

Edgar Filing: XIN NET CORP - Form 10QSB

XIN NET CORP
Form 10QSB
May 15, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

Quarterly Report Pursuant to Section 13 or 15(d) of

The Securities Exchange Act of 1934

For the quarterly period ended: March 31, 2002

Commission file number 0-26559

CIK No. 0001082603

XIN NET CORP.

(Exact name of registrant as specified in this charter)

Florida

330-751560

(State of other jurisdiction
of incorporation or organization)

(I.R.S. Employer
Identification No.)

#950 - 789 West Pender Street, Vancouver, B.C. Canada V6C 1H2

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (604) 632-9638

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to the filing requirements for at least the past 90 days.

YES X NO

As of March 31, 2002, there were 21,360,010 shares of \$0.001 par value common stock outstanding.

PART 1. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

XIN NET CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

Stated in U.S. dollars

March 31,
2002

Decemb
20

Edgar Filing: XIN NET CORP - Form 10QSB

(Unaudited)

ASSETS

Current Assets

| | | | |
|---|----|-----------|----|
| Cash and Cash Equivalents | \$ | 883,384 | \$ |
| Investments | | 62,785 | |
| Accrued Interest Receivables | | 1,033 | |
| Loan to ProtectServe Pacific Ltd. | | - | |
| Inventory | | 6,030 | |
| Prepaid Expenses and Other Current Assets | | 184,240 | |
| Net Assets of Discontinued Operations | | 293,396 | |
| Deferred Costs | | 603,334 | |
| Total Current Assets | | 2,034,202 | |
| Investment - at equity (Note 4) | | 824,652 | |
| Property and Equipment, Net (Note 2) | | 707,013 | |
| Goodwill | | - | |
| Total Assets | \$ | 3,565,867 | \$ |

LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities

| | | | |
|--|----|-----------|----|
| Accounts Payable and Other Accrued Liabilities | \$ | 661,870 | \$ |
| Deferred Revenue | | 1,818,888 | |
| Security Deposit | | 500,000 | |
| Capital Lease Obligation (Note 3) | | 43,784 | |
| | | 3,024,542 | |

Commitments and Contingencies

Stockholders' Equity

| | | | |
|--|--|-------------|--|
| Common Stock : \$0.001 Par Value | | | |
| Authorized : 50,000,000 | | | |
| Issued and Outstanding : 21,360,010 | | 21,360 | |
| Additional Paid In Capital | | 7,214,045 | |
| Accumulated Deficit | | (6,546,103) | |
| Accumulated Other Comprehensive Income | | (147,977) | |

Edgar Filing: XIN NET CORP - Form 10QSB

| | | | |
|--|-------|-----------|-------|
| Total Stockholders' Equity | ----- | 541,325 | ----- |
| Total Liabilities and Stockholders' Equity | \$ | 3,565,867 | \$ |
| | ===== | ===== | ===== |

F-1

XIN NET CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE-MONTH PERIODS ENDED MARCH 31, 2002 AND 2001
(Unaudited)

| Stated in U.S. dollars | 2002 |
|-------------------------------|------------|
| Revenue | |
| Domain Name Registration | \$ 723,187 |
| E-Solutions | 285,403 |
| | ----- |
| | 1,008,590 |
| Cost of Revenue | |
| Domain Name Registration | 379,410 |
| E-Solutions | 16,175 |
| | ----- |
| | 395,585 |
| Gross Profit | 613,005 |
| Expenses | |
| Advertising and promotion | 30,955 |
| Depreciation and Amortization | 57,029 |
| General and administrative | 137,559 |
| Rent | 96,574 |
| Salaries, wages and benefits | 347,251 |
| Telephone and communication | 77,535 |
| | ----- |
| | 746,903 |
| | ----- |
| Operating Loss | (133,898) |

Edgar Filing: XIN NET CORP - Form 10QSB

Other Income

| | | |
|---|--------------|-------|
| Interest income | 1,015 | |
| Equity in undistributed earnings of investee company (Note 4) | 24,352 | |
| | ----- | ----- |
| | 25,367 | |
| Loss from Continuing Operations | (108,531) | |
| Loss from Discontinued Operations | - | |
| | ----- | ----- |
| Net Loss Available to Common Stockholders | \$ (108,531) | ===== |
| Loss per share attributable to common stockholders: | | |
| Loss from continuing operations | \$ (0.01) | |
| Loss from discontinued operations | - | |
| | ----- | ----- |
| Total basic and diluted | \$ (0.01) | ===== |
| Weighted average number of common shares outstanding: | | |
| Basic and diluted | 21,360,010 | ===== |

F-2

XIN NET CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
FOR THE THREE MONTHS ENDED MARCH 31, 2002 AND THE YEARS ENDED DECEMBER 31, 2001
(Unaudited)

| Stated in U.S. dollars | Common Shares | Stock Amount At Par Value | Additional Paid In Capital | Accumulated Deficit |
|---|------------------|---------------------------------|----------------------------------|------------------------|
| ----- | ----- | ----- | ----- | ----- |
| Balance, December 31, 1999 | 21,360,000 | \$ 21,360 | \$ 7,214,025 | \$ (1,318,945) |
| Exercise of Warrant for cash at \$2.00 per share in September 2000 | 10 | - | 20 | |
| Net loss | | | | (3,607,724) |
| Translation Adjustments | | | | |

Edgar Filing: XIN NET CORP - Form 10QSB

| | | | | |
|----------------------------|------------|-----------|--------------|----------------|
| Balance, December 31, 2000 | 21,360,010 | 21,360 | 7,214,045 | (4,926,669) |
| Net loss | | | | (1,510,903) |
| Translation Adjustments | | | | |
| Balance, December 31, 2001 | 21,360,010 | 21,360 | 7,214,045 | (6,437,572) |
| Net loss | | | | (108,531) |
| Translation Adjustments | | | | |
| Balance, March 31, 2002 | 21,360,010 | \$ 21,360 | \$ 7,214,045 | \$ (6,546,103) |

F-3

XIN NET CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE MONTHS ENDED MARCH 31, 2002 AND 2001
(Unaudited)

| Stated in U.S. dollars | 2002 |
|--|-------------|
| Cash flows from operating activities | |
| Net loss | \$(108,531) |
| Adjustments to reconcile net loss to net cash | |
| Provided by (Used in) operating activities | |
| Depreciation and amortization | 57,026 |
| Translation adjustments | 61 |
| Equity income of The Link Group, Inc. | (24,352) |
| Changes in assets and liabilities | |
| (Increase) Decrease in accrued interest receivables | (332) |
| Increase in prepaid expenses and other current assets | (1,052) |
| (Increase) Decrease in inventory | (45) |
| (Increase) Decrease in net assets of discontinued operations | |
| (Increase) Decrease in deferred costs | (31,656) |
| Increase (Decrease) in accounts payable | (21,958) |
| Increase (Decrease) in deferred revenue | (42,812) |
| Net cash used in operating activities | (173,097) |
| Cash flows from investing activities | |
| Purchases of property and equipment | (49,926) |

Edgar Filing: XIN NET CORP - Form 10QSB

| | |
|---|-----------|
| Reduction in investment | 1,29 |
| Reduction in loan to ProtectServe Pacific Ltd. | 360,40 |
| Investment in The Link Group, Inc. | (600,300) |
| Net cash flows used in investing activities | (288,534) |
| Cash flows from financing activities | |
| Principal payments on capital lease obligations | (15,056) |
| Net cash flows used in financing activities | (15,056) |
| Decrease in cash and cash equivalents | (476,687) |
| Cash and cash equivalents - beginning of period | 1,360,07 |
| Cash and cash equivalents - end of period | \$ 883,38 |
| Supplemental Information : | |
| Cash paid for : | |
| Interest | 2,97 |
| Income taxes | |

F-4

XIN NET CORP. AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2002

(Unaudited)

1. Basis of Presentation

The accompanying unaudited financial statements have been prepared in conformity with generally accepted accounting principles. However, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted or condensed pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). In the opinion of the management all adjustments of a normal recurring nature necessary for a fair presentation have been included. The results for interim periods are not necessarily indicative of results for the entire year. These condensed consolidated financial statements and accompanying notes should be read in conjunction with the Company's annual consolidated financial statements and the notes thereto for the fiscal year ended December 31, 2001 included in its Annual Report on Form 10-KSB.

The unaudited condensed consolidated financial statements include Xin Net Corp.

Edgar Filing: XIN NET CORP - Form 10QSB

and its subsidiaries. Significant inter-company transactions and accounts have been eliminated.

2. Property and Equipment

Property and equipment consists of the following :

| | March 31, 2002 | December 31, 2001 |
|---------------------------------|----------------|-------------------|
| Office equipment | \$ 219,799 | \$ 229,300 |
| Equipment | 904,407 | 757,600 |
| Computer software | 83,299 | 83,200 |
| Furniture | 27,976 | 27,900 |
| Total | 1,235,481 | 1,098,200 |
| Less : Accumulated depreciation | (528,468) | (384,000) |
| Net book value | \$ 707,013 | \$ 714,200 |

The depreciation expense charged to continuing operations for the three-month period ended March 31, 2002 is \$57,029.

F-5

XIN NET CORP. AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2002

(Unaudited)

3. Capital Lease Obligation

The Company leases computer equipment, through its wholly owned subsidiary company Infonet Investment Corp., repayable at approximately \$5,330 (CND 8,407) per month to June 30, 2002. The liability includes imputed interest at an average rate of 6.12% per annum.

| | | |
|--|----|----------|
| Total minimum lease payments | | |
| For the year ended March 31 | | |
| 2003 | \$ | 44,457 |
| Less : Amount representing interest | | (673) |
| | | 43,784 |
| Present value of minimum lease payment | | 43,784 |
| Less : Current portion | | (43,784) |
| | \$ | - |

Edgar Filing: XIN NET CORP - Form 10QSB

4. Investment in The Link Group, Inc. ("Link")

Pursuant to a Subscription Agreement dated January 18, 2002, the Company paid \$600,300 in a private placement of Link for 14,500,000 (pre-reverse one for four split) common shares at \$0.0414 per share, as well as 10,875,000 special warrants convertible into 10,875,000 post-reverse one for four split common shares on or before January 31, 2004 at no additional consideration. The Company exercised the 10,875,000 special warrants on March 12, 2002. An option to purchase an additional 7,500,000 post-reverse one for four split common shares at \$0.04 per share, or \$300,000, until February 15, 2002, was also granted to the Company, which was not exercised.

By an agreement dated January 21, 2002, Link agreed to purchase all of the outstanding shares of Protectserve Pacific Ltd. ("PSP") through the issuance of 37,500,000 (post-reverse one for four split) common shares. Link has the right to buy back its shares at \$0.001 per share from these individuals if PSP's after tax profit is less than Hong Kong \$9 million dollars ("HKD") for the twelve months ending December 31, 2002. The buy back formula is for every HKD \$333,333 that PSP falls short of the HKD \$9 million after tax profit, Link can buy back one million (post-reverse one for four split) common shares from these individuals.

F-6

XIN NET CORP. AND SUBSIDIARIES
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
 March 31, 2002

(Unaudited)

4. Investment in The Link Group, Inc. ("Link") - Continued

On February 18, 2002, the shareholders of Link approved the reverse split of the issued and outstanding common shares of Link at the ratio of one for four, thereby making the Company's total Link shares held equal to 15,370,675 shares, representing 28.8% of the total issued and outstanding shares of Link. The Company therefore accounted for its investment in Link on the equity basis, which is carried at cost, adjusted for the Company's proportionate share of their undistributed earnings or losses as follow:

| | |
|--|------------|
| Original cost of 15,370,675 shares of The Link Group, Inc. | \$ 800,300 |
| Equity in undistributed earnings of investee company | 24,352 |
| | ----- |
| Investment - at equity | \$ 824,652 |
| | ===== |

5. Basic and Diluted Earnings (Loss) Per Share

Basic earnings (loss) per share are computed by dividing net earnings (loss) available to common stockholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net earnings available to common stockholders by the weighted-average

Edgar Filing: XIN NET CORP - Form 10QSB

number of common shares outstanding during the period increased to include the number of additional common shares that would have been outstanding if potentially dilutive common shares had been issued.

The following table sets forth the computations of shares and net loss used in the calculation of basic and diluted loss per share for the three-month periods ended March 31, 2002 and 2001:

F-7

XIN NET CORP. AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2002

(Unaudited)

5. Basic and Diluted Loss Per Share - Continued

| | Three months ended | |
|--|--------------------|--------------|
| | 3/31/2002 | 3/31/2001 |
| Net loss from continuing operations | \$ (108,531) | \$ (596,000) |
| Weighted-average shares outstanding | 21,360,010 | 21,360,010 |
| Effect of dilutive securities : | | |
| Dilutive options | - | - |
| Dilutive warrants | - | - |
| Dilutive potential common shares | - | - |
| Adjusted weighted-average shares and assumed conversions | 21,360,010 | 21,360,010 |
| Basic loss from continuing operations per share | \$ (0.01) | \$ (0.03) |
| Diluted loss from continuing operations per share | \$ (0.01) | \$ (0.03) |

Due to the loss for the three-month periods ended March 31, 2002 and 2001, the effect of outstanding options and warrants was not included as the effect would be anti-dilutive.

6. Total Amount Advanced to Joint Venture

As at March 31, 2002, the total amount advanced to the joint venture project is \$3,151,527.

7. Segment and Geographic Data

Edgar Filing: XIN NET CORP - Form 10QSB

The Company's reportable segments are geographic areas that provide internet-related services and products to the Chinese markets. Summarized financial information concerning the Company's reportable segments is shown in the following table. The "Other" column includes corporate related items, and, as it relates to segment profit (loss), income and expenses not allocated to reportable segments.

F-8

XIN NET CORP. AND SUBSIDIARIES
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
 March 31, 2002
 (Unaudited)

7. Segment and Geographic Data - Continued

| | China | Canada | Other |
|---------------------------------------|--------------|---------|-----------|
| For three months ended March 31, 2002 | | | |
| | | | |
| Revenue from continuing | | | |
| Operations | \$ 1,008,590 | - | - |
| Operating loss | (70,177) | (5,309) | (58,412) |
| Total assets | 2,553,326 | 6,763 | 1,005,778 |
| For three months ended March 31, 2001 | | | |
| | | | |
| Revenue from continuing | | | |
| Operations | \$ 675,831 | - | - |
| Operating loss | (585,249) | (3,117) | (36,562) |
| Total assets | 3,146,529 | 34,123 | 1,450,740 |

F-9

Edgar Filing: XIN NET CORP - Form 10QSB

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

The information presented here should be read in conjunction with Xin Net Corp.'s consolidated financial statements and related notes. In addition to historical information, the following discussion and other parts of this document contain certain forward-looking information. When used in this discussion, the words "believes," "anticipates," "expects," and similar expressions are intended to identify forward-looking statements. Such statements are subject to certain risks and uncertainties, which could cause actual results to differ materially from those projected due to a number of factors beyond the Company's control. The Company does not undertake to publicly update or revise any of its forward-looking statements even if experience or future changes show that the indicated results or events will not be realized. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Readers are also urged to carefully review and consider the Company's discussions regarding the various factors, which affect its business, included in this section and elsewhere in this report.

LIQUIDITY AND CAPITAL RESOURCES

The Company had net cash, receivables and investments of \$947,202 at March 31, 2002.

The Company has no other capital resources other than the ability to use its common stock to achieve additional capital raising. It did not raise any additional capital during the first quarter of 2002. It has equipment of \$707,013 on the books, which is not necessarily liquid at such value. It has an investment in The Link Group, Inc. valued at \$824,652. Other than cash capital, its other assets would be illiquid.

At the end of the quarter, it had \$2,034,202 in current assets. It had Current liabilities of \$3,024,542, which included deferred revenues of \$1,818,888 and a security deposit of \$500,000 from the sale of its Internet Access Provision business in June 2001. (The Company is experiencing some delays in obtaining new funding; it plans to close the sale of its Internet Access Provision services when this issue is resolved).

The cash capital at the end of the quarter of \$883,384 will be used to fund continued operations, which management believes is adequate to satisfy its cash requirements for at least the next twelve months. The trend of operating losses could continue due to costs of equipment, design of new value-added services, start up operations for new locations and advertising & marketing which precede development of additional revenue for the Company.

Net cash flows used in operating activities decreased to \$173,097 in the first quarter in 2002 from \$419,133 in the corresponding quarter in 2001. The single most important item which contributed to this result was the decrease in net loss to \$108,531 in the first quarter in 2002, as compared to \$828,331 (\$596,216 due to continuing operations and \$232,115 due to discontinued operations) in first quarter 2001. Net cash flow used in investing increased to \$288,534 in first quarter 2002 as compared \$70,968 in first quarter 2001 primarily due to an investment of \$600,300 in The Link Group, Inc., combined with the repayment of a \$360,400 loan to the Company by ProtectServe Pacific Ltd. Purchases of equipment decreased to \$49,926 in first quarter 2002 from \$72,301 in first quarter 2001. Net cash flow used in financing activities decreased to \$15,056 in first quarter 2002, compared to \$20,365 in first quarter 2001.

Edgar Filing: XIN NET CORP - Form 10QSB

Changes in Financial Condition:

At the end of the first quarter 2002 Company assets had decreased to \$3,565,876 compared to \$3,753,612 at year-end 2001. The current assets totaled \$2,034,202 at the end of first quarter 2002 compared to \$2,839,441 at year-end 2001. Total liabilities at end of first quarter 2002 were \$3,024,542 compared to \$3,104,368 at year-end 2001. At March 31, 2002 the Company had \$883,384 in cash compared to \$1,360,071 at year-end 2001; approximately half of the cash used in the first quarter 2002 was due to the Company "net" investment in The Link Group, Inc. Net cash, investments and receivables at March 31, 2002 totaled \$947,202.

Need for Additional Financing:

The Company believes it has sufficient capital to meet its short-term cash needs, including the costs of compliance with the continuing reporting requirements of the Securities Exchange Act of 1934. But if losses continue it may have to seek loans or equity placements to cover longer term cash needs to continue operations and expansion. The Company signed a funding agreement with the iBanc Group, Inc. in November 2001. If and when this agreement comes to fruition, a sum of 5-6 million will be made available to the Company. There is no assurance, however, that such funds will become available.

No commitments to provide additional funds have been made by management or other stockholders. Accordingly, there can be no assurance that any additional funds will be available to the Company to allow it to cover operations expenses.

If future revenue declines, or operations are unprofitable, it will be forced to develop another line of business, or to finance its operations through the sale of assets it has, or enter into the sale of stock for additional capital, none of which may be feasible when needed. The Company has no specific management ability, nor financial resources or plans to enter any other business as of this date.

From the aspect of whether it can continue toward the business goal of maintaining and expanding the joint venture for internet services in China, it may use all of its available capital without generating a profit.

The effects of inflation have not had a material impact on its operation, nor is it expected to in the immediate future.

Although the Company is unaware of any major seasonal aspect that would have a material effect on the financial condition or results of operation, the first quarter of each fiscal year is always a financial concern. It is not uncommon for companies to shut down their operation or operate on a skeletal crew during the Chinese New Year holiday. Therefore in effect, the first quarter really has only two months for generating revenue.

Market Risk:

The Company's investments in The Link Group, Inc. will be subject to market volatility. It does not hold any derivatives or other investments that are subject to market risk. The carrying values of any financial instruments, approximate fair value as of those dates because of the relatively short-term maturity of these instruments which eliminates any potential market risk associated with such instruments.

Edgar Filing: XIN NET CORP - Form 10QSB

RESULTS OF OPERATIONS FOR THE QUARTER ENDED MARCH 31, 2002 AS COMPARED TO THE QUARTER ENDED MARCH 31, 2001.

Revenues in first quarter 2002 rose by 49% to \$1,008,590 in the form of net sales from its joint venture with Xin Hai Technology Ltd, as compared to net sales of \$675,831 in first quarter 2001. The Company had cost of revenues of \$395,585 in first quarter 2002, as compared to \$283,366 in first quarter 2001. Gross profit in first quarter 2002 was \$613,005 compared to \$392,465 in first quarter 2001. The Company incurred operating expenses of \$746,903 in first quarter 2002 compared to operating expenses of \$1,017,393 in first quarter 2001. Operating loss for first quarter 2002 decreased substantially to \$133,898 in contrast to the first quarter 2001 operating loss of \$624,928. The company had interest and equity income of \$25,367 in first quarter 2002 and \$28,712 in first quarter 2001. The net loss in first quarter 2002 was \$108,531 (\$0.01/share) compared to the net loss in first quarter 2001 of \$828,331 (\$0.04/share).

Revenues (excluding those generated by Internet Access Provision services, which the Company stopped providing as of June 2001) increased from \$675,831 in first quarter 2001 to \$1,008,590 in first quarter 2002, up 49%, as a result of the Company's continued efforts in expanding its customer base due to sales and marketing strategies in the areas of domain name registration and e-solutions services.

Operating expenses decreased to \$746,903 in first quarter 2002 from \$1,017,393 in first quarter 2001. This result, achieved against the backdrop of an increase in revenues of almost 50%, was made possible by the cost-cutting measures which the Company implemented throughout 2001. Except for amortization, which increased to \$57,029 in the first quarter of 2002 from \$46,287 in the corresponding quarter in 2001, all expense categories saw a decrease: advertising and promotion to \$30,955 from \$134,750; general and administrative to \$137,599 from \$160,605; rent to \$96,574 from \$117,609; salaries, wages and benefits to \$347,251 from \$424,453, and telephone and communications to \$77,535 from \$133,689.

Future Trends:

The Company will continue its cost-saving measures and ongoing efforts to increase revenues in order to achieve profitability. However the Company cannot assure that any profit on revenues can occur in the future. It may have to continue, through its joint venture business, to advertise and promote its services and develop additional value-added services. Operating losses may continue. If the Company acquires additional capital, for example through sale of stock in private placements or through investors exercising warrants, it may be able to advertise and promote its services more aggressively and expand its business more rapidly.

PART II

OTHER INFORMATION

- Item 1. Legal Proceedings - None.
- Item 2. Changes in securities - None.
- Item 3. Defaults upon senior securities - None.
- Item 4. Submission of matters to a vote of security holders - None.

Edgar Filing: XIN NET CORP - Form 10QSB

Item 5. Other information - None.

Item 6. Exhibits and reports on Form 8-K

(a) The following are filed as Exhibits to this Quarterly Report. The numbers refer to the Exhibit Table of Item 601 of Regulation S-K:

None.

(b) Reports on Form 8-K filed during the three months ended March 31, 2002. (incorporated by reference)

None.

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf of the undersigned thereunto duly authorized.

Dated: May 14, 2002

XIN NET CORP.

by: /s/ Ernest Cheung

Ernest Cheung, Secretary/Director