure devices can be converted to Simple Network Management Protocol (SNMP) traps and sent to PRIISMS for centralized viewing and forwarding to third party enterprise management and operational support systems. Network and port-level diagnostic utilities can also be used by administrators to remotely troubleshoot infrastructure devices. The automation of administrative tasks can be implemented both in PRIISMS and ION security appliances. Action triggers can be set for automating common tasks such as event notification via SNMP trap, pager or e-mail, the power recycling of infrastructure devices, or the uploading of logs from ION security appliances. ION security appliances also provide a native scripting (computer programming) language and task scheduler that can run these scripts based on an alarm, date or time for custom automation requirements.

Low Total Cost of Ownership. The ION solution is designed to minimize the purchase, installation and maintenance costs of infrastructure security. The list prices for our infrastructure security appliances currently begin at $3,125 and scale up with products and features that address a wide array of customer requirements. Many studies have shown that the complex systems integration of multiple security products is a significant component of the total cost of implementing security solutions. We believe that our cost-effective, integrated solution, consisting of easy-to-manage security appliances and management software, enables customers to avoid the expense of costly systems integration

that may otherwise be required to implement and maintain an effective infrastructure security solution.

Rapid Return on Investment. ION solutions help protect against the growing threat of security breaches that can result in among other losses, significant financial losses and legal liabilities, lost productivity, poor network availability, brand defamation, and theft of proprietary information. ION solutions enable customers to centrally perform administrative functions that otherwise may require a dispatch of an administrator to a remote location. Fewer service calls reduce the need for having costly technical personnel on staff.

Ease of Installation and Use. The ION Secure product family delivers plug-and-play appliances designed for easy installation and use. Installation involves simply connecting an ION security appliance to the network, and providing nothing more than a network address. Appliances can be remotely configured through ION PRIISMS centralized management software, including software upgrades and configuration of new software features.

ION Networks Products and Services

ION Networks provides a complete infrastructure security solution that includes secure access, authentication, authorization, audit and administration functions that form a secure management portal for managing infrastructure devices. The ION Secure infrastructure security solution is based on centralized security policy management and distributed security policy enforcement. It consists of centralized ION Secure PRIISMS software and distributed ION Secure 3000 and 5000 series security appliances forming a secure management network. We also provide training, consulting and support services to our customers and distribution partners.

ION Secure PRIISMS Centralized Management Software. PRIISMS provides centralized, 24x7 surveillance and provisioning across the entire suite of ION Secure 3000 and 5000 security appliances, resulting in the simplified management of thousands of infrastructure devices. Through its web-based user interface, PRIISMS enables administrators to configure, troubleshoot and manage geographically dispersed critical infrastructure devices from central operations centers, thereby reducing the cost and time required for remote appliance maintenance, security administration, data collection and reporting. Key features include:

.. Global View With Single Sign-on: Proactively monitor ION security appliances from central network operations centers. Administrators can securely log into PRIISMS once instead of logging into each individual appliance.

.. Multi-factor Authentication: Utilize a number of security measures to protect infrastructure devices, including the ability to lock out a specific administrator across the network in seconds. This feature requires the use of ION Secure tokens.

.. Centralized Alarm Notification and Logging: Simultaneously view alarms and events within PRIISMS for ION security appliances and infrastructure devices.

.. Centralized Provisioning and Job Scheduling: Centrally manage the scheduling of jobs for managing configuration files

and software updates.

.. Automatic Backups: Automatically back up configuration files for all ION security appliances on the network to PRIISMS servers.

.. Real-time Inventory and Status: Track system health to ensure that ION security appliances and infrastructure devices are running properly 24 x 7.

.. Multi-level Authorization: Use security policies to enforce strict control over administrators' actions when accessing infrastructure devices.

ION Secure 3000 Series. The ION Secure 3100, 3200 and 3300 security appliances provide advanced security measures and combine console, alarm and sensor management functions into a single centrally manageable solution. With support for up to 28 console ports, up to 80 contact closures, 1 LAN Ethernet interface and 2 WAN interfaces in a single platform, the 3000 series protects user access and control for a wide variety of infrastructure devices requiring out-of-band or VPDN access.

ION Secure 5000 Series. The ION Secure 5010 supports the same ISOS features as the 3000 series, providing support for 4 console ports, 1 external IP router interface, 3 internal LAN Ethernet interfaces, and 2 WAN interfaces. It has an integral VPN router to securely carry administrative traffic through an intranet or a public network via IP-VPN connectivity. It also includes advanced security measures and combines console, alarm and sensor management functions in a single centrally manageable solution.

ION Secure 500 Series Tokens. ION Secure 510 hardware and 520 software security tokens are as simple to use as entering a password, but much more secure. Each user is assigned an ION Secure token that generates a new, unpredictable pass code every time a user desires to request remote access to ION PRIISMS. ION Secure authentication requires very few steps and authorized users are positively identified within seconds. Employees, business partners and customers can use ION Secure tokens whether local, remote or mobile.

Wide Range of Protected Infrastructure Devices

ION infrastructure security solutions protect a growing variety of infrastructure devices provided by leading IT and telecommunications network and system vendors, including vendors of:

.. Access Servers
.. Application Servers
.. Bus & Tag Channel Extenders
.. Call Management Systems
.. Carrier Grade Multi-Service Switches
.. Cellular Switches
.. CSU/DSUs
.. DSLAMs
.. Integrated Access Devices
.. LAN Switches
.. Mail Servers
.. Messaging Servers

. Multi-Service Switches
. Optical Switches
. PBXs (Switched & IP)
. Power Protection Systems (UPS)
. Routers
. SONET Switches
. SS7 Switches
. Storage Area Networks
. Terminal Servers
. Various Types of PC Class Servers
. Various Types of UNIX Class Server
. Wireless Switches

Strategy

Our goal is to extend our market position to remain one of the industry leaders for infrastructure security solutions for service providers, corporations and government agencies. Key elements of our strategy include:

Extend Our Market Position in Infrastructure Security. We believe that we are establishing a growing market position as a provider of infrastructure security solutions designed for our target markets by offering an integrated, robust, reliable, easy-to-use suite of products at attractive prices. We intend to continue to focus our product development efforts, distribution strategies and marketing programs to satisfy the growing needs of these markets. We believe that many of the current infrastructure security offerings of other vendors are expensive, incomplete, technically complex and generally unable to satisfy these target markets.

Develop New Products and Reduce Manufacturing Costs. We intend to use our product design and development expertise to expand our product offerings and reduce our manufacturing costs. We believe that new product offerings and associated cost reductions will strengthen our market position and assist us in penetrating new markets.

Establish the ION Networks Brand. We believe that strong brand recognition in our target markets is important to our long-term success. We intend to continue to strengthen our ION NetworksTM and ION SecureTM brand names through industry trade shows, our web site, advertising, direct mailings to both our resellers and our end-users, and public relations. The continued development of our reputation as a comprehensive, reliable, easy-to-use and cost effective infrastructure security vendor will contribute to our sales efforts.

Expand Our Direct Channel. We intend to continue to build and expand our base of direct relationships with customers through additional marketing programs and increased targeted advertising.

Expand Our Indirect Channels. Our distribution channels are currently in place to serve ION target markets. We have begun to penetrate these markets by partnering with value-added resellers who sell our solutions in seven countries. We intend to continue to build and expand our base of indirect channel relationships through additional marketing programs and increased targeted advertising.

Expand Strategic Original Equipment Manufacturer Relationships. By entering into original equipment manufacturer ("OEM") arrangements to sell our products, we intend to build upon the brand awareness and worldwide channels of major networking and telecommunications equipment suppliers to further penetrate our target markets.

Customers

125 customers purchased ION Secure solutions in fiscal year ended March 31, 2002 and our products are now deployed in over 10,000 locations. As of March 31, 2002, ION has sold more than 40,000 infrastructure security appliances. Historically, our largest customers have been service providers primarily in the United States and in Europe. See also Risk Factors, "We rely on several key customers for a significant portion of our business, the loss of which would likely significantly decrease our revenues" on page 12. However, over the last two quarters we have begun to diversify away from our traditional customer base and continue to introduce products that lend themselves to the evolving needs of an expanding number of markets. ION has begun to penetrate the corporate market and, in particular, the financial services sector including institutions such as Wells Fargo, Fortis Bank of Belgium and others. We believe our recent success in the financial services sector is evidence of the flexibility of ION Secure solutions.

ION customers can be categorized based on three market segments: Corporations, Service Providers and Government Agencies:

Corporations. The Corporate market consists of non-governmental organizations that do not provide goods or services from a network infrastructure, but rather use their network infrastructure as a platform to provide their own goods or services. There are many sectors in the corporate market, including, but not limited to, banking, financial services, insurance, energy, manufacturing, retailers, pharmaceuticals, healthcare, technology and transportation. Representative ION customers in the corporate market for the fiscal year ended March 31, 2002 include: AIG, First National Bank of Omaha, Chicago Stock Exchange, Chubb Financial Services, Coca Cola Enterprises, Deutsche Bank, Entergy, Ericcson, Wachovia, Florida Power and Light, Fortis Bank, Intel, Kaiser Permanente, MayoClinic, Neuberger Berman, Nortel, Oracle, and Wells Fargo.

Service Providers. The service provider market consists of businesses that use their network infrastructure to provide services to their customers, including specific sectors such as (i) transport service providers that provide voice, data, and long-distance transport of telephone and data services, including ILECs, CLECs, long-distance carriers, cable telephony, and optical network providers; (ii) managed service providers that provide network infrastructure, managed services, and managed network services, including Internet Data Centers, ISPs and ASPs; (iii) broadband service providers that provide wire line-based broadband services to residential and business customers. Broadband services include DSL, CATV, cable modems, VoD (Voice over Data) and VoIP (Voice over IP) services; and (iv) wireless service providers that provide wireless voice and data services. This includes mobile/cellular, wireless data, satellite, and wireless LAN services. Representative ION customers in the service provider market for the fiscal year ended March 31, 2002 include: BT, Cablevision, GTI, KPN and Verizon.

Government Agencies. The Government market consists of governmental agencies that do not provide services from a network infrastructure, but rather use their network infrastructure as a platform to provide their own goods and services. There are many sectors in the government market, including, but not limited to, federal and national agencies, military, state agencies, local agencies, police departments, fire departments, and emergency services. Representative ION customers in the government market for the fiscal year ended March 31, 2002 include various domestic and foreign government agencies.

Sales and Marketing

Our sales and marketing efforts focus on successfully penetrating the corporate, service provider and government agency markets. Our marketing programs promote ION Networks and ION Secure brand awareness and reputation as a highly scalable, robust, reliable, easy-to-use and cost-effective infrastructure security solution. We try to strengthen our brand through a variety of marketing programs which include on-going public relations, our web site, advertising, direct mail, industry and regional trade shows and seminars. We intend to continue expanding and strengthening our direct and indirect channel relationships through additional marketing programs, additional marketing staff and increased promotional activities.

Direct Sales. On March 31, 2002, the Company's sales force stood at 17. In fiscal year ended March 31, 2002, ION had over 125 customers with products located at more than 10,000 locations worldwide. We believe that ION solutions are ideally suited for both direct sale to customers and indirect channels where

it is not economically efficient for us to sell directly to the end users of our products. In the fiscal year ended March 31, 2002, approximately 67% of ION revenue came from direct sales.

Indirect Sales/Channel Partners. We also market and sell our solutions via indirect channels through a distribution structure of Value Added Resellers (VARs) or Channel Partners in the United States and in Europe. VARs accounted for approximately 21% of our total revenue for the fiscal year ended March 31, 2002. Our VAR agreements are non-exclusive. Representative U.S. and international indirect channel partners include: Siemens (U.S.), Bomara (U.S.), SafeLink (Sweden), TrueCom (Netherlands), Systeam (Germany), CreaNORD (Finland), Elexo (France).

We support our international distributors by offering customizable marketing materials, sales tools, leads, co-operative marketing funds, joint advertising, discounted demonstration units and training. We also participate in regional press tours, trade shows and seminars. International distributors include TrueCom in the Netherlands, Elexo in France and CreaNORD in Finland.

Original Equipment Manufacturers (OEMs). We enter into select original equipment manufacturer relationships in order to take advantage of the channels of well-established companies that sell into our target markets. We believe these channels expand our overall market while having a minor impact on our own indirect channel sales. The terms of our agreements with these customers are variable and can generally be cancelled under certain conditions. In the fiscal year ended March 31, 2002, our original equipment manufacturer revenue accounted for approximately 12% of total revenue.

Geographic Distribution. We divide our sales organization regionally into two territories: the United States and Canada; and Europe, the Middle East and Africa. Regional sales representatives manage our relationships with our network of channel partners, sell to and support key customer accounts, and act as a liaison between our indirect channels and our marketing organization. We also have an internal sales staff that supports the indirect channel, and a dedicated business development organization whose primary responsibilities are identifying, promoting and managing strategic relationships to sell our solutions with industry leaders and original equipment manufacturers.

Approximately 72% of ION's sales were in the United States and 28% elsewhere for the fiscal year ended March 31, 2002. (Refer to Note 12 in the Company's Consolidated Financial Statements.)

Customer Service and Technical Support

We offer our customers a comprehensive range of support services under the ION SecureCare brand that includes electronic support, product maintenance and personalized technical support services on a worldwide basis. Our technical support staff is located in Piscataway, New Jersey with field representatives located around the world.

Our ION SecureCare offering includes ION 24x7 support. This support offering provides replacement for failing hardware, telephone and/or web-based technical support and software updates. Incentive programs are offered to ION SecureCare customers to provide added benefits for upgrading to newer products.

Competition

The market for infrastructure security solutions is worldwide and highly competitive, and we expect competition to intensify in the future. Competitors can be generally categorized as either: (i) information security vendors who provide high performance, security point products, or (ii) suppliers of network management appliances that provide limited infrastructure security features.

Many of these solutions require additional security products in order to implement a comprehensive infrastructure security solution. Current and potential competitors in our markets include, but are not limited to the following companies, all of which sell worldwide or have a presence in most of the major markets for such products:

- Security software vendors such as RSA Security, Check Point Software and Symantec;

- Network equipment manufacturers such as Cisco, Lucent Technologies, Nortel Networks;
- Computer or network component manufacturers such as Intel;
- Operating system software vendors such as Microsoft, Novell and Sun Microsystems;
- Security appliance suppliers such as SonicWall and NetScreen Technologies; and
- Low cost management-only appliance vendors, which may include limited infrastructure security functionality.

Many of our competitors have generally targeted large organizations' information security needs with VPN, firewall and 3A (Authorization, Authentication and Audit) products that range in price from under one thousand to hundreds of thousands of dollars. These offerings may increase competitive pressure on some of our solutions, resulting in both lower prices and gross margins. Many of our current or potential competitors have longer operating histories, greater name recognition, larger customer bases and significantly greater financial, technical, marketing and other resources than we do. Nothing prevents or hinders these actual or potential competitors from entering our target markets at any time. In addition, our competitors may bundle products competitive to ours with other products that they may sell to our current or potential customers. These customers may accept these bundled products rather than separately purchasing our products. If these companies were to use their greater financial, technical and marketing resources in our target markets, it could adversely affect our business.

Sources And Availability Of Materials

The Company designs its security appliances utilizing readily available parts manufactured by multiple suppliers and relies on and intends to continue to rely on these suppliers. Our principal suppliers are XeTel Corporation, Da-Tech Corporation and Youngtron. The Company has been and expects to continue to be able to obtain the parts required to manufacture its products without any significant interruption or sudden price increase, although there can be no assurance that it will be able to continue to do so.

The Company sometimes utilizes a component available from only one supplier. If a supplier were to cease to supply this component, the Company would most likely have to redesign a feature of the affected device. In these situations, the Company maintains a greater supply of the component on hand in order to allow the time necessary to effect a redesign or alternative course of action should the need arise.

Dependence On Particular Customers

Historically, the Company has been dependent on several large customers each year, but they are not necessarily the same every year. In general, the Company cannot predict with certainty, which large customers will continue to order. The loss of any of these large customers, or the failure to attract new large customers, could have a material adverse effect on the Company's business.

Intellectual Property, Licenses And Labor Contracts

The Company holds no patents on its technology. Although it licenses some of its technology from third parties, the Company does not consider any of these licenses to be critical to its operation.

The Company has made a consistent effort to minimize the ability of competitors to duplicate the software technology utilized in its solutions. However, the possibility of duplication of its products remains, and competing products have already been introduced.

Governmental Approvals And Effect Of Governmental Regulation

The Company's solutions may be exported to any country in the world except those countries restricted by the anti-terrorism controls imposed by the Department of Commerce. These anti-terrorism controls prohibit the Company from exporting some of its solutions to Cuba, Libya, Iran, Iraq, North Korea, Sudan and Syria without a license. As with all U.S. origin items, the Company's solutions are also subject to the Bureau of Export Administration's ten general prohibitions that restrict exports to certain countries, organizations, and persons.

As required by law or demanded by customer contract, the Company obtains approval of its solutions by Underwriters' Laboratories. Additionally, because many of the products interface with telecommunications networks, the Company's products

are subject to several key Federal Communications Commission ("FCC") rules requiring FCC approval.

Part 68 of the FCC rules contains the majority of the technical requirements with which telephone systems must comply in order to qualify for FCC registration for interconnection to the public telephone network. Part 68 registration requires telecommunication equipment interfacing with the public telephone network to comply with certain interference parameters and other technical specifications. FCC Part 68 registration for ION's products has been granted, and the Company intends to apply for FCC Part 68 registration for all of its new and future products.

Part 15 of the FCC rules requires equipment classified as containing a Class A computing device to meet certain radio and television interference requirements, especially as they relate to operation of such equipment in a residential area. Certain of ION's products are subject to and comply with Part 15.

The European Community has developed a similar set of requirements for its members and the Company has begun the compliance process for its products in Europe. Additionally, ION has certified certain of its products to the NEBS (Network Equipment Business Specification) level of certification. This is a certification that was developed by Bellcore (now Telcordia Technologies) and is required by many of ION's telecommunications customers.

Research And Development Activities

The Company believes the current R&D staff of 10 employees will be sufficient to allow it to keep up with technology advances for the foreseeable future.

The current staff has successfully completed and released the new ION Secure 5010 security appliance and related PRIISMS and ISOS software releases. This product provides ION Networks with the ability to address a more diverse IP based network market due to its ability to provide connectivity across secure IP tunnels by utilizing integrated VPN router technology.

As a result of the changes implemented in the last fiscal year, research and development spending was reduced from $2,126,246 in FY2001 to $891,542 in FY2002.

Employees

As of June 19, 2002, the Company had 59 employees, all of whom are full-time employees, and of which 13 are technical personnel, 31 are in sales, marketing and support, 4 are in production, and 11 are in executive, financial and administrative capacities. None of the Company's employees are represented by labor unions. The Company considers its relations with its employees to be satisfactory.

Risk Factors

We are vulnerable to technological changes, which may cause our products and services to become obsolete which could materially and negatively impact our cash flow.

Our industry experiences rapid technological change, changing customer requirements, frequent new product introductions and evolving industry standards that may render existing products and services obsolete. As a result, more advanced products produced by competitors could erode our position in existing markets or other markets that they choose to enter. It is difficult to estimate the life cycles of our products and services, and future success will depend, in part, upon our ability to enhance existing products and services and to develop new products and services on a timely basis. We might experience difficulties that could delay or prevent the successful development, introduction and marketing of new products and services. New products and services and enhancements might not meet the requirements of the marketplace and achieve market acceptance. If these things happen, they would materially and negatively affect cash flow, financial condition and the results of operations.

Hardware and software incorporated in our products may experience bugs or "errors" which could delay the commercial introduction of our products and require time and money to alleviate.

Due to the complex and sophisticated hardware and software that is incorporated in our products, our products have in the past experienced errors or "bugs" both during development and subsequent to commercial introduction. We cannot be certain that all potential problems will be identified, that any bugs that are located can be corrected on a timely basis or at all, or that additional errors will not be located in existing or future products at a later time or when usage increases. Any such errors could delay the commercial introduction of new products, the use of existing or new products, or require modifications in systems that have already been installed. Remedying such errors could be costly and time consuming. Delays in debugging or modifying

products could materially and adversely affect our competitive position.

There is potential for fluctuation in our quarterly and annual operating results, which could cause the price of our Common Stock to significantly decrease.

In the past, we experienced fluctuations in our quarterly and annual operating results and we anticipate that such fluctuations will continue. Our quarterly and annual operating results may vary significantly depending on a number of factors, including:

.. the timing of the introduction or acceptance of new products and services;

.. changes in the mix of products and services provided;

.. long sales cycles;

.. changes in regulations affecting our business;

.. increases in the amount of research and development expenditures necessary for new product development and innovation;

.. changes in our operating expenses;

.. uneven revenue streams; and

.. general economic conditions.

We cannot assure you that our levels of profitability will not vary significantly among quarterly periods or that in future quarterly periods our results of operations will not be below prior results or the expectations of public market analysts and investors. If this occurs, the price of our common stock could significantly decrease. See also Risks Associated with Our Securities, "There is potential for fluctuation in the market price of our securities" page 13.

In the past we have experienced significant losses and negative cash flows from operations. If these trends continue in the future, it could adversely affect our financial condition.

We have incurred significant losses and negative cash flows from operations in the past. For the fiscal years ended March 31, 2001 and 2002, we experienced net losses of $16,676,666 and $6,929,379, respectively, and negative cash flows from operations of $7,086,246 and $5,026,038, respectively. These results have had a negative impact on our financial condition. There can be no assurance that our business will become profitable in the future and that additional losses and negative cash flows from operations will not be incurred. If these trends continue in the future, it could have a material adverse affect on our financial condition.

If our expected revenues and assumptions are not met, we may need to raise additional capital, which may not be available. If we fail to raise additional capital, we may not be able to execute our business plan and growth strategy.

Our business plan and growth strategy are dependent on our working capital. To the extent that expected revenue assumptions are not achieved, we will have to raise additional equity or debt financing and/or curtail certain expenditures contained in the current operating plans. We can not assure that our sales efforts or expense reduction programs will be successful, or that additional financing will be available to us, or, if available, that the terms will be

satisfactory to us. If we are not successful in increasing our revenue, reducing our expenses or raising additional equity capital, to generate sufficient cash flows to meet our obligations as they come due, our financial condition and results of operations may be materially and adversely affected.

We face significant competition and if we do not compete successfully, our results of operations may be adversely affected.

We are subject to significant competition from different sources for our different products and services. We can not assure you that the market will continue to accept our hardware and software technology or that we will be able to compete successfully in the future. We believe that the main factors affecting competition in the network management business are:

.. the products' ability to meet various network management and security requirements;

.. the products' ability to conform to the network and/or computer systems;

.. the products' ability to avoid becoming technologically outdated;

.. the willingness and the ability of distributors to provide support customization, training and installation; and

.. the price.

Although we believe that our present products and services are competitive, we compete with a number of large data networking, network security and enterprise management manufacturers which have financial, research and development, marketing and technical resources far greater than ours. Our competitors include RSA Security, Check Point Software, Symantec, Cisco, Lucent Technologies, Nortel Networks, Intel, Microsoft, Novell, and Sun Microsystems. Such companies may succeed in producing and distributing competitive products more effectively than we can produce and distribute our products, and may also develop new products which compete effectively with our products. Many of our current or potential competitors have longer operating histories, greater name recognition, larger customer bases and significantly greater financial, technical, marketing and other resources than we do. Nothing prevents or hinders these actual or potential competitors from entering our target markets at any time. In addition, our competitors may bundle products competitive to ours with other products that they may sell to our current or potential customers. These customers may accept these bundled products rather than separately purchasing our products. If our current or potential competitors were to use their greater financial, technical and marketing resources in our target markets and if we are unable to compete successfully, our business, financial condition and results of operations may be materially and adversely affected.

We have recently changed our marketing position, and introduced a new product which we expect to account for a significant portion of our revenues. If this product is not accepted by the market, our revenues and results of operations could be materially adversely affected.

We recently changed our marketing position and focus from that of network management monitoring to that of network security. In connection with this change, we introduced a new product, the ION Secure 5010 in early February 2002. To date, we have only sold limited amounts of this new product and have not yet achieved marketplace acceptance. While we still generate revenues from our previously existing products, our continued revenue growth depends largely on

the success of our new marketing position and product offerings. Therefore, if the ION Secure 5010 does not gain marketplace acceptance, our revenues could be negatively impacted, which in turn is likely to materially and adversely affect our business, financial condition and results of operations.

We may be unable to protect our proprietary rights, permitting competitors to duplicate our products and services, which could negatively impact our business and operations.

We hold no patents on any of our technology. If we are unable to license any technology or products that we may need in the future, our business and operations may be materially and adversely impacted. However, we do not consider any of these licenses to be critical to our operations. We have made a consistent effort to minimize the ability of competitors to duplicate our software technology utilized in our products. However, there remains the possibility of duplication of our products, and competing products have already been introduced. Any such duplication by our competitors could negatively impact on our business and operations.

We rely on several key customers for a significant portion of our business, the loss of which would likely significantly decrease our revenues.

Historically, we have been dependent on several large customers each year, but they are not necessarily the same every year. For the fiscal year ended March 31, 2002, our most significant customers were AT&T (approximately 15% of revenues), Avaya (approximately 12% of revenues), SBC (approximately 12% of revenues), Nortel (approximately 10% of revenues), and Siemens (approximately 6% of revenues). For the fiscal year ended March 31, 2001, our most significant customers were SBC (16% of revenues), Worldcom (12% of revenues), Rhythms (8% of revenues), Celestica (6% of revenues), and KPN (5% of revenues). In general, we cannot predict with certainty which large customers will continue to order. The loss of any of these large customers, or the failure to attract new large customers would likely significantly decrease our revenues and future prospects, which could materially and adversely affect our business, financial condition and results of operations.

All of our key customers are telecommunications companies. If the telecommunications industry continues to experience significant economic downturn, our sales could be adversely impacted.

A significant portion of our revenues is generated from sales of our products and services to various telecommunications

companies. During the last twelve to eighteen months, the telecommunications industry has endured a significant economic downturn. Telecommunications service providers have typically reduced planned capital spending, have reduced staff, and sought bankruptcy proceedings and/or ceased operations. Consequently, the spending cutback of these organizations has affected the Company through reduced product orders. The decline in product orders negatively impacted our revenues, resulting in significant operating losses and negative cash flows. If the telecommunications industry experiences further economic downturns, this could negatively impact our sales and revenue generation, and consequently have a material adverse effect on our business, financial condition and results of operations.

We depend upon key members of our employees and management, the loss of which could have a material adverse effect upon our business, financial condition and results of operations.

Our business is greatly dependent on the efforts of our President and CEO, Mr. Kam Saifi, our Chief Operating Officer, Mr. Cameron Saifi, our Chief Technology Officer, Mr. David Arbeitel and our Chief Financial Officer, Mr. Ted Kaminer and other key employees, and on our ability to attract key personnel. Other than with respect to Messrs. K. Saifi, C. Saifi, Arbeitel and Kaminer, we do not have employment agreements with our other key employees. Our success depends in large part on the continued services of our key management, sales, engineering, research and development and operational personnel and on our ability to continue to attract, motivate and retain highly qualified employees and independent contractors in those areas. Competition for such personnel is intense and we cannot assure you that we will successfully attract, motivate and retain key personnel. While all of our employees have entered into non-compete agreements, there can be no assurance that any employee will remain with us. Our inability to hire and retain qualified personnel or the loss of the services of our key personnel could have a material adverse effect upon our business, financial condition and results of operations. Currently, we do not maintain "key man" insurance policies with respect to any of our employees.

We rely on several contract manufacturers to supply our products. If our product manufacturers fail to deliver our products, or if we lose these suppliers, we may be unable to deliver our product and our sales and revenues could be negatively impacted.

We rely on three contract manufacturers to supply our products. If these manufacturers fail to deliver our products or if we lose these suppliers and are unable to replace them, then we would not be able to deliver our products to our customers. This could negatively impact our sales and revenues and have a material adverse affect on our business, financial condition and results of operations.

Our corporate charter and bylaws contain limitations on the liability of our directors and officers, which may discourage suits against directors and executive officers for breaches of fiduciary duties.

Our Certificate of Incorporation, as amended, and our Bylaws contain provisions limiting the liability of our directors for monetary damages to the fullest extent permissible under Delaware law. This is intended to eliminate the personal liability of a director for monetary damages on an action brought by or in our right for breach of a director's duties to us or to our stockholders except in certain limited circumstances. In addition, our Certificate of Incorporation, as amended, and our Bylaws contain provisions requiring us to indemnify our directors, officers, employees and agents serving at our request, against expenses, judgments (including derivative actions), fines and amounts paid in settlement. This indemnification is limited to actions taken in good faith in the reasonable belief that the conduct was lawful and in, or not opposed to our best interests. The Certificate of Incorporation and the Bylaws provide for the indemnification of directors and officers in connection with civil, criminal, administrative or investigative proceedings when acting in their capacities as agents for us. These provisions may reduce the likelihood of derivative litigation against directors and executive officers and may discourage or deter stockholders or management from suing directors or executive officers for breaches of their fiduciary duties, even though such an action, if successful, might otherwise benefit us and our stockholders.

RISKS ASSOCIATED WITH OUR SECURITIES

We do not anticipate the payment of dividends.

We have never declared or paid cash dividends on our common stock. We currently anticipate that we will retain all available funds for use in the operation of our business. Thus, we do not anticipate paying any cash dividends

on our common stock in the foreseeable future.

There is potential for fluctuation in the market price of our securities.

Because of the nature of the industry in which we operate, the market price of our securities has been, and can be expected to continue to be, highly volatile. Factors such as announcements by us or others of technological innovations, new commercial products, regulatory approvals or proprietary rights developments, and competitive developments all may have a

significant impact on our future business prospects and market price of our securities.

Shares that are eligible for sale in the future may affect the market price of our common stock.

As of June 19, 2002, an aggregate of 2,499,122 of the outstanding shares of our common stock are "restricted securities" as that term is defined in Rule 144 of the Securities Act of 1933 (Rule 144). These restricted shares may be sold pursuant only to an effective registration statement under the securities laws or in compliance with the exemption provisions of Rule 144 or other securities law provisions. In addition, 2,682,548 shares are issuable pursuant to currently exercisable options, and 1,624,250 shares are issuable pursuant to currently exercisable warrants, including 1,120,000 of the shares registered hereby, which may be exercised for shares that may be restricted or registered, further adding to the number of outstanding shares. Future sales of substantial amounts of shares in the public market, or the perception that such sales could occur, could negatively affect the price of our common stock.

Our common stock may be delisted from Nasdaq.

The National Association of Securities Dealers, Inc. has established certain standards for the continued listing of a security on the Nasdaq National Market and the Nasdaq SmallCap Market. The standards for continued listing on either market require, among other things, that the minimum bid price for the listed securities be at least $1.00 per share. A deficiency in the bid price maintenance standard will be deemed to exist if the issuer fails the stated requirement for thirty consecutive trading days, with a 90-day cure period, with respect to the Nasdaq National Market, and a 180-day cure period with respect to the Nasdaq SmallCap Market. Our Common Stock has traded below $1.00 since January 29, 2002, and on March 13, 2002, we received notice from Nasdaq stating that our Common Stock has not met the $1.00 continuing listing standard for a period of 30 consecutive trading days. While our Common Stock continues to be traded on the Nasdaq National Market, we have applied (within 90 days of the date of deficiency notice) for a transfer to the Nasdaq SmallCap Market in order to take advantage of the longer 180-day cure period. If we chose to transfer to the Nasdaq SmallCap Market and the price deficiency is cured during the 180-day period, and we otherwise continue to comply with the Nasdaq National Market maintenance standards, we could then transfer back to the Nasdaq National Market. There can be no assurance that we will satisfy the requirements for maintaining a Nasdaq National Market or SmallCap listing. If our common stock were to be excluded from Nasdaq, the prices of our common stock and the ability of holders to sell such stock would be adversely affected, and we would be required to comply with the initial listing requirements to be relisted on Nasdaq.

Item 2: Description of Property

The Company leases 26,247 square feet of space at 1551 South Washington Avenue, Piscataway, New Jersey, for its principal executive offices. This lease, which commenced on February 18, 1999, is for a term of ten (10) years with monthly rent payable by us to the landlord as follows: $555,911 for the first two years of the term; $595,291 for the next year of the term; $601,843 for the next year of the term; $654,337 for the next year of the term; $610,242 for the next two years of the term; and $662,736 for the remaining three years of the term. In accordance with the lease, the Company is also obligated to make additional payments to the landlord relating to certain taxes and operating expenses.

The Company also leases 245 square meters of office space in Antwerp, Belgium for its European operating headquarters. This lease provides for a monthly rental of (euro)2,832 per month as of March 31, 2002 and expires on July 31, 2005.

In addition, the Company leases 0.298 hectare of space at SolCom House, Meikle Road, Kirkton Campus, Livingston EH547DE, Scotland. This lease provides for monthly rentals of (pound)3,583 and expires on August 31, 2011.

The Company also leases approximately 5,600 square feet of space at 48834 Kato Road, Fremont, California in the Bedford Fremont Business Center. This lease commenced on June 1, 1999 and is for a term of 60 months with monthly rent payable by the Company to the landlord as follows: $7,360 per month for the first 12 months of the term; $7,590 per month for months 13-24; $7,820 per month for months 25-36; $8,050 per month for months 37-48; and $8,280 per month for months 49-60.

Item 3: Legal Proceedings

There are no material pending legal proceedings to which the Company is a party or to which any of its properties are subject.

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

The Company did not submit any matters to a vote of the security holders during the fourth quarter of fiscal year ended March 31, 2002.

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PART II

Item 5: Market For Common Equity and Related Stockholder Matters

Market Information

The Company's common stock, par value $.001 per share (the "Common Stock"), is listed on the NASDAQ National Market under the symbol "IONN". The following table sets forth the high ask and low bid prices of the Common Stock for the periods indicated as reported on the NASDAQ National Market.

Fiscal Year 2002, Quarter Ending	HIGH	LOW
June 30, 2001	$ 1.15	$0.57
September 30, 2001	0.79	0.16
December 31, 2001	0.85	0.08
March 31, 2002	1.84	0.65

Fiscal Year 2001, Quarter Ending

June 30, 2000	$31.00	$2.00
September 30, 2000	5.94	2.00
December 31, 2000	3.06	0.28
March 31, 2001	3.00	0.38

Recent Sales of Unregistered Securities

On February 14, 2002, the Company issued an aggregate of 4,000,000 shares of Common Stock at a price of $0.87 per share, for an aggregate total consideration of $3,480,000. The shares were issued to a group of accredited investors pursuant to Rule 506 promulgated under the Securities Act of 1933.

Security Holders

As of June 19, 2002 there were 391 holders of record of the Common Stock (not including beneficial owners of Common Stock held by brokers in street name).

Dividends

The Company has not paid any cash dividends on its Common Stock during the two fiscal years ended March 31, 2002 and March 31, 2001. The Company presently intends to retain all earnings to finance its operations and therefore does not presently anticipate paying any cash dividends in the foreseeable future.

Item 6: Management's Discussion and Analysis or Plan of Operation

Overview

ION Networks, Inc. (the "Company"), designs, develops, manufactures and sells infrastructure security and management products to corporations, service providers and government agencies. The Company's hardware and software products are designed to form a secure auditable portal to protect IT and network infrastructure from internal and external security threats. ION's products operate in the IP, data center, telecommunications and transport, and telephony environments and are sold by a direct sales force and indirect channel partners mainly throughout North America and Europe.

The Company is a Delaware corporation founded in 1999 through the combination of two companies - MicroFrame ("MicroFrame"), a New Jersey Corporation (the predecessor entity to the Company, originally founded in 1982), and SolCom Systems Limited ("SolCom"), a Scottish corporation located in Livingston, Scotland (originally founded in 1994). From the time of the merger in 1999 through the third quarter of fiscal 2002, the Company's principal objective was to address the need for security based network management solutions, primarily for the PBX-based telecommunications market, resulting in a significant portion of our revenues being generated from sales to various telecommunications companies. During the last twelve to eighteen months, the telecommunications industry has endured a significant economic downturn. Telecommunications service providers have typically reduced planned capital spending, have reduced staff, and sought bankruptcy proceedings and/or ceased operations. Consequently, the spending cutback of the organizations has affected the Company through reduced product orders.

The decline in product orders negatively impacted our revenues, resulting in

significant operating losses and negative cash flows. As a result, it is imperative for us to be successful in increasing our revenue, reducing costs, and/or securing additional funding in fiscal 2003 in order to continue operating as a going concern.

During the third quarter of fiscal 2002, the Company reduced headcount by seventeen employees thereby reducing costs while retaining enough staff to sufficiently maintain the Company's existing technology and capitalize on new technological developments. Also in the third fiscal quarter of 2002, a new management team joined the Company and evaluated ION's revenue and expenditures, existing product suite, present customer base, and evolving addressable market. As a result of this evaluation, the Company refocused its product line from that of network management monitoring to that of infrastructure security, which was the original focus of MicroFrame prior to the merger with Solcom. We also added significant network features to the product to broaden the scope of the potential customer base, emphasizing enterprise infrastructure security. We identified additional enterprise markets that extend beyond the telecommunications industry and believe that successfully penetrating these additional markets could positively impact revenue, although there can be no assurance that these efforts will be successful. Additionally, in the fourth fiscal quarter of 2002, we received $3,480,000 in a private placement.

Results Of Operations

Fiscal Year 2002 (FY2002) Compared to Fiscal Year 2001(FY2001)

Revenues for the year ended March 31, 2002 were $7,312,235 as compared with revenues of $11,676,547 for the year ended March 31, 2001, a decrease of approximately 37%. This decrease is attributable mainly to the reduction in the number of units sold in fiscal 2002. The Company sold mostly the ION Secure 3000 series security appliances (formerly called the Sentinel 2000) in both periods so there was no impact on revenue from a change in product mix. The overall downturn impacting the information technology and the telecommunications industry caused companies to severely cut capital expenditures during fiscal 2002. The Company's business historically has been dependent upon the expansion of these company's networks and therefore the decrease in revenues is a direct reflection of the environment in the industries. The Company's unit sales volumes decreased by approximately 1,100 units which contributed to approximately $2.5 million of the revenue decrease year over year. The Company's prices remained relatively consistent throughout most of fiscal 2002 as compared to fiscal 2001. The Company's cost of goods sold decreased to $3,484,132 for the year ended March 31, 2002 compared to $7,184,666 for the year ended March 31, 2001. Cost of goods sold as a percentage of sales decreased from 61.5% for the previous comparable fiscal period to 47.6% for this fiscal period. The decrease is due to the impact of additional provisions of approximately $1,549,099 that were established at various points during fiscal 2001, to recognize slow moving inventory. Without these reserves, cost of goods sold would have been 48.3% of sales in fiscal 2001.

Research and development expenses, net of capitalized software development, decreased from $2,126,246 in the year ended March 31, 2001 to $891,542 in the current fiscal year, a decrease of 58%. The decrease of research and development expenditures in FY2002 as compared to FY2001 was a result of a significant headcount reduction during FY2001, from a high of 35 people to 8 at the end of FY 2001. FY2002 reflects the impact of this reduction for a full year. A substantial amount of the reduction was a result of stopping the research and development efforts on the discontinued products as well as the reduction in research and development activities that resulted from the completion of the development cycle on certain products. The Company believes that the annual research and development expenditures were reduced to an amount sufficient to support new releases and product updates for our existing product lines.

Selling, general and administrative expenses decreased 31.6% from $11,870,263 for the year ended March 31, 2001 to $8,119,601 for the year ended March 31, 2002. Overall selling, general and administrative expenses have been reduced on a quarter-to-quarter basis throughout the fiscal year, as a result of the Company's cost reduction efforts.

Depreciation and amortization was $1,852,090 for FY2002 compared to $3,742,450 for FY2001, a decrease of approximately 50.5%. Amortization expense for capitalized software decreased from $2,138,707 in fiscal 2001 to $828,032 in fiscal 2002, primarily as a result of management's decision during fiscal 2001 to abandon the products and the technology associated with the SolCom acquisition. The decision resulted in write-offs of $2,332,120 relating to this technology thereby decreasing the amortization expense for future periods.

As a result of the Company's operating performance during the first six months of FY2002, the Company, during the third quarter of FY2002, announced the layoff of 17 employees to reduce its overhead expenses. As a result, the Company reduced its overhead expenses by approximately $1,600,000 in annual salaries and employee benefits (approximately $135,000 per month). The Company recorded approximately $217,467 of severance and termination related costs. Termination benefits of approximately $214,000 were paid during the third and fourth quarters of FY2002. All of the affected employees have left the Company as of March 31, 2002. As of April 30, 2002 the remaining termination benefits of $3,467 were paid.

The Company had a loss before taxes of $6,905,015 for the year ended March 31, 2002 compared to a loss before taxes of $16,669,098 for the year ended March 31, 2001. The loss before taxes improved primarily as a result of the Company's cost reduction efforts and management's decision during year ended March 31, 2001 to abandon certain products and technology associated with the SolCom acquisition. At March 31, 2002 and March 31, 2001 the Company had federal and state net operating loss carryforwards of approximately $35.5 million and $27.4 million respectively. The expiration dates for its net operating losses range from the years 2011 through 2022. The net loss for the year ended March 31, 2002 was $6,929,379 compared to a net loss of $16,676,666 for the prior fiscal year.

Financial Condition And Capital Resources

The Company's working capital balance as of March 31, 2002 was $5,040,922 as compared to $6,918,057 at March 31, 2001. This decline in working capital was due to continued operating losses generated throughout fiscal 2002, which was partially offset by $3,480,000 raised through the issuance of new shares in a private placement of 4,000,000 shares of Common Stock at a price of $0.87 per share. We believe that our working capital as of March 31, 2002 will fund the Company's operations, as currently planned, until January 2003. We believe that a minimum of $2,000,000 in additional capital will be needed in order to fund the Company's planned operations through June 2003. We plan to seek equity financing to provide funding for operations but the current market for equity financing is very weak. If we are not successful in raising additional equity capital to generate sufficient cash flows to meet our obligations as they come due, we plan to continue to reduce our overhead expenses by the reduction of headcount and other available measures. We may also explore the possibility of mergers and acquisitions. If we are not successful in increasing our revenue, reducing our expenses or raising additional equity

capital to generate sufficient cash flows to meet our obligations as they come due, we may not be able to continue as a going concern.

Net cash used in operating activities during FY2002 was $5,026,038 compared to net cash used during FY2001 of $7,086,246. The decrease in net cash used resulted primarily as a result of the decrease in operating losses in FY2002 as compared to FY2001; the reduction in operating losses was partially offset by the reduction in certain non-cash expenses.

Net cash provided by investing activities during FY2002 was $527,236 compared to net cash used during FY2001 of $3,213,835. Cash provided by investing activities during the year ending March 31, 2002 included the partial repayment of $813,593 by a former CEO for certain notes receivable and the release of $249,300 from the restriction of $375,000 in cash relating to the Piscataway, New Jersey operating lease.

Net cash provided by financing activities during FY2002 was $3,337,115 compared to net cash provided during the same period in FY2001 of $5,149,302. Financing activities during the year ended March 31, 2002 include the sale of 4,000,000 shares of Common Stock at a price of $0.87 per share, for total consideration of $3,480,000 in a private equity transaction. Financing activities during the year ended March 31, 2001 included the sale of 2,857,142 shares of Common Stock at a price of $1.75 per share, for total consideration of $5,000,000 in a private equity transaction.

Our consolidated financial statements have been prepared on the basis that we will continue as a going concern, which contemplates the realization and satisfaction of liabilities and commitments in the normal course of business. At March 31, 2002, we had an accumulated deficit of $37,094,424 and working capital of $5,040,922. We also realized net losses of $6,929,379 for the year ended March 31, 2002 and $16,676,666 for the year ended March 31, 2001. Our existing working capital might not be sufficient to sustain our operations.

Our plans to overcome this condition includes refocusing our sales efforts to include penetrating additional markets with our enterprise infrastructure security products, reducing expenses and raising additional equity capital. On February 14, 2002, we received $3,480,000 from the issuance of new shares in a private placement of 4,000,000 shares of Common Stock. We have restructured and reorganized to reduce our operating expenses by the layoff of 8 employees in July 2002 which reduced the Company's overhead expenses by approximately $575,000 in annual salaries and employee benefits. The Company has refocused its sales effort to emphasize the selling of its software products and reengineered its hardware products in an effort to increase gross margins. The Company has begun to establish alternate channels that will open opportunities in the future to sell our products without the overhead expenses associated with headcount. We can not assure that our sales efforts or expense reduction programs will be successful, or that additional financing will be available to us, or, if available, that the terms will be satisfactory to us. If we are not successful in increasing our revenue, reducing our expenses or raising additional equity capital, to generate sufficient cash flows to meet our obligations as they come due, we may not be able to continue as a going concern. Our financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or to amounts and classification of liabilities that may be necessary should we be unable to continue as a going concern.

Significant Accounting Policies - The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that

affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. We believe that our critical accounting policies are limited to those described below.

Revenue Recognition - The Company recognizes revenue from product sales to end users, value-added resellers (VARs) and original equipment manufacturers (OEMs) upon shipment if no significant vendor obligations exist and collectibility is probable. We do not offer our customers the right to return products, however the Company records warranty costs at the time revenue is recognized. Management estimates the anticipated warranty costs but actual results could differ from those estimates. Maintenance contracts are sold separately and maintenance revenue is recognized on a straight-line basis over the period the service is provided, generally one year.

Allowance for Doubtful Accounts Receivable - Accounts receivable are reduced by an allowance to estimate the amount that will actually be collected from our customers. Many of our customers have been adversely affected by economic downturn in the telecommunications industry. If the financial condition of our customers were to materially deteriorate, resulting in an impairment of their ability to make payments, additional allowances could be required.

Inventory Obsolescence Reserves - Inventories are stated at the lower of cost (average cost) or market. Reserves for slow moving and obsolete inventories are provided based on historical experience and current product demand. If our estimate of future demand is not correct or if our customers place significant order cancellations, inventory reserves could increase from our estimate. We may also receive orders for inventory that has been fully or partially reserved. To the extent that the sale of reserved inventory has a material impact on our financial results, we will appropriately disclose such effects. Our inventory carrying costs are not material; thus we may not physically dispose of reserved inventory immediately.

Impairment of Software Development and Purchased Software Costs - The Company capitalizes computer software development costs in accordance with the provisions of Statement of Financial Accounting Standards No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed" ("SFAS 86"). SFAS 86 requires that the Company capitalize computer software development costs upon the establishment of the technological feasibility of a product, to the extent that such costs are expected to be recovered through future sales of the product. Management is required to use professional judgment in determining whether development costs meet the criteria for immediate expense or capitalization. These costs are amortized by the greater of the amount computed using (i) the ratio that current gross revenues from the sales of software bear to the total of current and anticipated future gross revenues from the sales of that software, or (ii) the straight-line method over the estimated useful life of the product. As a result, the carrying amount of the capitalized software costs may be reduced materially in the near term.

We record impairment losses on capitalized software and other long-lived assets used in operations when events and circumstances indicate that the assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amount of those items. Our

cash flow estimates are based on historical results adjusted to reflect our best estimate of future market and operating conditions. The net carrying value of assets not recoverable is reduced to fair value. While we believe that our estimates of future cash flows are reasonable, different assumptions regarding such cash flows could materially affect our estimates.

Accounting Pronouncements

In July 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No.141 "Business Combinations" and SFAS No.142 "Goodwill and Other Intangible Assets." SFAS No.141 requires use of the purchase method of accounting for business combinations initiated after June 30, 2001. SFAS No.142, which is effective for the Company beginning April 1, 2002, requires that the amortization of goodwill and certain other intangible assets cease and that the related asset values be reviewed annually for impairment. The Company does not anticipate any material impact on its results of operations or financial position related to implementation of SFAS No.141 and 142.

In July 2001, the FASB also issued SFAS No.143, "Accounting for Asset Retirement Obligations". SFAS No.143 requires entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the entity capitalizes the cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, the entity either settles the obligation for the amount recorded or incurs a gain or loss. SFAS No.143 is effective for fiscal years beginning after June 15, 2002. The Company does not anticipate any material

impact on its results of operations or financial position related to implementation of SFAS No.143.

Item 7: Financial Statements

The financial statements required hereby are located on pages F-1 through F-21.

Item 8: Changes in and Disagreements with Accountants on Accounting and Financial Disclosures

On June 27, 2001, PricewaterhouseCoopers LLP ("PwC") indicated that upon completion of their audit of the financial statements for the year ended March 31, 2001, it would decline to stand for re-election as Ion Networks, Inc's independent accountant for the fiscal year ending March 31, 2002. PwC completed their audit on June 28, 2001. PwC's reports on the consolidated financial statements of the Company for fiscal years 2001 and 2000 did not contain any adverse opinion or a disclaimer of opinion, and were not qualified or modified as to uncertainty, audit scope or accounting principles. During fiscal years 2001 and 2000 and the subsequent interim period through June 28, 2001, there were no disagreements with PwC regarding any matters of accounting principles or practices, financial statement disclosure or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of PwC, would have caused PwC to make reference to the subject matter of the disagreement in their report on the financial statements for such years. The Company requested that PwC furnish it with a letter addressed to the Securities and Exchange Commission stating whether it agrees with the above statements. The letter, dated June 28, 2001 has been filed as Exhibit 16.1 to the Company's Form 10KSB for the year ending March 31, 2001.

The Company with the Approval of the Audit Committee of the Company's Board of Directors appointed Deloitte & Touche LLP as the Company's independent public accountants for the fiscal year ended March 31, 2002, effective as of August 13, 2001.

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Part III

Item 9: Directors, Executive Officers, Promoters and Control Persons; Compliance With Section 16(a) of the Exchange Act.

As of June 19, 2002 the directors and executive officers of the Company were as follows:

Name	Age	Position Held with the Company
Kam Saifi*	42	Chief Executive Officer, President and Director
Cameron Saifi*	40	Chief Operating Officer, Executive Vice President and Secretary
David Arbeitel	40	Chief Technology Officer and Vice President
Ted Kaminer	43	Chief Financial Officer and Vice President
Ronald Forster	39	Vice President Finance/Control
Douglas Reilly	41	Vice President, Sales and Managing Director of Market Operations for EMEA
Stephen M. Deixler/(1)(2)(3)(4)/	66	Chairman of the Board of Directors
Alexander C. Stark, Jr./(1)(2)(3)(4)/	69	Director
Alan Hardie/(3)/	61	Director
William Martin Ritchie/(4)/	53	Director
Baruch Halpern	51	Director
Frank S. Russo/(4)/	59	Director
Vincent Curatolo	43	Director

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(1) Member of Compensation/Stock Option Committee
(2) Member of Nominating Committee
(3) Member of Audit Committee

(4) Member of Strategic Steering Committee
* Mr. Kam Saifi and Mr. Cameron Saifi are brothers.

KAM SAIFI has served as Chief Executive Officer, President and Director of the Company since October 2001. Mr. Saifi also served as interim Principal Financial Officer from October 2001 until May 2002. Prior to joining ION, from November 2000 to August 2001, Mr. Saifi served as the Chairman of the Board of Directors and Chief Executive Officer of Internet Refinery, a provider of collaborative commerce and business intelligence solutions. From June 2000 to August 2000, Mr. Saifi served as Vice Chairman and Executive Vice President of Visual Networks, Inc. which merged with Avesta Technologies, Inc., a New York-based software company focusing on managing Internet infrastructure. Mr. Saifi was the Founder, Chairman of the Board of Directors, Chief Executive Officer and President of Avesta Technologies, Inc. from October 1996 to May 2000. He has also served as a member of the Board of Directors for MetaMatrix from 1998 to 2000.

CAMERON SAIFI has served as Chief Operating Officer and Executive Vice President of the Company since October 2001 and Secretary of the Company since December 2001. Prior to joining ION, from October 2000 to October 2001, Mr. Saifi served as the President, Chief Operating Officer and Co-Founder of Internet Refinery, a provider of collaborative commerce and

business intelligence technology for Business-to-Business applications. Previously, from January 1997 to June 2000, Mr. Saifi served as Senior Vice President and Chief Operating Officer for Avesta Technologies, Inc.

DAVID ARBEITEL has served as Chief Technology Officer and Vice President of the Company since October 2001. Prior to joining ION, Mr. Arbeitel was the sole proprietor of his consulting firm, Arbeitel Associates 2 from September 2000 to October 2001. From June 2000 to September 2000, Mr. Arbeitiel served as Vice President and Chief Technology Officer of Visual Networks, Inc. and was one of the founders of Avesta Technologies, Inc. where he was Senior Vice President and Chief Technology Officer from October 1996 to May 2000.

TED KAMINER has served as Chief Financial Officer and Vice President of the Company since May 2002. Prior to joining ION, from October 2000 to April 2002, Mr. Kaminer was an independent consultant. From March 1998 to September 2000, Mr. Kaminer served as Senior Vice President of Finance and Chief Financial Officer of CMPExpress, a provider of computer hardware and software to corporate, government and education accounts. Previously, he served as Senior Vice President, Investment Banking at Berwind Financial Group, L.P., from October 1994 to January 1998.

RONALD FORSTER has served as Vice President Finance/Controller since October 2001, and was the Controller from February 2000 to October 2001. Prior to joining ION, from March 1991 to February 2000, Mr. Forster served as Controller of Meto, a company engaged in electronic bar code and human readable marking and identification systems.

DOUGLAS REILLY served as Vice President, Sales and Managing Director of Market Operations for EMEA since October 2001 and was the Managing Director of European Operations from July 2000 to October 2001. Prior to joining ION, from February 1995 to June 2000, Mr. Reilly served as the Worldwide Head of Sales for the Wireless Division of KSCL, a telecommunications and billing software company.

STEPHEN M. DEIXLER has been Chairman of the Board of Directors since

1985 and served as Chief Executive Officer of the Company from April 1996 to May 1997. He was President of the Company from May 1982 to June 1985 and served as Treasurer of the Company from its formation in 1982 until September 1993. Mr. Deixler currently also serves as Chairman of the Board of Trilogy Leasing Co, LLC and became Chief Financial Officer of Multipoint Communications, LLC in March 2002. Mr. Deixler was the Chairman of Princeton Credit Corporation until April 1995.

ALEXANDER C. STARK, JR. has been a director of the Company since 1997. From 1995 to 2000, Mr. Stark served as the President of AdCon, Inc., a consulting firm organized to advise and counsel senior officers of global telecom companies. Mr. Stark previously worked for 40 years at AT&T, where he most recently served as a Senior Vice President.

ALAN HARDIE has served as a director of the Company since 1999. From 1995 until 2001, when he retired, Mr. Hardie served as Chief of Operations for AT&T and BT Global Venture-Concert.

WILLIAM MARTIN RITCHIE has served as a director of the Company since 1999. Since 1995, Mr. Ritchie has been a consultant in his own consulting entity, Mr. Ventures, where he provides various start-up companies with management assistance and early stage investment. Mr. Ritchie was a founder of Spider Systems, a Scottish electronics company, where he served in several capacities, including as Managing Director, from 1984 to 1995. Mr. Ritchie currently serves on the board of directors of various companies in Scotland.

BARUCH HALPERN has served as a director of the Company since 1999. From 1995 to 1999, Mr. Halpern was an institutional research analyst with Goldsmith & Harris Incorporated, where he advised institutions about investment opportunities. He was also an advisor in connection with a leveraged buy-out of a public company and several private placements. In 1999, Mr. Halpern formed Halpern Capital as a DBA entity under Goldsmith & Harris Incorporated. Currently, Halpern Capital is a DBA entity under UVEST Investment Services, a member of NASD/SIPC. Over the last two years Baruch Halpern's entities was involved in numerous financings, having raised over $225 million in capital for several public entities.

FRANK RUSSO has served as a director of the Company since 2000. Mr. Russo was with AT&T Corporation from September 1980 to September 2000 and most recently served as its Corporate Strategy and Business Development Vice President. While at AT&T Solutions, Mr. Russo held a number of other positions including that of General Manager, Network Management Services from which he helped architect and launch AT&T's entry into the global network outsourcing and

professional services business. Mr. Russo retired from AT&T in 2000. Prior to joining AT&T, Mr. Russo was employed by IBM Corporation in a variety of system engineering, sales and sales management positions. Mr. Russo served on the Board of Director of Oak Industries, Inc., a manufacturer of highly engineered components, in 1999 and 2000, and currently serves on the Board of Directors of Advance-com, a private e-commerce company headquartered in Boston, Massachusetts.

VINCENT CURATOLO has served as director of the Company since 2002. Mr. Curatolo has held several executive positions at Cisco Systems since May 1998. He is currently the Senior Director of Business Development for the Global Service Provider Business Unit of Cisco Systems. Prior to that position, he served as the Senior Director and Director of Cisco Systems in the areas of field operations and technical field operations. From December 1994 to May 1998,

Mr. Curatolo served as Vice President of Global Data Networks at JP Morgan.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities and Exchange Act of 1934, as amended (the "Exchange Act"), requires the Company's directors, executive officers and persons who own more than 10% of the Company's Common Stock (collectively, "Reporting Persons") to file reports of ownership and changes in ownership of the Company's Common Stock with the Securities and Exchange Commission and The Nasdaq Stock Market, Inc. Copies of these reports are also required to be delivered to the Company.

The Company believes, based solely on its review of the copies of such reports received or written representations from certain Reporting Persons, that during the fiscal year ended March 31, 2002, Mr. Vincent Curatolo was inadvertently late in filing his Form 3 to report his appointment to the Board of Directors of the Company in March 2002 and a grant of options to purchase 10,000 shares of Common Stock. Mr. Ronald Forster was inadvertently late in filing his Form 3 to report his appointment to the office of Vice President Finance/Controller in October 2001 and a grant of options to purchase 80,000 shares of Common Stock and his holding of 180 shares of Common Stock and options to purchase 81,273 shares of Common Stock at the time of the filing of his Form 3. Mr. Douglas Reilly was in advertently late in filing his Form 3 to report his appointment to the office of Vice President and Managing Director of Market Operations for EMEA and the Pacific Rim in October 2001 and a grant of options to purchase 100,000 shares of Common Stock and his holding of options to purchase 124,652 shares of Common Stock at the time of the filing of his Form 3. All such inadvertently late filings have been filed and reported by the Reporting Persons on a Form 5 for the fiscal year ended March 31, 2002.

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Item 10: Executive Compensation

The following table sets forth the compensation earned, whether paid or deferred, by the Company's Chief Executive Officer, its other four most highly compensated executive officers during the year ended March 31, 2002 and up to two additional individuals for whom disclosure would have been provided but for the fact that the individual was not serving as an executive officer at the end of fiscal year ended March 31, 2002 (the "Named Executive Officers") for services rendered in all capacities to the Company.

Summary Compensation Table

		Annual Compensation				Long-term Com
					Awards	
Principal Position	Year	Salary($)	Bonus($)	Other Annual Compen-sation ($)	Restricted Stock Award(s)($)	Securitie Underying Options (

Current CEO and Executive Officers:						
Kam Saifi/(2)(7)/ President & Chief Executive Officer	2002	132,681/(8)/	50,000	--	240,000/(11)/	--
Cameron Saifi/(3)(7)/ Executive Vice President & Chief Operating Officer	2002	90,519	25,000	--	186,000/(12)/	--
David Arbeitel/(4)(7)/ Vice President & Chief Technology Officer	2002	72,231	12,500	--	93,000/(13)/	--
Ronald Forster	2002	107,019	9,000	--	--	80,000
Vice President of	2001	94,000	3,540			64,809
Finance & Controller	2000	13,962	--			16,476
Douglas Reilly	2002	129,246/(9)/	2,250	--	--	100,000
Vice President, Sales & Managing Director, EMEA	2001	78,936/(10)/	--	--	--	124,652
Former CEO and Executive Officers:						
Ronald C. Sacks	2002	--	--	--	--	21,500
/(5)(7)/ Former Chief-Executive Officer and Interim Principal Financial Officer	2001	--	--	--	--	119,400
Jane Kaufman/(6)/	2002	93,402	10,000	22,383	--	50,000
Former President	2001	159,000	--	--	--	172,430
and Chief Operating Officer	2000	36,115	--	10,000	--	153,376

(1) Represents contribution of the Company under the Company's 401(k) Plan.

(2) Mr. K. Saifi joined the Company on 10/1/01. Pursuant to his employment agreement, he will receive an annualized base salary of $250,000.

(3) Mr. C. Saifi joined the Company on 10/17/01. Pursuant to his employment agreement, he will receive an annualized base salary of $186,000.

(4) Mr. Arbeitel joined the Company on 10/17/01. Pursuant to his employment agreement, he will receive an annualized base salary $148,000.

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(5) The services of Mr. Sacks were being provided through a consulting agreement between the Company and Venture Consulting Group, Inc. ("VCGI"). During the fiscal year ended March 31, 2002, $248,000 was paid to VCGI for consulting fees related to services performed by Mr. Sacks. Mr. Sacks terminated his consulting services with the Company as of September 18, 2001.

(6) Ms. Kaufman separated from the Company on 10/3/01 as the result of a reduction in force. As per the terms of her Severance Agreement and General Release, Ms. Kaufman received a one-time severance payment of $15,542. Ms. Kaufman also received payment of $6,841 for accrued unused vacation time.

(7) Refer to the Employment Contracts, Termination of Employment and Change of Control Arrangements section below for a more detailed description of all consulting and employment agreements.

(8) Includes $7,200 in auto allowance.

(9) Includes $9,000 in auto allowance and $21,496 in commissions.

(10) Includes $6,750 in auto allowance and $4,686 in commissions.

(11) These shares vest as follows: 250,000 on October 4, 2001, 550,000 on September 30, 2002 and 150,000 at the end of each quarter, commencing with the quarter ended December 31, 2002, and ending with the quarter ending September 30, 2004, for a total of 1,200,000. The value of these shares as of March 31, 2002 is $1,520,000 and dividends, if declared, will be paid.

(12) These shares vest as follows: 75,000 on October 17, 2001, 165,000 on September 30, 2002 and 45,000 at the end of each quarter, commencing with the quarter ended December 31, 2002, and ending with the quarter ending September 30, 2004, for a total of 360,000. The value of these shares as of March 31, 2002 is $456,000 and dividends, if declared, will be paid.

(13) These shares vest as follows: 37,500 on October 17, 2001, 82,500 on September 30, 2002 and 22,500 at the end of each quarter, commencing with the quarter ended December 31, 2002, and ending with the quarter ending September 30, 2004, for a total of 180,000. The value of these shares as of March 31, 2002 is $228,000 and dividends, if declared will be paid.

Option Grants in Fiscal Year Ended March 31, 2002

The following table sets forth certain information concerning stock option grants during the fiscal year ended March 31, 2002 to the Named Executive Officers:

	Individual Grants		
Name	Number of Securities Underlying Options Granted(#)	Percent of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price ($/Sh)
Current CEO and Executive Officers:			
Kam Saifi	--		
Cameron Saifi	--		
David Arbeitel	--		

Ronald Forster	80,000/(1)(4)/	3.5%	.175
Douglas Reilly	100,000/(1)(5)/	4.3%	.175
Former CEO and Executive Officers:			
Ronald C. Sacks	21,500/(2)/	1.0%	.205
Jane Kaufman	50,000/(3)/	2.2%	1.01

(1) Represents options granted for retention purposes following the October 3, 2001 reduction in force.

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(2) 20,000 options were granted upon election to the Board of Directors on 9/24/01 and 1.500 options were granted for attendance at Annual Meeting of the Board of Directors held on September 24, 2001. These options vested immediately and have been exercised

(3) Represents options granted upon promotion to President and Chief Operating Officer. These options vested immediately upon Ms. Kaufman's resignation from the Company on October 3, 2001. Ms. Kaufman has until October 3, 2003 to exercise these options.

(4) 27,200 options will vest on October 12, 2002 and 6,600 options will vest every 3 months thereafter.

(5) 34,000 options will vest on October 12, 2002 and 8,250 options will vest every 3 months thereafter.

Aggregated Option Exercises in Fiscal Year Ended March 31, 2002
And Fiscal Year End Option Values

The following table sets forth certain information concerning each exercise of stock options during the fiscal year ended March 31, 2002 by each of the Named Executive Officers and the number and value of unexercised options held by each of the Named Executive Officers on March 31, 2002.

Name	Shares Acquired on Exercise (#)	Value Realized($)	Number of Securities Underlying Unexercised Options at FY-End(#) Exercisable/Unexercisabl
Current CEO and Executive Officers:			
Kam Saifi	--	--	--
Cameron Saifi	--	--	--
David Arbeitel	--	--	--
Ronald Forster	--	--	37,225/124,060

Douglas Reilly	--	--	49,600/175,052
Former CEO and Executive Officers:			
Ronald C. Sacks	21,500	5,160	119,400/0
Jane Kaufman	--	--	200,000/0

(1) The average price for the Common Stock as reported by the Nasdaq Stock Market on March 28, 2002, was $.76 per share. Value is calculated on the basis of the difference between the option exercise price and $.76 multiplied by the number of shares of Common Stock underlying the options.

Compensation of Directors: Standard Arrangements

For the fiscal year ended March 31, 2002, each of the members of the Board of Directors who is not also an employee of the Company ("Non-Employee Directors") received fully vested options to purchase 10,000 shares of Common Stock at exercise prices per share equal to the fair market value of the Common Stock on the date of grant. Non-Employee Directors were also granted fully vested options to purchase an additional 1,500 shares of Common Stock for each meeting of the Board of Directors attended by such Non-Employee Director at exercise prices per share equal to the fair market value of the common stock on the date of the grant. Non-Employee Directors serving on committees of the Board of Directors were granted, on an annual basis, fully vested options to purchase 1,500 shares of Common Stock for each committee served thereby at exercise prices per share equal to the fair market value of the common stock on the date of the grant.

In July 2001, the Board of Directors approved a modification to the director compensation plan for the fiscal year ending March 31, 2002. The modification provides that any director who was not previously serving as such at the time of the last

annual stockholder's meeting would receive an additional grant of options to purchase 20,000 shares upon election by the stockholders at exercise prices per share equal to the fair market value of the common stock on the day of the grant. In addition, the Company reimburses all Non-Employee Directors traveling more than fifty miles to a meeting of the Board of Directors for all reasonable travel expenses.

Compensation of Directors: Other Arrangements

On October 31, 2001, the Board of Directors granted options to purchase 25,000 share of Common Stock to each of Messrs. Deixler, Halpern, Stark, Hardie, Ritchie and Russo in recognition of their services to the Company with the retention of the new executive management team. These options were granted at an exercise price of $0.335 per share (the fair market value of the

Common Stock on the date of grant), are fully vested and expire on October 30, 2006.

The Company paid the Chairman of the Board of Directors of the Company, $132,000 in the year ended March 31, 2002 for executive search and mergers and acquisitions services provided to the Company from June through October 2001.

Employment Contracts, Termination of Employment and Change of Control Arrangements

The Company entered into an employment agreement with Kam Saifi dated October 4, 2001. Pursuant to the agreement, Mr. Saifi shall serve as Chief Executive Officer and President commencing October 1, 2001 and continuing until September 30, 2004 unless earlier terminated as provided in the agreement. Mr. Saifi will receive a base salary at an annual rate of $250,000 during the period of October 1, 2001 and ending March 31, 2002, or total compensation for the six-month period of $125,000. He will receive a base salary at an annual rate of $350,000 during the period of April 1, 2002 and ending September 30, 2002, or total compensation for the six-month period of $175,000. In addition he will receive a monthly car allowance of $1,200. Mr. Saifi will also receive a quarterly bonus payment of $50,000 each time the Company achieves its gross sales target in such fiscal quarter. Pursuant to the agreement, Mr. Saifi was granted restricted stock consisting of 2,000,000 shares of the Company's Common Stock at a price of $0.13 per share. These shares vest as follows: 250,000 on execution of the agreement, 550,000 on September 30, 2002 and 150,000 at the end of each quarter, commencing with the quarter ended December 31, 2002, and ending with the quarter ending September 30, 2004, for a total of 1,200,000. In the event of a change in control event (as described in the employment agreement) all shares will become immediately vested. If Mr. Saifi's employment is terminated by the Company for other than "Cause", Mr. Saifi shall be entitled to a severance payment equal to the lesser of the remaining salary due for the balance of the contract or payment of salary for the next six months as if the Agreement had not been terminated.

The Company entered into an employment agreement with Cameron Saifi dated October 17, 2001. Pursuant to the agreement, Mr. C. Saifi shall serve as Chief Operating Officer and Executive Vice President commencing October 17, 2001 and continuing until September 30, 2004 unless earlier terminated as provided in the agreement. Mr. C. Saifi will receive a base salary at an annual rate of $186,000. Mr. C. Saifi will also receive a quarterly bonus payment of $25,000 each time the Company achieves its gross sales target in such fiscal quarter. Pursuant to the agreement, Mr. C. Saifi was granted restricted stock consisting of 600,000 shares of the Company's Common Stock at a price of $0.31 per share. These shares vest as follows: 75,000 on execution of the agreement, 165,000 on September 30, 2002 and 45,000 at the end of each quarter, commencing with the quarter ended December 31, 2002, and ending with the quarter ending September 30, 2004, for a total of 360,000. In the event of a change in control event (as described in the employment agreement) all shares will become immediately vested. If Mr. Saifi's employment is terminated by the Company for other than "Cause", Mr. Saifi shall be entitled to a severance payment equal to the lesser of the remaining salary due for the balance of the contract or payment of salary for the next three months as if the Agreement had not been terminated.

The Company entered into an employment agreement with David Arbeitel dated October 17, 2001. Pursuant to the agreement, Mr. Arbeitel shall serve as Chief Technology Officer and Vice President commencing October 17, 2001 and continuing until September 30, 2004 unless earlier terminated as provided in the agreement. Mr. Arbeitel will receive a base salary at an annual rate of $148,000. Mr. Arbeitel will also receive a quarterly bonus payment of $12,500 each time the Company achieves its gross sales target in such fiscal quarter.

Mr. Arbeitel was granted restricted stock consisting of 300,000 shares of the Company's Common Stock at a price of $0.31 per share. These shares vest as follows: 37,500 on execution of the agreement, 82,500 on September 30, 2002 and 22,500 at the end of each quarter, commencing with the quarter ended December 31, 2002, and ending with the quarter ending September 30, 2004, for a total of 180,000. In the event of a change in control event (as described in the employment agreement) all shares will become immediately vested. If Mr. Arbeitel's employment is terminated by the Company for other than "Cause", Mr. Arbeitel shall be entitled to a severance payment equal to the lesser of the remaining salary due for the balance of the contract or payment of salary for the next three months as if the Agreement had not been terminated.

The Company entered into a consulting agreement with Venture Consulting Group, Inc. ("VCGI") on October 5, 2000 (the "Consulting Agreement"). VCGI performed certain management services for the Company and provided the services of Ronald C. Sacks, William Gilbert, George Jarrold and Daniel Hunt. Pursuant to the terms of the Consulting Agreement, Mr. Sacks was appointed as the Chief Executive Officer of the Company and provided his services on a full time, exclusive basis until September 18, 2002. The other persons specified above provided consulting services 10 days per quarter each, with respect to such services. The Consulting Agreement was terminable at will on thirty days written notice by either party, and provided for a fee of $500,000, payable over twelve (12) months to VCGI. The Company did not pay salaries to any of the VCGI management team members. In addition, the Company granted options to the persons performing services on behalf of VCGI to purchase an aggregate of 240,000 shares of Common Stock, at an exercise price of $2.00 per share which are fully vested. The consulting

relationship established by this contract terminated effective September 18, 2001.

Item 11: Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Equity Compensation Plan Information

	(a) Number of securities to be issued upon exercise of outstanding options, warrants, and rights	(b) Weighted-average exercise price of outstanding options, warrants, and rights	r eq r
Plan Category			
Equity compensation plans approved by security holders/(1)/	4,438,260	1.82	
Equity compensation plans not approved by security holders/(2)/	688,000	1.30	
Total	5,126,260	1.75	

(1) Shareholder Approved Plans

In November 2000, the Company adopted its 2000 Stock Option Plan (the "2000 Plan"). The aggregate number of shares of common stock for which options may be granted under the 2000 Plan is 3,000,000. The maximum number of options which may be granted to an employee during any calendar year under the 2000 Plan shall be 400,000. The term of these non-transferable stock options may not exceed ten years. The exercise price of these stock options may not be less than 100% (110% if the person granted such options owns more than ten percent of the outstanding common stock) of the fair value of one share of common stock on the date of grant. During the years ended March 31, 2002 and 2001, the Company granted options to purchase 1,854,000 and 1,724,500 shares, respectively. At March 31, 2002, 2,560,200 options were outstanding under the 2000 Plan, of which 759,915 options were exercisable.

The aggregate number of shares of common stock for which options may be granted under the 1998 Stock Option Plan (the "1998 Plan") is 3,000,000. The maximum number of options which may be granted to an employee during any calendar year under the 1998 Plan shall be 400,000. The term of these non-transferable stock options may not exceed ten years. The exercise price of these stock options may not be less than 100% (110% if the person granted such options owns more than ten percent of the outstanding common stock) of the fair value of one share of common stock on the date of grant. During the years ended March 31, 2002 and 2001, the Company granted options to purchase 463,800 and 1,596,078 shares, respectively. At March 31, 2002 1,783,459 options were outstanding under the 1998 Plan, of which 1,367,642 options were exercisable.

In August 1994, the Company adopted its 1994 Stock Option Plan (the "1994 Plan"). The 1994 Plan, as amended, increased the number of shares of common stock for which options may be granted to a maximum of 1,250,000 shares. The term of these non-transferable stock options may not exceed ten years. The exercise price of these stock options may not be less than 100% (110% if the person granted such options owns more than ten percent of the outstanding common stock) of the fair market value of one common stock on the date of grant. During the years ended March 31, 2002 and 2001, there were no option grants provided under the 1994 Plan. At March 31, 2002, 94,601 options were outstanding under the 1994 Plan, of which 64,991 options were exercisable.

Of the options granted in fiscal 2002 and 2001, 0 and 578,528, respectively, were granted under the Company's Time Accelerated Restricted Stock Award Plan ("TARSAP"). The options vest after seven years, however, under the TARSAP, the vesting is accelerated to the last day of the fiscal year in which the options are granted if the Company meets certain predetermined sales targets. The Company did not meet the targets for 2001 and, as such, all options granted under the TARSAP in 2001 will vest seven years from the original date of grant.

(2) Non-Shareholder Approved Awards

The Company has granted options and warrants to purchase 688,000 shares of Common Stock outside of the shareholder approved plans. The awards have been made to employees, directors and consultants, and except as noted below, have been granted with an exercise price equal to the fair market value of the Common Stock on the date of grant. The Company has not reserved a specific number of shares for such awards. The non-shareholder approved awards are more specifically described below.