ION NETWORKS INC
Form 10QSB
November 14, 2002

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

FORM 10-QSB

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

For the quarterly period ended September 30, 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.

(Exact Name of Small Business Issuer in Its Charter)

Delaware	22-2413505
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

1551 South Washington Avenue Piscataway, New Jersey 08854

(Address of Principal Executive Offices)

(732) 529-0100

(Issuer's telephone number, including area code)

Check whether the issuer: (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No___

There were 24,875,500 shares of Common Stock outstanding as of November 8, 2002.

Transitional Small Business Disclosure Format:

Yes___ No X

ION NETWORKS, INC. AND SUBSIDIARIES

FORM 10-QSB

FOR THE QUARTER ENDED SEPTEMBER 30, 2002

PART I. FINANCIAL INFORMATION

PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL INFORMATION

The condensed consolidated financial statements included herein have been prepared by the registrant without audit pursuant to the rules and regulations of the Securities and Exchange Commission. Although the registrant believes that the disclosures are adequate to make the information presented not misleading, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. It is suggested that these condensed financial statements be read in conjunction with the audited financial statements and the notes thereto included in the registrant's Annual Report on Form 10-KSB , as amended, for the year ended March 31, 2002.

ION NETWORKS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	September 30, 2002	
ASSETS		
Current assets:		
Cash and cash equivalents..	$ 1,723,599	$
Accounts receivable, net of allowance for doubtful accounts of $202,626 and $149,999 respectively..................	929,468	
Inventory, net...	1,321,126	
Prepaid expenses and other current assets........................	232,629	
Related party notes receivable.................................	83,657	
Total current assets.......................................	4,290,479	
Restricted cash...	125,700	
Property and equipment at cost, net of accumulated depreciation of $2,965,949 and $2,684,152, respectively............	597,751	
Capitalized software, less accumulated amortization of $3,755,028 and $3,412,040, respectively.......................................	858,950	
Other assets..	71,442	
Total assets...	$ 5,944,322	$
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of capital leases................................	$ 74,426	$
Current portion of long-term debt................................	12,148	
Accounts payable...	1,076,810	
Accrued expenses...	345,595	
Accrued payroll and related liabilities..........................	293,874	
Deferred income..	176,292	
Sales tax payable..	118,829	
Other current liabilities..	102,909	
Total current liabilities.................................	2,200,883	
Long-term portion of capital leases...............................	106,754	
Long-term debt, net of current portion............................	-	
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, par value $.001 per share; Authorized Shares-1,000,000 at September 30, 2002 and March 31, 2002 Designated Shares- 200,000 at September 30, 2002 and none at March 31, 2002 Issued and Outstanding-166,835 September 30, 2002 and none at March 31, 2002..	167	
Common stock, par value $.001 per share; Authorized Shares-50,000,000 at September 30, 2002 and March 31, 2002 Issued and outstanding - 24,875,500 shares at September 30, 2002 and 25,138,000 at March 31, 2002................................	24,876	
Additional paid-in capital.......................................	44,585,740	
Notes receivable from officers...................................	(479,268)	
Deferred compensation..	-	
Accumulated deficit..	(40,503,210)	(
Accumulated other comprehensive income...........................	8,380	
Total stockholders' equity..	3,636,685	
Total liabilities and stockholders' equity..........................	$ 5,944,322	$

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

ION NETWORKS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	For the Three Months Ended September 30, 2002	For the Three Months Ended September 30, 2001	For the Six Months September 30, 2002	
Net sales	$ 1,522,336	$ 1,088,380	$ 2,482,468	$ 3
Cost of sales	557,564	572,576	914,068	1
Gross margin	964,772	515,804	1,568,400	1
Research and development expenses	280,893	158,622	516,202	
Selling, general and administration	1,614,473	2,250,262	3,751,441	4
Restructuring charges	154,370	-	154,370	
Depreciation and amortization	281,596	472,688	563,567	
Total operating expenses	2,331,332	2,881,572	4,985,580	5
Loss from operations	(1,366,560)	(2,365,768)	(3,417,180)	(4
Interest income	15,663	26,250	25,197	
Interest expense	(6,255)	(8,508)	(11,502)	
Loss before income tax expense	(1,357,152)	(2,348,026)	(3,403,485)	(4
Income tax expense	-	-	5,301	
Net loss	$ (1,357,152)	$ (2,348,026)	$ (3,408,786)	$ (4
PER SHARE DATA				
Net loss per share Basic and diluted	$ (0.06)	$ (0.13)	$ (0.15)	$
Weighted average number of common shares outstanding: Basic and diluted	22,608,273	18,203,301	22,604,408	18

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

ION NETWORKS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

FOR THE SIX MONTHS ENDED SEPTEMBER 30, 2002
(Unaudited)

	Convertible Preferred Stock		Common Stock	
	Shares	Par Value	Shares	Par Val
Balance April 1, 2002....................	-	-	25,138,000	$ 25,1
Net loss.................................	-	-	-	
Issuance of preferred stock..............	166,835	$ 167	-	
Issuance (Cancellation) of restricted stock......................	-	-	(262,500)	(2
Notes receivable from officers...........	-	-	-	
Deferred compensation....................	-	-	-	
Translation adjustments..................	-	-	-	
Balance September 30, 2002...............	166,835	$ 167	24,875,500	$ 24,8

	Accumulated Other Comprehensive Income	Notes Receivable from officers	Deferred Compensation
Balance April 1, 2002....................	$ 27,866	$ (549,914)	$ (62,893)
Net loss.................................	-	-	-
Issuance of preferred stock..............	-	-	-
Issuance (Cancellation) of restricted stock......................	-	85,322	-
Notes receivable from officers...........	-	(14,676)	-
Deferred compensation....................	-	-	62,893
Translation adjustments..................	(19,486)	-	-
Balance September 30, 2002...............	$ 8,380	$ (479,268)	-

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

ION NETWORKS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	FOR THE SIX MO SEPTEMB 2002
CASH FLOWS FROM OPERATING ACTIVITIES	
Net loss	$(3,408,786)
Adjustments to reconcile net loss to net cash used in operating activities:	
Depreciation and amortization	563,567
Asset impairments and other charges	(28,877)
Noncash stock-based compensation charges	62,893
Interest on Notes Receivable from Officers	(10,466)
Changes in operating assets and liabilities:	
Accounts receivable	591,762
Inventory	(297,000)
Prepaid expenses and other current assets	195,191
Accounts payable and accrued expenses	130,793
Accrued payroll and related liabilities	(59,716)
Deferred income	60,365
Sales tax payable	(69,606)
Other current liabilities	28,986
Net cash used in operating activities	(2,240,894)
CASH FLOWS FROM INVESTING ACTIVITIES	
Capital expenditures	(11,386)
Capitalized software expenditures	(274,916)
Related party notes receivable, net of repayments	-
Net cash generated (used) in investing activities	(286,302)
CASH FLOWS FROM FINANCING ACTIVITIES	
Principal payments on debt and capital leases	(65,679)
Issuance of preferred stock	285,303
Net cash generated (used) in financing activities	219,624
Effects of exchange rates on cash	(19,486)
Net decrease in cash	(2,327,058)
Cash and cash equivalents, beginning of period	4,050,657
Cash and cash equivalents, end of period	$ 1,723,599

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

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ION NETWORKS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS
September 30, 2002
(Unaudited)

NOTE 1 - CONDENSED CONSOLIDATED FINANCIAL STATEMENTS:

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.

The condensed consolidated balance sheet as of September 30, 2002, the condensed consolidated statements of operations for the three and six month periods ended September 30, 2002 and 2001, the condensed consolidated statements of cash flows for the six month periods ended September 30, 2002 and 2001 and the condensed consolidated statement of stockholders' equity for the six month period ended September 30, 2002, have been prepared by the Company without audit. In the opinion of management, all adjustments (which include only normal non-material recurring adjustments) necessary for the fair presentation of the Company's financial position, results of operations and cash flows at September 30, 2002 and 2001 have been made.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. It is suggested that these condensed consolidated financial statements be read in conjunction with the audited consolidated financial statements and notes thereto included in the annual report on Form 10-KSB as amended, for the year ended March 31, 2002.

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 September 30, 2002, we had an accumulated deficit of $40,503,210 and working capital of $2,089,596. We also realized a net loss of $3,408,786 for the six months ended September 30, 2002. Our existing working capital might not be sufficient to sustain our operations.

Our plans to overcome this condition include refocusing our sales efforts to include penetrating additional markets with our enterprise infrastructure security products, reducing expenses and raising additional equity capital. We have restructured and reorganized to reduce our operating expenses by the elimination of 13 employees during the quarter ended September 30, 2002, which is expected to reduce the Company's overhead expenses by approximately $960,000 ($80,000 per month) 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 direct sales. 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. We believe that our working capital as of September 30, 2002 will fund the Company's operations, as currently planned, through the quarter ended March 31, 2003. We believe that approximately $2,000,000 in additional capital will be needed in order to fund the Company's planned operations through December 2003. We plan to seek equity financing to provide funding for operations but the current market for equity financing may be weak. If we are not successful in increasing our revenue, reducing our expenses and 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.

Certain amounts in the financial statements for the three and six month periods ended September 30, 2002 have been reclassified to conform to the presentation of the financial statements for the quarter ended September 30, 2002.

NOTE 2 - RESTRICTED CASH:

Due to the expiration of the Company's $1,500,000 line of credit on September 30, 2000, the Company pledged $375,000 on September 7, 2000 as collateral on an outstanding letter of credit related to the required security deposit for the Company's Piscataway, New Jersey corporate headquarters facility. On November 9, 2001, the Company entered into an agreement with the landlord for its Piscataway, NJ facility to amend the Lease Agreement dated February 18, 1999. The amendment allowed the Company to use $250,000 of its restricted cash from the letter of credit towards the rent payments for 10 months starting January 2002. On January 10, 2002, the Landlord received the $250,000 from the letter of credit per the above mentioned lease amendment. The Company agreed to replenish the letter of credit by November 2003. Accordingly, $125,700 has been reflected as restricted cash as a non-current asset at September 30, 2002.

NOTE 3 - INVENTORY:

Inventory, net of allowance for obsolescence of $1,080,529 and $1,005,907 at September 30, 2002 and March 31, 2002, respectively, consists of the following:

	September 30, 2002	March 31, 2002
Raw materials	$ 196,321	$ 265,725
Work in process	908	2,161
Finished goods	1,123,897	756,240
Total	$1,321,126	$1,024,126

NOTE 4 - EARNINGS PER SHARE:

The computation of basic earnings per share is based on the weighted average number of common shares outstanding for the period. Diluted earnings per share is based on the weighted average number of common shares outstanding for the period plus common stock equivalents, comprised of the dilutive effect of convertible preferred stock outstanding on an as if converted basis and outstanding stock options and warrants.

The following is a reconciliation of the denominator used in the calculation of basic and diluted earnings per share:

	Three Months Ended 9/30/02	Three Months Ended 9/30/01	Six Months Ended 9/30/02	Six Months Ended 9/30/01
Weighted Average No. of Shares Outstanding	22,608,273	18,203,301	22,604,408	18,203,301
Incremental Shares for Common Stock Equivalents	467,240	12,308	578,323	18,624
Total	23,075,513	18,215,609	23,182,731	18,221,925

The potential incremental common shares above were excluded from the computation of diluted earnings per share for all periods presented, because their inclusion would have had an antidilutive effect on earnings per share due to the Company's net loss for each respective period.

NOTE 5 - COMPREHENSIVE INCOME:

The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 130, "Reporting Comprehensive Income". The following table reflects the reconciliation between net loss per the financial statements and comprehensive loss.

	Three Months Ended 9/30/02	Three Months Ended 9/30/01	Six Months Ended 9/30/02	Six Months Ended 9/30/01
Net loss	$(1,357,152)	$(2,348,026)	$(3,408,786)	$(4,339,942)
Effect of foreign currency translation	(209)	(10,064)	(19,486)	(12,877)
Comprehensive loss	$(1,357,361)	$(2,358,090)	$(3,428,272)	$(4,352,819)

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NOTE 6 - INCOME TAXES:

The Company has recorded a full valuation allowance against the federal and state net operating loss carry-forwards and a full valuation allowance against the foreign net operating loss carry-forwards and the research and development credit because management currently believes that it is more likely than not that substantially all of the net operating loss carry-forwards and credits will expire unutilized.

NOTE 7 - NEW 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 has adopted SFAS No.141 and SFAS No.142 and as a result there has been no material impact on its results of operations or financial position related to implementation of SFAS Nos. 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.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". SFAS No. 144 superceded Statement of Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets to be Disposed Of," and the accounting and reporting provisions relating to the disposal of a segment of a business in Accounting Principles Board Opinion No. 30. On April 1, 2002, The Company adopted SFAS No. 144 and as a result there has been no material impact on the Company's operating results or financial condition related to the implementation of SFAS No. 144.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" and nullified EITF Issue No. 94-3. SFAS No. 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred, whereas EITF No. 94-3 had recognized the liability at the commitment date to an exit plan. The Company is required to adopt the provisions of SFAS No. 146 effective for exit or disposal activities initiated after December 31, 2002. The Company is currently evaluating the impact of adoption of this statement.

NOTE 8 - RELATED PARTY TRANSACTIONS:

During April 2000, the Company made a loan (the "Loan") to the former Chief Executive Officer (the "Former CEO") of the Company in the amount of $750,000. At the time that the Loan was issued to the Former CEO in April 2000, the Company was contemplating a secondary public offering and potential mergers and acquisitions opportunities. As a result, the Company did not want the Former CEO to exercise his stock options. In consideration for not exercising his stock options at that time, the Company issued the Loan to him. At that time, the Company had sufficient cash and it was contemplated that the Loan would be repaid within one year. The Loan accrues interest at a rate of LIBOR plus 1%. The LIBOR plus one percent interest rate in April 2000 was 7.197% as compared to the first mortgage interest rate in April 2000 of 6.90% for a 1-year ARM, 7.97% for a 15-year FRM and 8.30% for a 30-year FRM. This Loan had an original maturity date of the earlier of April 2005 or thirty days after the Company for any reason no longer employed the Former CEO.

The Former CEO resigned his position at the Company effective September 29, 2000. On October 5, 2000, the Company entered into an agreement with the Former CEO pursuant to which the $750,000 promissory note for the Loan was amended to extend the due date to April 30, 2001, and to provide that interest on the note shall accrue through September 29, 2000 (the "Separation and Forbearance Agreement"). The Loan is collateralized by a first mortgage interest on the personal residence of the Former CEO. The Company agreed to extend the repayment date of the Loan so that the Former CEO would be able to repay the Loan to the Company by selling his personal residence. In addition to the Loan, pursuant to the terms of the Separation and Forbearance Agreement between the Company and the Former CEO, the Former CEO also agreed to reimburse the Company for certain expenses totaling $200,000, to be paid over a period of six months ending March 31, 2001. These certain expenses were incurred by the Former CEO as part of his personal expense account arrangement with the Company. During the year ended March 31, 2001, $50,000 of the amounts owed to the Company by the Former CEO was repaid and $22,000 has been recorded as a non-cash offset as a result of earned but unpaid vacation owed to the Former CEO. During the year ended March 31, 2002, $813,593 was repaid which included proceeds in the amount of $777,713 received by the Company on August 3, 2001 for the sale of the Former CEO's personal residence.

At September 30, 2002, the total amount owed to the Company by the Former CEO was approximately $152,474, which includes interest accrued through September 30, 2002. Of this amount approximately $68,817 has been recorded as a reserve against the note receivable. The net balance of $83,657 is classified as a related party notes receivable on the Company's consolidated balance sheet. Because the amounts were not paid by their respective maturity dates, interest is accruing at the default interest rate of 12% per annum.

The Company entered into a definitive Sublease Agreement with Multipoint Communications, LLC (the "Tenant") on April 17, 2002 to sublease approximately 5,400 square feet of its facility for a period of 24 months. The rental rate and the other material terms of the lease with Multipoint Communications, LLC ("Multipoint") were negotiated through a real estate broker and separate attorneys representing each party. The rental rate was established by prorating the amount of space leased by Multipoint by the current rent paid by the Company to its landlord. Given the current real estate market condition in the area, the Company believes that the terms of the lease with Multipoint are comparable to terms of leases that might have been obtained from a non-affiliate. The rent will be $5,200 per month for the first nine months and $10,400 per month for the last fifteen months, but with a 100% abatement for the first three months. As part of the rental payment the Company was to be issued shares totaling the value of $77,400, which shall be based on the per share price of the Tenant's common stock as priced in the first round of institutional financing (the "Financing") which was intended to close on or before June 30, 2002. These shares shall have the registration rights as other shares issued in the Financing. The Financing did not close by June 30, 2002, consequently, the Tenant shall pay the Company additional rent in the amount of $4,300 per month commencing on July 1, 2002. At September 30, 2002, future minimum lease payments due from the Tenant are approximately $220,500. The Chairman of the Board of Directors of the Company currently serves as the Chief Financial Officer of the Tenant.

NOTE 9 - STOCKHOLDERS' EQUITY:

On September 13, 2002 the Company received equity financing in the amount of $300,303 ($285,303, net of issuance cost) for the issuance of 166,835 unregistered shares of the Company's Preferred Stock at $1.80 per share. The Company has designated 200,000 of the 1,000,000 authorized shares of preferred stock as Series A Preferred Stock ("Preferred Stock"). Each share of Preferred Stock is convertible into 10 shares of the Company's common stock at the conversion price of $0.18 per share of common stock, which was the closing bid price of the Company's common stock on September 13, 2002. The Preferred Stock is non-voting, has a standard liquidation preference equal to its purchase price, and does not pay dividends. Proceeds of the equity financing will be used for working capital and general corporate purposes. All of the shares of Preferred Stock were purchased by directors and management of the Company. The purpose of the Preferred Stock Financing was to enable the Company to comply with the Nasdaq SmallCap Market's initial listing requirement of a minimum of $5,000,000 of stockholders' equity so that the Company was eligible for an additional 180-day grace period to attempt to regain compliance with the $1.00 minimum bid price requirement of the Nasdaq SmallCap Market (based on stockholders equity of $5,004,215 at June 30, 2002, adjusted on a proforma basis for the equity financing). The preferred stock is recorded in Stockholders' equity, net of issuance costs.

Effective October 2001, the Company approved and granted 2,900,000 shares of restricted stock to Messrs. Kam Saifi, Cameron Saifi, and David Arbeitel at fair value. The Restricted Shares are subject to a repurchase right which will permit the Company to repurchase any shares which have not yet vested at the effective date of termination of the officers' employment, as defined in their employment agreements, for an amount equal to the purchase price per share paid by the officers. The Company received a series of recourse interest bearing (5.46% on an annual basis) promissory notes for the value of the Restricted Shares to be repaid by the officers. The notes are to be repaid by the officers at the earlier of ten years or the date upon which the employees dispose of their shares or under certain circumstances, when the borrower's employment with the company terminates for any reason. The issuance of the restricted shares and the notes receivable due from the officers is recorded in the Company's financial statements. Only the vested portion of the shares has been included in the weighted average number of common shares outstanding at September 30, 2002. As of September 30, 2002 Mr. Kam Saifi owes approximately $272,027 (including approximately $14,027 of interest) for 2,000,000 Restricted Shares and; Mr. Cameron Saifi owes approximately $195,051 (including approximately $9,651 of interest)for 600,000 Restricted Shares. On September 29, 2002 , Mr. David Arbeitel separated employment from the Company. As a result, the note relating to Mr. Arbeitel's 37,500 vested Restricted Shares became due and payable and as of September 30, 2002, Mr Arbeitel owes approximately $12,190 (including approximately $602 of interest) with respect to such vested shares. On November 11, 2002, Mr. Arbeitel paid the Company $12,264 (including accrued interest of $676) in satisfaction of the note for the 37,500 vested shares. The Company and Mr. Arbeitel agreed to rescind the stock purchase transaction with respect to 262,500 of the unvested Restricted Shares thereby canceling the unpaid portion of the notes in an amount of $ 85,322 (including accrued interest of $4,210) relating to such unvested shares.

NOTE 10 - RESTRUCTURING CHARGES:

During the quarter ended September 30, 2002, the company announced the elimination of thirteen employees in order to reduce operating expenses. The elimination of these employees resulted in a charge during the quarter ended September 30, 2002 of $154,370 in severance and other related matters, of which all has been paid prior to September 30, 2002. As a result, the company will reduce its annual operating expenses by approximately $960,000 in salaries and employee benefits (approximately $ 80,000 per month).

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

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, those described in the Company's filings with the Securities and Exchange Commission included in its annual report Form 10-KSB, as amended, for the fiscal year ended March 31, 2002. Subsequent to the filing of our Form 10-KSB, as amended, for the fiscal year ended March 31, 2002, we hereby amended the risk factor, "Our Common Stock may be delisted from Nasdaq" with the following:

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 grace period, with respect to the Nasdaq National Market, and a 180-day grace 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 Nasdaq National Market's $1.00 continuing listing standard for a period of 30 consecutive trading days. On June 4, 2002, prior to the expiration of our 90-day cure period, we applied for a transfer to the Nasdaq SmallCap Market in order to take advantage of the longer 180-day grace period. On August 5, 2002, we received a letter from Nasdaq approving the transfer of the Company's securities from the Nasdaq National Market to the Nasdaq SmallCap Market, effective as of the opening of business on August 7, 2002. The Nasdaq SmallCap Market requires that the Company's securities close at $1.00 per share or more for a minimum of 10 consecutive trading days. If the price deficiency is cured during the 180-day grace period provided by the Nasdaq SmallCap Market by September 9, 2002, and we otherwise continue to comply with the Nasdaq National Market maintenance standards, we could then transfer back to the Nasdaq National Market. If we cannot demonstrate compliance with the Nasdaq SmallCap Market minimum bid price requirement by the end of the 180-day grace period, the Company may be eligible for an additional 180-day grace period, if we demonstrate compliance with the initial listing criteria for the Nasdaq SmallCap Market.

On September 17, 2002 we received a letter from Nasdaq granting us the additional 180 day grace period, or until March 10, 2003, to regain compliance with the minimum $1.00 bid price requirement of the Nasdaq SmallCap Market. The Company was granted this additional grace period after raising $300,303 in equity financing on September 13, 2002 thereby satisfying the Nasdaq SmallCap Market requirement of minimum stockholders' equity of $5 million (based on stockholders equity of $5,004,215 at June 30, 2002, adjusted on a pro forma basis for the equity financing).

In addition to maintaining compliance with other continuing listing requirements, if the Company's common stock does not close at $1.00 per share or more for a minimum of 10 consecutive trading days by March 10, 2003, it will be subject to delisting from the Nasdaq SmallCap Market.

There can be no assurance that we will satisfy the requirements for maintaining a Nasdaq SmallCap Market listing. If our Common Stock were to be excluded from Nasdaq, the price 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.

We may not be able to continue as a going concern.

The Company's working capital balance as of September 30, 2002 was $2,089,596 as compared to $5,040,922 at March 31, 2002. This decline in working capital was due to continued operating losses generated throughout the six months ended

September 30, 2002. We believe that our working capital as of September 30, 2002 will fund the Company's operations, as currently planned, through the quarter ended March 31,2003. We believe that approximately $2,000,000 in additional capital will be needed in order to fund the Company's planned operations through December 2003. We plan to seek equity financing to provide funding for operations but the current market for equity financing may be 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.

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.

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 securing additional funding in 2003 in order to continue operating as a going concern.

RESULTS OF OPERATIONS

For the three months ended September 30, 2002 compared to the same period in 2001

Net sales for the three months ended September 30, 2002, was $1,522,336 compared to Net sales of $1,088,380 for the same period in 2001, an increase of $ 433,956 or 40.0%. The increase in net sales was attributable to the sale of products with a higher per unit selling price during the quarter ending September 30, 2002 as compared to the comparable period of the prior year and continued management focus on sales execution. These factors, combined with the adverse impact of the September 11, 2001 tragedy on the quarter ended September 30, 2001, resulted in the growth in sales.

Cost of sales for the three months ended September 30, 2002 was $557,564 compared to $572,576 for the same period in 2001. Cost of sales as a percentage of net sales for the three months ended September 30, 2002 decreased to 36.6% from 52.6% for the same period in 2001, and therefore gross margin increased to 63.4% from 47.4% as compared to the prior year. This increase in gross margin was due to an improved revenue mix of higher margin products and services as well as the reduction of the Company's manufacturing overhead expenses.

Research and development expense, net of capitalized software development, for the three months ended September 30, 2002 was $280,893 compared to $158,622 for the same period in 2001 or an increase of $122,271 as compared to the comparable period of the prior year. The increase is primarily attributable to additional costs associated with the continued development effort to reengineer our hardware products to better serve the enterprise market and to lower the cost of goods sold.

Selling, general and administrative expenses ("SG&A") for the three months ended September 30, 2002 were $1,614,473 compared to $2,250,262 for the same period in 2001, a decrease of $635,789. This is the result of a corporate-wide effort to reduce operating expenses, which included the elimination of the seventeen employees during the quarter ended December 31, 2001 and an additional elimination of the thirteen employees in the quarter ended September 30, 2002 for a total labor cost reduction of $2,560,000 in annual salaries and employee benefits. The elimination of the thirteen employees during the quarter ended September 30, 2002 resulted in a restructuring charge during the quarter of $154,370 in severance and other related matters, all of which has been paid prior to September 30, 2002.

Depreciation and amortization expenses - amortization of capitalized software, goodwill and other acquisition related intangibles, and depreciation on equipment, furniture and fixtures - was $281,596 for the three months ended September 30, 2002 compared to $472,688 in the same period in 2001. The decrease was primarily the result of the three-year amortization period for the acquisitions of LeeMAH and Solcom Systems, Ltd coming to an end on March 31, 2002.

Net loss for the three months ended September 30, 2002 was $1,357,152 compared to a loss of $2,348,026 for the same period in 2001. This is a result of increase in sales, improved gross margins and the decrease in operating expenses resulting from the Company's corporate-wide effort to reduce operating expenses.

For the six months ended September 30, 2002 compared to the same period in 2001

Net sales for the six months ended September 30, 2002, was $2,482,468 compared to Net sales of $3,021,822 for the same period in 2001, a decrease of $539,354 or 17.8%. Despite the increase in sales for the three months ended September 30, 2002 versus the comparable period in 2001, Net Sales for the six month period ended September 30, 2002 declined as compared to the comparable period. This was due to lower unit sales, which was partially offset by a higher per unit selling price, because of the severe impact of the weakness of capital and IT spending particularly in the telecommunications service provider sector which adversely impacted the quarter ended June 30, 2002 and resulted in the decrease in net sales for the six month period ended September 30, 2002 as compared to the same period of the prior year.

Cost of sales for the six months ended September 30, 2002 was $914,068 compared to $1,430,176 for the same period in 2001. Cost of sales as a percentage of net sales for the six months ended September 30, 2002 decreased to 36.8% from 47.3% for the same period in 2001 and therefore gross margins improved from 52.7% to 63.2% as compared to the prior year. This increase in gross margin percentage was due to an improved revenue mix of higher margin products and services as well as reduction the Company's manufacturing overhead expenses.

Research and development expense, net of capitalized software development, for the six months ended September 30, 2002 was $516,202 compared to $508,497 for the same period in 2001. The slight increase in expenditures as compared to the same period for the prior year was due to the increase in costs associated with the continued development effort to reengineer our hardware products to better serve the enterprise market and to lower cost of goods sold, that was offset by the decrease in spending on third party consultants.

Selling, general and administrative expenses ("SG&A") for the six months ended September 30, 2002 were $3,751,441 compared to $4,535,285 for the same period in 2001 or a decrease of $783,844 as compared to the same period in 2001. This is the result of a corporate-wide effort to reduce operating expenses, which included the elimination of seventeen employees during the quarter ended December 31, 2001 and an additional elimination of thirteen employees in the quarter ended September 30, 2002 for a total labor cost reduction of $2,560,000 in annual salaries and employee benefits. The elimination of the thirteen employees during the quarter ended September 30, 2002 resulted in a restructuring charge during the quarter of $154,370 in severance and other related matters, all of which has been paid prior to September 30, 2002.

Depreciation and amortization expenses - amortization of capitalized software, goodwill and other acquisition related intangibles, and depreciation on equipment, furniture and fixtures - was $563,567 for the six months ended September 30, 2002 compared to $943,964 in the same period in 2001. The decrease was primarily the result of the three-year amortization period for the acquisitions of LeeMAH and Solcom Systems, Ltd coming to an end on March 31, 2002.

Net loss for the six months ended September 30, 2002 was $ 3,408,786 compared to a loss of $4,339,942 for the same period in 2001. Despite the reduction in sales as compared to the comparable period of the prior year, net loss for the year improved by $931,156 as a result of improved gross margins and the decrease in operating expenses resulting from the Company's corporate-wide effort to reduce operating expenses.

FINANCIAL CONDITION AND CAPITAL RESOURCES

The Company's working capital balance as of September 30, 2002 was $2,089,596 as compared to $5,040,922 at March 31, 2002. This decline in working capital was due to continued operating losses generated throughout the six months ended September 30, 2002. We believe that our working capital as of September 30, 2002 will fund the Company's operations, as currently planned, through the quarter ended March 31,2003. We believe that approximately $2,000,000 in additional capital will be needed in order to fund the Company's planned operations through December 2003. We plan to seek equity financing to provide funding for operations but the current market for equity financing may be 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 the six months ended September 30, 2002 was $2,240,894 compared to net cash used during the same period in 2001 of $3,329,222. The decrease in net cash used during the six months ended September 30, 2002 compared to the same period in 2001, was primarily due to improved gross margins and the reduction in operating expenses as a result of the corporate-wide effort to reduce expenses. The $2,240,894 net cash used in operating activities during the six-month period ended September 30, 2002 was primarily the result of operating losses incurred during this period which was partially offset by the cash generated from the net decrease in accounts receivable.

Net cash used in investing activities during the six months ended September 30, 2002 was $286,302 compared to net cash generated during the same period in 2001 of $568,449. This increase in cash used in investing activities during the six months ended September 30, 2002 as compared to the comparable period of 2001 was primarily the result of the collection of a related party note receivable in 2001, which did not occur in 2002. This was partially offset by an increase in capitalized software expenditures.

Net cash generated from financing activities during the six months ended September 30, 2002 was $219,624 compared to net cash used during the same period in 2001 of $60,392. This increase in cash generated from financing activities during the six months ended September 30, 2002 as compared to the comparable period of 2001 was primarily due to the proceeds generated from the preferred stock financing completed in September 2002.

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 September 30, 2002, we had an accumulated deficit of $40,503,210 and working capital of $2,089,596. We also realized net losses of $3,408,786 for the six months ended September 30, 2002. 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. We have restructured and reorganized to reduce our operating expenses by the elimination of thirteen employees during the quarter ended September 30, 2002, which is expected to reduce the Company's overhead expenses by approximately $960,000 ($80,000 per month) 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 direct sales. 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.

NEW 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 has adopted SFAS No. 141 and SFAS No. 142 and as a result there has been no material impact on its results of operations or financial position related to implementation of SFAS Nos. 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.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". SFAS No. 144 superceded Statement of Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets to be Disposed Of," and the accounting and reporting provisions relating to the disposal of a segment of a business in Accounting Principles Board Opinion No. 30. On April 1, 2002, the Company adopted SFAS No. 144 and as a result there has been no material impact on the Company's operating results or financial condition related to the implementation of SFAS No. 144.

In July 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" and nullified EITF Issue No. 94-3. SFAS No. 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred, whereas EITF No. 94-3 had recognized the liability at the commitment date to an exit plan. The Company is required to adopt the provisions of SFAS No. 146 effective for exit or disposal activities initiated after December 31, 2002. The Company is currently evaluating the impact of adoption of this statement.

ITEM 3. CONTROLS AND PROCEDURES.

The Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, performed an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures within 90 days before the filing date of this quarterly report. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect internal controls subsequent to their evaluation.

PART II. OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES.

On September 13, 2002 the Company received equity financing in the amount of $300,303 for the issuance of 166,835 unregistered shares of the Company's Series A Preferred Stock ("Preferred Stock") at $1.80 per share. Each share of

Preferred Stock is convertible into 10 shares of the Company's common stock at the conversion price of $0.18 per share of common stock, which was the closing bid price of the Company's common stock on September 13, 2002. The Preferred Stock is non-voting, has a standard liquidation preference equal to its purchase price, and does not pay dividends. Proceeds of the equity financing will be used for working capital and general corporate purposes. All of the shares of Preferred Stock were purchased by directors and management of the Company. The purpose of the Preferred Stock Financing was to enable the Company to comply with the Nasdaq SmallCap Market's initial listing requirement of a minimum of $5,000,000 of stockholders' equity so that the Company would receive an additional 180-day grace period to attempt to regain compliance with the $1.00 minimum bid price requirement of the Nasdaq SmallCap Market (based on stockholders equity of $5,004,215 at June 30, 2002, adjusted on a proforma basis for the equity financing).

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

On October 17, 2002, the Company held its 2002 Annual Meeting of Stockholders (the "2002 Meeting").

At the 2002 Meeting, the Company's Stockholders elected six directors to serve until the 2003 Annual Meeting of Stockholders and until their successors shall be elected and qualified. The vote with respect to the election of such directors was as follows:

	NAME	FOR	AUTHORITY WITHHELD
(a)	Stephen M. Deixler	17,985,231	369,723
(b)	Baruch Halpern	17,985,431	369,523
(c)	Alexander S. Stark, Jr	17,985,431	369,523
(d)	Frank S. Russo	17,985,431	369,523
(e)	Kam Saifi	17,985,431	369,523
(f)	Vincent Curatolo	17,985,431	369,523

In addition to electing the directors, the Company's Stockholders voted to approve an amendment to the Company's Certificate of Incorporation, as amended, to effect a reverse stock split of all of the outstanding shares of common stock at a ratio between one-to-two and one-to-ten, to be determined at the discretion of the Board of Directors. 17,986,291 votes were cast in favor of the approval of such amendment, 351,956 votes were cast in opposition to such approval, 16,707 votes abstained and no broker non-votes.

The Company's Stockholders also voted to approve the adoption of the 2002 Stock Incentive Plan. 17,570,813 votes were cast in favor of the approval of the 2002 Stock Incentive Plan, 752,282 votes were cast in opposition to such approval, 31,859 votes abstained and no broker non-votes.

The Company's Stockholders also voted to approve the ratification of the selection of Deloitte and Touche LLP as the Company's independent auditors. 18,265,262 votes were cast in favor of the ratification and selection of Deloitte and Touche LLP as the Company's independent auditors, 60,700 votes were cast in opposition to such approval, 28,992 votes abstained and no broker non-votes.

The Company's Stockholders also voted to approve the amendment to the Company's Certificate of Incorporation, as amended, to increase the number of shares of common stock that the Company is authorized to issue from 50,000,000 to 100,000,000, which would become effective upon the filing of a Certificate of Amendment of Amended and Restated Certificate of Incorporation with the Delaware Secretary of State. 17,718,156 votes were cast in favor of the approval of such amendment, 612,134 votes were cast in opposition to such approval, 24,664 votes abstained and no broker non-votes.

The Company's Stockholders also voted to approve the issuance of up to 35,000,000 shares of common stock or securities convertible into or exercisable for up to 35,000,000 shares of common stock (such as convertible preferred stock or warrants) or any of the foregoing in combination, at such prices and on such terms as may be approved by the Board of Directors; provided that such issuance(s) would (i) generate gross proceeds to the Company in an aggregate amount not to exceed $7,000,000, (ii) occur within three months of the date this proposal is approved by our stockholders, and (iii) be sold at market value or, if market conditions warrant, at prices no lower than (or having an exercise price no lower than) a 20% discount to the last bid price of the common stock on the day prior to the date that a binding agreement is entered into for the sale of such securities. 17,718,156 votes were cast in favor of the approval of such issuance, 628,152 votes were cast in opposition to such approval, 23,754 votes abstained and 12,495,713 of broker non-votes.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits:

Exhibit No.	Description
3.1	Certificate of Incorporation of the Company, as filed with the Secretary of State of the State of Delaware on August 5, 1998./(1)/
3.2	Certificate of Amendment of the Certificate of Incorporation, as filed with the Secretary of State of the State of Delaware on December 11, 1998./(1)/
3.3	Certificate of Amendment of the Certificate of Incorporation, as filed with the Secretary of state of the State of Delaware an October 12, 1999./(2)/
3.4	By-Laws of the Company./(1)/
3.5	Form of Specimen Common Stock Certificate of the Company./(3)/
4.1	1998 Stock Option Plan of the Company./(1)/
4.2	1998 U.K. Sub-Plan of the Company, as amended./(1)/
10.1	Lease Agreement dated February 18, 1999 by and between the Company and Washington Plaza Associates, L.P., as landlord. /(3)/
10.2	Business Park Gross Lease dated May 17, 1999 by and between the Company and Bedford Property Investors, Inc./(3)/
10.3	Supply Agreement dated October 20, 1998 by and between the Company and Lucent Technologies. (Incorporated by reference to the Company's Annual Report on form 10-KSB for the fiscal year ended March 31, 1999)./(3)/

10.4	OEM Purchase Agreement dated April 13, 1999 by and between the Company and the Hewlett-Packard Company./(3)/
10.5	Agreement dated as of December 19, 1994 by and between LeeMAH DataCom Security Corporation and Siemens Rolm Communications Inc./(3)/
10.6	Equipment Lease Agreements dated June 10, 1999 and May 5, 1999 by and between the Company and Siemens Credit Corporation. (Incorporated by reference to the Company's Annual Report on form 10-KSB for the fiscal year ended March 31, 1999)./(3)/
10.7	Equipment Lease Agreement dated June 17, 1999 by and between the Company and Lucent Technologies./(3)/

Exhibit No.	Description
10.8	(i) Non-negotiable Promissory Note in the principal amount of $750,000 issued by Stephen B. Gray to the Company./(4)/
	(ii) First Amendment to Promissory Note dated as of August 5, 2000 by and between the Company and Stephen B. Gray./(4)/
10.9	Line of Credit Agreement with United Nations Bank dated September 30, 1999./(4)/
10.10	Asset Purchase Agreement dated as of February 25, 1999 by and among the Registrant, LeeMAH and the Parent./(5)/
10.11	Assignment of Patents of LeeMAH dated February 25, 1999./(5)/
10.12	Assignment of Trademarks of LeeMAH dated February 25, 1999./(5)/
10.13	(i) Separation and Forebearance Agreement made as of October 5, 2000 between the Company and Stephen B. Gray./(6)/
	(ii) Promissory Note in the amount of $163,000 dated October 5, 2000 made by Stephen B. Gray to the Company./(6)/
10.14	Consulting Agreement entered into September 18, 2000 between the Company and Venture Consulting Group, Inc./(6)/
10.15	Materials and Services Contract dated January 16, 2001, between the Company and SBC Services, Inc./(7)/
10.16	Stock Purchase Agreement dated August 11, 2000 by and between the Company and the parties identified

	therein./(7)/
10.17	Form of Warrant Agreement dated July 17, 2001./(12)/
10.18	Form of Warrant Agreement dated January 4, 2002./(12)/
10.19	Form of Non-Qualified Stock Option Agreement dated March 19, 1999 by and between the Company's predecessor, Microframe, Inc. and its consultants./(12)/
10.20	Form of Non-Employee Director Stock Option Contract dated March 10, 1998 between the Company's predecessor, Microframe, Inc. and its non-employee directors./(12)/
10.21	Form of Non-Employee Director Stock Option Contract dated September 17, 1997 by and between the Company's predecessor, Microframe, Inc. and its non-employee directors./(12/)
10.22	Form of Non-Qualified Stock Option Agreement dated September 25, 1996 by and between the Company's predecessor, Microframe, Inc. and its employees./(12)/

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Exhibit No.	Description
10.23	Amended and Restated Non-Qualified Stock Option Agreement dated May 19, 1997 by and between the Company's Predecessor, Microframe, Inc. and its employees./(8)/
10.24	Employment Agreement dated October 4, 2001 between the Company and Kam Saifi./(10)/
10.25	Employment Agreement dated October 17, 2001 between the Company and Cameron Saifi./(11)/
10.26	Employment Agreement dated October 17, 2001 between the Company and David Arbeitel./(11)/
10.27	Sublease Agreement dated April 17, 2002 between the Company and Multipoint Communications, LLC./(13)/
10.28	Employment Agreement dated May 20, 2002 between the Company and Ted Kaminer./(14)/
10.29	Agreement and General Release dated August 15, 2002 between the Company and Ron Forster.*
10.30	Rescission Agreement dated September 29, 2002 between the Company and David Arbeitel.*
10.31	Separation Agreement and General Release dated October 31, 2002 between the Company and David Arbeitel.*
16.1	Letter dated June 28, 2001, from PricewaterhouseCoopers LLP to the Securities and Exchange Commission./(9)/

21.1	List of Subsidiaries./(13)/
99.1	Section 906 Certification of the Chief Executive Officer.*
99.2	Section 906 Certification of the Chief Financial Officer.*

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(1) Incorporated by Reference to the Company's Registration Statement on Form S-8 filed on April 22, 1999.
(2) Incorporated by reference to the Company's Registration Statement on Form S-8 filed on March 17, 2000.
(3) Incorporated by reference to the Company's Annual Report on Form 10-KSB for the fiscal year ended March 31, 1999.
(4) Incorporated by reference to the Company's Annual Report on Form 10-KSB filed on June 28, 2000.
(5) Incorporated by Reference to the Company's Current Report on Form 8-K filed on March 12, 1999.
(6) Incorporated by reference to the Company's quarterly report on Form 10-QSB filed on November 14, 2000.
(7) Incorporated by reference to the Company's annual report on Form 10-KSB filed on June 29, 2001.
(8) Incorporated by reference to the Company's Registration Statement on Form S-8 filed on November 17, 2000.
(9) Incorporated by reference to the Company's annual report on Form 10-KSB filed on June 29, 2001.
(10) Incorporated by Reference to the Company's Current Report on Form 8-K filed on October 23, 2001.
(11) Incorporated by Reference to the Company's Current Report on Form 8-K filed on October 24, 2001.
(12) Incorporated by reference to the Company's Annual Report on Form 10-KSB for the fiscal year ended March 31, 2002, as filed on July 1, 2002.
(13) Incorporated by reference to the Company's Annual Report on Form 10-KSB/A, Amendment No.2, for the fiscal year ended March 31, 2002, as filed on August 2, 2002.
(14) Incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed on August 14, 2002.
* Filed herewith

(b) Reports on Form 8-K:

On August 6, 2002, the Company filed a report on Form 8-K reporting the issuance of a press release announcing the results of the fiscal first quarter ended June 30, 2002.

On August 6, 2002, the Company filed a report on Form 8-K reporting the issuance of a press release announcing its transfer from the Nasdaq National Market to the Nasdaq SmallCap Market, effective August 7, 2002.

On August 14, 2002, the Company filed a report on Form 8-K reporting the filing of its quarterly report on Form 10-QSB accompanied by certifications by Kam Saifi, its Chief Executive Officer and Ted Kaminer, its Chief Financial Officer, in accordance with Section 906 of the Sarbanes-Oxley Act of 2002.

On August 21, 2002, the Company filed a report on Form 8-K reporting the filing of Amendment No. 3 of its annual report on Form 10-KSB for the year ended March 31, 2002 and Amendment No. 1 to its quarterly report on Form 10-QSB for the quarter ended June 30, 2002 accompanied by certifications by Kam Saifi, its

Chief Executive Officer and Ted Kaminer, its Chief Financial Officer, in accordance with Section 906 of the Sarbanes-Oxley Act of 2002.

On September 16, 2002, the Company filed a report on Form 8-K reporting its receipt of $300,303.00 in an equity financing for the issuance of 166,835 unregistered shares of the Company's Series A Preferred Stock at $1.80 per share.

On September 18, 2002, the Company filed a report on Form 8-K reporting the issuance of a press release announcing that it had been granted an additional 180-day grace period, or until March 10, 2003, to regain compliance with the $1.00 minimum bid price requirement of the Nasdaq SmallCap Market.

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SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: November 14, 2002

ION NETWORKS, INC.

/s/ Kam Saifi

Kam Saifi, Chief Executive Officer and President (Principal Executive Officer)

/s/ Ted Kaminer

Ted Kaminer, Chief Financial Officer and Vice President
(Principal Financial Officer and Principal Accounting Officer)

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CERTIFICATIONS

I, Kam Saifi, certify that:

1. I have reviewed this quarterly report on Form 10-QSB ION Networks, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in

this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

   a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
   b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within in 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
   c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were any significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

By: /s/ Kam Saifi

Kam Saifi, Chief Executive Officer and President

I, Ted Kaminer, certify that:

1. I have reviewed this quarterly report on Form 10-QSB ION Networks, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:

   a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
   b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within in 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
   c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   d) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   e) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were any significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: : November 14, 2002

By: /s/ Ted Kaminer

Ted Kaminer, Chief Financial Officer and Vice President (Principal Financial Officer and Principal Accounting Officer)

EXHIBIT INDEX

Exhibit No.	Description
3.1	Certificate of Incorporation of the Company, as filed with

	the Secretary of State of the State of Delaware on August 5, 1998./(1)/
3.2	Certificate of Amendment of the Certificate of Incorporation, as filed with the Secretary of State of the State of Delaware on December 11, 1998./(1)/
3.3	Certificate of Amendment of the Certificate of Incorporation, as filed with the Secretary of state of the State of Delaware an October 12, 1999./(2)/
3.4	By-Laws of the Company./(1)/
3.5	Form of Specimen Common Stock Certificate of the Company./(3)/
4.1	1998 Stock Option Plan of the Company./(1)/
4.2	1998 U.K. Sub-Plan of the Company, as amended./(1)/
10.1	Lease Agreement dated February 18, 1999 by and between the Company and Washington Plaza Associates, L.P., as landlord. /(3)/
10.2	Business Park Gross Lease dated May 17, 1999 by and between the Company and Bedford Property Investors, Inc./(3)/
10.3	Supply Agreement dated October 20, 1998 by and between the Company and Lucent Technologies. (Incorporated by reference to the Company's Annual Report on form 10-KSB for the fiscal year ended March 31, 1999)./(3)/
10.4	OEM Purchase Agreement dated April 13, 1999 by and between the Company and the Hewlett-Packard Company./(3)/
10.5	Agreement dated as of December 19, 1994 by and between LeeMAH DataCom Security Corporation and Siemens Rolm Communications Inc./(3)/
10.6	Equipment Lease Agreements dated June 10, 1999 and May 5, 1999 by and between the Company and Siemens Credit Corporation. (Incorporated by reference to the Company's Annual Report on form 10-KSB for the fiscal year ended March 31, 1999)./(3)/
10.7	Equipment Lease Agreement dated June 17, 1999 by and between the Company and Lucent Technologies./(3)/
10.8	(i) Non-negotiable Promissory Note in the principal amount of $750,000 issued by Stephen B. Gray to the Company./(4)/
	(ii) First Amendment to Promissory Note dated as of August 5, 2000 by and between the Company and Stephen B. Gray./(4)/

Exhibit No.	Description
10.9	Line of Credit Agreement with United Nations Bank dated

	September 30, 1999./(4)/
10.10	Asset Purchase Agreement dated as of February 25, 1999 by and among the Registrant, LeeMAH and the Parent./(5)/
10.11	Assignment of Patents of LeeMAH dated February 25, 1999./(5)/
10.12	Assignment of Trademarks of LeeMAH dated February 25, 1999. /(5)/
10.13	(i) Separation and Forebearance Agreement made as of October 5, 2000 between the Company and Stephen B. Gray./(6)/
	(ii)Promissory Note in the amount of $163,000 dated October 5, 2000 made by Stephen B. Gray to the Company./(6)/
10.14	Consulting Agreement entered into September 18, 2000 between the Company and Venture Consulting Group, Inc./(6)/
10.15	Materials and Services Contract dated January 16, 2001, between the Company and SBC Services, Inc./(7)/
10.16	Stock Purchase Agreement dated August 11, 2000 by and between the Company and the parties identified therein./(7)/
10.17	Form of Warrant Agreement dated July 17, 2001./(12)/
10.18	Form of Warrant Agreement dated January 4, 2002./(12)/
10.19	Form of Non-Qualified Stock Option Agreement dated March 19, 1999 by and between the Company's predecessor, Microframe, Inc. and its consultants./(12)/
10.20	Form of Non-Employee Director Stock Option Contract dated March 10, 1998 between the Company's predecessor, Microframe, Inc. and its non-employee directors./(12)/
10.21	Form of Non-Employee Director Stock Option Contract dated September 17, 1997 by and between the Company's predecessor, Microphone, Inc, and its non-employee directors./12/
10.22	Form of Non-Qualified Stock Option Agreement dated September 25, 1996 by and between the Company's predecessor, Microframe, Inc. and its employees./(12)/
10.23	Amended and Restated Non-Qualified Stock Option Agreement dated May 19, 1997 by and between the Company's predecessor, Microframe, Inc. and its employees./(8)/
10.24	Employment Agreement dated October 4, 2001 between the Company and Kam Saifi./(10)/
10.25	Employment Agreement dated October 17, 2001 between the Company and Cameron Saifi./(11)/
10.26	Employment Agreement dated October 17, 2001 between the Company and David Arbeitel./(11)/

Exhibit

No.	Description
10.27	Sublease Agreement dated April 17, 2002 between the Company and Multipoint Communications, LLC./(13)/
10.28	Employment Agreement dated May 20, 2002 between the Company and Ted Kaminer./(14)/
10.29	Agreement and General Release dated August 15, 2002 between the Company and Ron Forster.*
10.30	Rescission Agreement dated September 29, 2002 between the Company and David Arbeitel.*
10.31	Separation Agreement and General Release dated October 31,2002 between the Company and David Arbeitel.*
16.1	Letter dated June 28, 2001, from PricewaterhouseCoopers LLP to the Securities and Exchange Commission./(9)/
21.2	List of Subsidiaries./(13)/
99.1	Section 906 Certification of the Chief Executive Officer.*
99.2	Section 906 Certification of the Chief Financial Officer.*

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(1) Incorporated by Reference to the Company's Registration Statement on Form S-8 filed on April 22, 1999.
(2) Incorporated by reference to the Company's Registration Statement on Form S-8 filed on March 17, 2000.
(3) Incorporated by reference to the Company's Annual Report on Form 10-KSB for the fiscal year ended March 31, 1999.
(4) Incorporated by reference to the Company's Annual Report on Form 10-KSB filed on June 28, 2000.
(5) Incorporated by Reference to the Company's Current Report on Form 8-K filed on March 12, 1999.
(6) Incorporated by reference to the Company's quarterly report on Form 10-QSB filed on November 14, 2000.
(7) Incorporated by reference to the Company's annual report on Form 10-KSB filed on June 29, 2001.
(8) Incorporated by reference to the Company's Registration Statement on Form S-8 filed on November 17, 2000.
(9) Incorporated by reference to the Company's annual report on Form 10-KSB filed on June 29, 2001.
(10) Incorporated by Reference to the Company's Current Report on Form 8-K filed on October 23, 2001.
(11) Incorporated by Reference to the Company's Current Report on Form 8-K filed on October 24, 2001.
(12) Incorporated by reference to the Company's Annual Report on Form 10-KSB, for the fiscal year ended March 31, 2002, as filed on July 1, 2002.
(13) Incorporated by reference to the Company's Annual Report on Form 10-KSB/A, Amendment No.2, for the fiscal year ended March 31, 2002, as filed on August 2, 2002.
(14) Incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed August 14, 2002.
* Filed herewith