
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the quarterly period ended January 31, 2005.

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the transition period from _____ to _____.

Commission file number 000-26399



DELAWARE
(State of incorporation)

62-1482176
(I.R.S. Employer Identification No.)

4105 Royal Drive NW, Suite 100, Kennesaw, Georgia, 30144
(Address of principal executive office)

(770) 423-2200
(Telephone number)

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

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

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of the latest practicable date: 12,840,379 shares of Common Stock, \$.001 par value, as of February 28, 2005.

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EON COMMUNICATIONS CORPORATION
FORM 10-Q
QUARTER ENDED JANUARY 31, 2005

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PART I - FINANCIAL INFORMATION

ITEM 1. CONDENSED FINANCIAL STATEMENTS

eOn Communications Corporation
Consolidated Condensed Balance Sheets
January 31, 2005 and July 31, 2004
(Dollars in thousands)

	January 31, 2005	July 31, 2004
	<u>(unaudited)</u>	<u></u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 4,222	\$ 4,679
Marketable securities	4,200	4,200
Trade accounts receivable, net of allowance of \$747 and \$774, respectively	4,767	6,656
Trade accounts receivable – related party, net of allowance of \$77 and \$18 respectively	1,196	615
Notes receivable	237	528
Inventories	3,052	2,733
Other current assets	1,126	1,913
	<u>18,800</u>	<u>21,324</u>
Total current assets	18,800	21,324
Property and equipment, net	777	971
	<u>19,577</u>	<u>22,295</u>
Total Assets	\$ 19,577	\$ 22,295
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Trade accounts payable	\$ 3,929	\$ 5,431
Trade accounts payable – related party	1,750	2,049
Note payable – current	296	767
Deferred acquisition payment	1,038	1,078
Accrued expenses and other	2,138	2,284
	<u>9,151</u>	<u>11,609</u>
Total current liabilities	9,151	11,609
Minority interest	1,368	1,227
Stockholders' equity:		
Preferred Stock	—	—
Common stock	13	13
Additional paid-in capital	54,398	54,369
Treasury stock	(1,502)	(1,502)
Accumulated deficit	(43,851)	(43,421)
	<u>9,058</u>	<u>9,459</u>
Total stockholders' equity	9,058	9,459
	<u>19,577</u>	<u>22,295</u>
Total	\$ 19,577	\$ 22,295

See notes to condensed financial statements.

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eOn Communications Corporation
Consolidated Condensed Statements of Operations (Unaudited)
For the Three Months and Six Months Ended January 31, 2005 and 2004
(Dollars in thousands, except per share data)

	Three Months Ended January 31,		Six Months Ended January 31,	
	2005	2004	2005	2004
Net revenue – third parties	\$ 4,663	\$ 3,958	\$10,866	\$8,997
Net revenue – related party	790	—	1,054	—
Net revenue	5,453	3,958	11,920	8,997
Cost of revenues – third parties	2,509	1,591	5,972	3,691
Cost of revenues – related party	635	—	840	—
Cost of revenues	3,144	1,591	6,812	3,691
Gross profit	2,309	2,367	5,108	5,306
Operating expenses:				
Selling, general, and administrative	1,972	1,542	3,817	3,460
Research and development	775	717	1,641	1,393
Total operating expenses	2,747	2,259	5,458	4,853
(Loss) income from operations	(438)	108	(350)	453
Interest income	(35)	(17)	(71)	(32)
Interest expense	—	9	—	17
Other (income) expense, net	(39)	29	(30)	51
(Loss) income before income tax expense and minority interest	(364)	87	(249)	417
Income tax expense	38	—	42	—
(Loss) income before minority interest	(402)	87	(291)	417
Minority interest	126	—	139	—
Net (loss) income	\$ (528)	\$ 87	\$ (430)	\$ 417
Net (loss) income per common share:				
Basic and diluted	\$ (0.04)	\$ 0.01	\$ (0.03)	\$ 0.03

See notes to condensed financial statements

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eOn Communications Corporation
Consolidated Condensed Statements of Cash Flows (Unaudited)
For the Six Months Ended January 31, 2005 and 2004
(Dollars in thousands)

	Six Months Ended January 31,	
	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) income	\$ (430)	\$ 417
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	249	321
Minority interest	141	—
Allowance for doubtful accounts	(27)	298
Changes in net assets and liabilities:		
Trade accounts receivable	1,916	(741)
Inventories	(319)	(313)
Notes receivable	291	—
Other current assets	787	—
Trade accounts payable	(1,502)	518
Receivable/payable to affiliate	(880)	(73)
Accrued expenses and other	(146)	(326)
Net cash provided by operating activities	80	101
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(82)	(159)
Disposals of property and equipment	27	62
Cash used in business acquisition	(40)	—
Net cash used in investing activities	(95)	(97)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment of note payable	(471)	(333)
Proceeds from ESPP and stock option exercises	29	537
Net cash (used in) provided by financing activities	(442)	204
Net (decrease) increase in cash and cash equivalents	(457)	208
Cash and cash equivalents, beginning of period	4,679	3,221
Cash and cash equivalents, end of period	\$ 4,222	\$3,429

See notes to condensed financial statements.

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eOn Communications Corporation
Notes to Consolidated Condensed Financial Statements (Unaudited)
For the Three Months and Six Months Ended January 31, 2005 and 2004
(Dollars in thousands)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated condensed financial statements have been prepared by eOn Communications Corporation (“eOn” or the “Company”). It is management’s opinion that these statements include all adjustments, consisting of only normal recurring adjustments necessary to present fairly the financial position, results of operations, and cash flows as of January 31, 2005 and for all periods presented.

Principles of Consolidation – The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, and include the accounts of the company’s majority owned subsidiary, Cortelco Shanghai. All significant inter-company balances and transactions have been eliminated in consolidation.

Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. It is suggested that these condensed financial statements be read in conjunction with the financial statements and notes thereto as of July 31, 2004 and 2003 and for each of the three years in the period ended July 31, 2004, which are included in the Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Stock Compensation Plans

At January 31, 2005, the Company had three stock-based compensation plans for employees and an Employee Stock Purchase Plan (ESPP), which are more fully described in the Company’s Annual Report on Form 10-K for the year ended July 31, 2004. The Company accounts for those plans under the intrinsic value method, which follows the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under the stock compensation plans had an exercise price equal to or greater than the market value of the underlying common stock on the grant date. Further, the ESPP is a noncompensatory plan under APB Opinion No. 25, and, as such, no compensation cost was recognized with respect to the ESPP.

The following table illustrates the effect on net income (loss) and net income (loss) per share if the Company had applied the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee compensation:

	Three Months Ended January 31		Six Months Ended January 31,	
	2005	2004	2005	2004
	(Thousands of Dollars, excluding per share data)		(Thousands of Dollars, excluding per share data)	
Net (loss) income as reported	\$ (528)	\$ 87	\$ (430)	\$ 417
Deduct: Total stock-based compensation determined under fair value based method for all awards, net of tax	(92)	(132)	(184)	(259)
Pro forma net (loss) income	\$ (620)	\$ (45)	\$ (614)	\$ 158
Net (loss) income per share – basic and diluted:				
Net (loss) income per share – as reported	\$ (0.04)	\$ 0.01	\$ (0.03)	\$ 0.03
Net (loss) income per share – pro forma	\$ (0.05)	\$ (0.00)	\$ (0.05)	\$ 0.01

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The fair value of shares and options issued pursuant to our stock-based compensation plans at the grant date were calculated using the Black-Scholes option pricing model as prescribed by SFAS No. 123 generally using the following weighted average assumptions; dividend yield 0.0%, expected volatility 100%, average risk free interest rate approximately 4.25%, and expected life in years 7.

2. REVENUE RECOGNITION

Revenues from our Millennium and eQueue products are recognized only when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price to the customer is fixed or determinable, and collectibility is reasonably assured. Generally, revenue is recognized (1) upon shipment for equipment and software, (2) as work is performed for professional services, and (3) in equal periodic amounts over the term of the contract for software and hardware maintenance. The Company believes that its revenue recognition policies are compliant with Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements," and Statement of Position No. 97-2, "Software Revenue Recognition."

3. INCOME (LOSS) PER SHARE

The computations of basic and diluted income (loss) per share were as follows:

	Three Months Ended January 31,		Six Months Ended January 31,	
	2005	2004	2005	2004
(In thousands, except per share data)				
Basic and diluted income (loss) per share:				
Net (loss) income	\$ (528)	\$ 87	\$ (430)	\$ 417
Weighted average shares outstanding	12,836	12,469	12,898	12,350
Basic and diluted (loss) income per share	\$ (0.04)	\$ 0.01	\$ (0.03)	\$ 0.03

4. INVENTORIES

Inventories consist of the following:

	Jan 31, 2005	July 31, 2004
(In thousands)		
Raw materials and purchased components	\$ 473	\$ 723
Finished goods	2,579	2,010
Total inventories	\$3,052	\$2,733

5. PRODUCT WARRANTIES

The Company provides standard product warranties from the date of purchase. The costs of satisfying warranty claims have historically been comprised of materials and direct labor costs. The Company estimates the cost of satisfying warranty claims based on analysis of past claims experience. Quarterly evaluations of these estimates are performed, and any changes in estimate, which could potentially be significant, are included in earnings in the period in which the evaluations are completed.

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Information regarding the changes in the Company's aggregate product warranty accrual included in accrued expenses and other, for the six months ended January 31, 2005 and 2004 were as follows:

	Six Months Ended January 31,	
	2005	2004
	(in thousands)	
Beginning balance	\$ 361	\$ 283
Warranty cost incurred	(92)	(123)
Accruals for warranties issued during the period	122	134
	<u>\$ 391</u>	<u>\$ 294</u>

6. CHANGES IN STOCKHOLDERS' EQUITY

The following represents the changes in stockholders' equity for the six months ended January 31, 2005:

	(In thousands, except share data)						Total Stockholders' Equity
	Common Stock		Additional Paid-in Capital	Treasury Stock		Accumulated Deficit	
	Shares	Amount		Shares	Amount		
Balance at July 31, 2004	13,487,160	\$ 13	\$ 54,369	(676,900)	\$(1,502)	\$ (43,421)	\$ 9,459
Net loss and comprehensive loss	—	—	—	—	—	(430)	(430)
Issuance of common stock under employee stock plan	19,892	—	19	—	—	—	19
Issuance of common stock under equity incentive Plans	10,227	—	10	—	—	—	10
Balance at January 31, 2005	<u>13,517,279</u>	<u>\$ 13</u>	<u>\$ 54,398</u>	<u>(676,900)</u>	<u>\$(1,502)</u>	<u>\$ (43,851)</u>	<u>\$ 9,058</u>

7. COMMITMENTS AND CONTINGENCIES

At January 31, 2005, the Company had outstanding commitments for inventory purchases under open purchase orders of approximately \$705,000.

The Company is involved in various matters of litigation, claims, and assessments arising in the ordinary course of business. In the opinion of management, the eventual disposition of these matters will not have a material adverse effect on the financial statements.

8. EQUITY INCENTIVE PLANS

The status of the Company's stock option plans since August 1, 2004 is as follows:

	Number of Shares	Weighted Average Exercise Price
Options outstanding, August 1, 2004	1,631,470	\$ 4.21
Granted	65,000	1.14
Exercised	(10,227)	1.04
Cancelled	(64,814)	1.07
Options outstanding, January 31, 2005	<u>1,621,429</u>	<u>\$ 4.23</u>
Options exercisable, January 31, 2005	<u>1,106,104</u>	<u>\$ 5.06</u>
Exercise price range	<u>\$0.24-\$24.25</u>	
Options available for grant, January 31, 2005	511,864	

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9. TRADE ACCOUNTS RECEIVABLE – RELATED PARTY

Trade accounts receivable – related party, consists primarily of receivables from Shanghai Bell, an entity related through common ownership. During the three months ended January 31, 2005 the company recorded a net additional receivable of \$647 thousand.

10. ACQUISITION OF CORTELCO SHANGHAI TELECOM EQUIPMENT COMPANY

On June 1, 2004, eOn acquired a controlling interest in Cortelco Shanghai Telecom Equipment Company (“Cortelco Shanghai”), a provider of fiber optic transmission equipment, data communications systems, and network management software in China.

Under the terms of the agreement, eOn acquired all of the stock of Cortelco China Corp, a California corporation that owns a 54.14% ownership interest in Cortelco Shanghai, from Cortelco Systems Holding Corporation (“CSHC”). CSHC received 157,167 shares of eOn common stock valued at \$321,250. The agreement anticipated that up to an additional 471,501 shares may be issued over the next four fiscal quarters if Cortelco Shanghai attained specified revenue targets as set forth in the purchase agreement.

The agreement specifies revenue targets for sales of eQueue products in China during the initial 12 month period following the close of the acquisition. From June 1, 2004 through January 31, 2005, eQueue revenues in China were \$810,000. The Agreement provides that if a \$2,000,000 revenue target is not met by May 31, 2005, either eOn or CSHC has the option to elect to unwind the acquisition. On March 14, 2005, eOn and CSHC executed a Letter Agreement eliminating this option in the agreement and agreed to further amend the agreement to fairly reflect a revised revenue growth plan and extend the time period in which CSHC will have an opportunity to receive eOn stock if the earnout thresholds are met.

11. SEGMENT INFORMATION

The company is comprised of two principal business segments: eOn US and Cortelco Shanghai. The eOn US business segment designs, develops and markets communication products for customer contact centers and other applications and offers a traditional voice-switching platform. Cortelco Shanghai provides fiber optic transmission equipment, data communications systems, and network management software. There is no overlap in operational management reporting or of decision making authority between the two segments as defined. Following is a tabulation of business segment information for the three and six months ended January 31, 2005.

	For the Quarter Ended January 31, 2005			
	eOn US	Cortelco Shanghai	Elimination	Consolidated
	(In thousands)			
Revenues from customers	\$ 2,553	\$ 2,900	\$ —	\$ 5,453
Business segment net income (loss)	\$ (676)	\$ 148	\$ —	\$ (528)
Business Segment Assets at January 31, 2005	\$12,510	\$ 8,362	\$ (1,295)	\$ 19,577

	For the Six Months Ended January 31, 2005			
	eOn US	Cortelco Shanghai	Elimination	Consolidated
	(In thousands)			
Revenues from customers	\$ 7,124	\$ 4,796	\$ —	\$ 11,920
Business segment net income (loss)	\$ (594)	\$ 164	\$ —	\$ (430)
Business Segment Assets at January 31, 2005	\$12,510	\$ 8,362	\$ (1,295)	\$ 19,577

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

This report contains forward-looking statements within the meaning of the federal securities laws. Forward-looking statements are those that express management's views of future events, developments, and trends. In some cases, these statements may be identified by terminology such as "may," "will," "should," "expects," "plans," "intends," "anticipates," "believes," "estimates," "predicts," "potential," or "continue" or the negative of such terms and other comparable expressions. Forward-looking statements include statements regarding our anticipated or projected operating performance, financial results, liquidity and capital resources. These statements are based on management's beliefs, assumptions, and expectations, which in turn are based on the information currently available to management. Information contained in these forward-looking statements is inherently uncertain, and our actual operating performance, financial results, liquidity, and capital resources may differ materially due to a number of factors, most of which are beyond our ability to predict or control. Factors that may cause or contribute to such differences include, but are not limited to, eOn's ability to compete successfully in its industry and to continue to develop products for new and rapidly changing markets. We also direct your attention to the risk factors affecting our business that are discussed below. eOn disclaims any obligation to update any of the forward-looking statements contained in this report to reflect any future events or developments. The following discussions should be read in conjunction with our condensed financial statements and the notes included thereto.

Overview

We design, develop and market next-generation communications servers which integrate and manage voice, email and Internet communications for customer contact centers and other applications. We also offer a traditional voice-switching platform for small and medium-sized installations. We also offer fiber optic transmission equipment, data communications systems, and network management software through our subsidiary Cortelco Shanghai Telecom Equipment Company.

Net revenues in quarters ending January 31 usually decline from the previous quarter, reflecting seasonal factors that affect some of our customers. U.S. government customers typically make substantial purchases during quarters ending October 31, the last quarter of the government's fiscal year, and these purchases decline significantly in the following quarter. Customers in such markets as contact centers, education, and retail also have seasonal buying patterns and do not purchase substantial amounts of equipment during the quarters ending January 31.

Critical Accounting Policies

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties and that could potentially result in materially different results under different assumptions and conditions. We believe that our critical accounting policies are limited to those described below. For a detailed description of our accounting policies, see Note 2, "Summary of Significant Accounting Policies," in Part II, Item 8, "Consolidated Financial Statements and Supplementary Data," of our Annual Report on Form 10-K for the year ended July 31, 2004.

- **Product Warranties** – We provide our customers with standard product warranties from the date of purchase. The costs of satisfying warranty claims have historically been comprised of materials and direct labor costs. We estimate the costs of satisfying warranty claims based on analysis of past claims experience. We perform quarterly evaluations of these estimates, and any changes in estimate, which could potentially be significant, are included in earnings in the period in which the evaluations are completed.
- **Inventory Obsolescence** – We carry inventories at the lower of cost or market. This policy depends on the timely identification of those items included in inventory whose market price may have declined below carrying value, such as slow-moving or obsolete items, and we record any necessary valuation reserves. We perform an analysis of slow-moving or obsolete inventory on a quarterly basis, and any necessary valuation reserves, which could potentially be significant, are included in earnings in the period in which the evaluations are completed.
- **Allowance for Doubtful Accounts** – We typically grant standard credit terms to customers in good credit standing. As a result, we must estimate the portion of our accounts receivable that are uncollectible and record any necessary valuation reserves. We generally reserve for estimated uncollectible accounts on a customer-by-customer basis,

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which requires us to make judgments about each individual customer's ability and intention to fully pay balances payable to us. We make these judgments based on our knowledge of and relationship with our customers, and we update our estimates on a monthly basis. Any changes in estimate, which can be significant, are included in earnings in the period in which the change in estimate occurs.

- **Deferred Taxes** – We recognize deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. Because of substantial losses in prior years, primarily during the years 2000 through 2002, the Company has available net operating loss (“NOL”) carryforwards of \$17.6 million.

Accounting principles generally accepted in the United States require the recording of a valuation allowance against the net deferred tax asset associated with this NOL and other timing differences if it is “more likely than not” that the Company will not be able to utilize the NOL to offset future taxes. Due to the size of the NOL carryforward in relation to the Company's taxable income in recent years and to the continuing uncertainties surrounding future earnings, management has not recognized any of its net deferred tax asset. Because this asset has been offset by a valuation allowance, the Company currently provides for income taxes only to the extent of expected cash payments of taxes, primarily state income taxes, for current income.

Should the Company's earnings trend cause management to conclude that it is more likely than not the Company will realize all or a material portion of the NOL carryforward, management would record the estimated net realizable value of its deferred tax asset at that time. The Company would then provide for income taxes at a rate equal to its combined federal and state effective rates, which would approximate 39% under current tax rates. Subsequent revisions to the estimated net realizable value of the deferred tax asset could cause the provision for income taxes to vary significantly from period to period, although the Company's cash tax payments would remain unaffected until the benefit of the NOL is utilized.

Three Months Ended January 31, 2005 and 2004

Net Revenues. Total revenues increased 37.7% to \$5.5 million in the quarter ended January 31, 2005 from \$4.0 million in the quarter ended January 31, 2004. The increase from Q2 2004 to Q2 2005 resulted from the inclusion of Cortelco Shanghai revenues of \$2.9 million partially offset by \$1.5 million combined decline in Millennium and eQueue revenues. Revenues from related parties in the quarter ended January 31, 2005 was \$0.8 million compared to \$0.0 in the prior year quarter.

Cost of Revenues and Gross Profit. Cost of revenues consist primarily of purchases from our contract manufacturers and other suppliers and costs incurred for final assembly of our systems. Gross profit decreased 2.5% to \$2.3 million in the quarter ended January 31, 2005 from \$2.4 million in the quarter ended January 31, 2004, primarily due to the decrease in Millennium revenues. Gross margin decreased to 42.34% in the quarter ended January 31, 2005 compared with gross margin of 59.8% in the quarter ended January 31, 2004. This decrease was primarily due to the inclusion of Cortelco Shanghai operations which have lower margins. Related party cost of revenues was \$0.6 million in the quarter ended January 31, 2005 compared to \$0.0 in the prior year quarter.

Selling, General and Administrative. Selling, general and administrative expenses consist primarily of salaries and benefit costs, advertising and trade show related costs, and facilities and other overhead expenses incurred to support our business. Selling, general and administrative expenses increased 28.1% to \$2.0 million in the quarter ended January 31, 2005, from \$1.5 million in the quarter ended January 31, 2004. The increase was due to the inclusion of Cortelco Shanghai expenses partially offset by a reduction in domestic expenses of \$116 thousand associated with the Company's cost-cutting initiatives.

Research and Development. Research and development expenses consist primarily of personnel and related facility costs for our engineering staff. Research and development expenses were relatively unchanged at \$0.7 million in the quarters ended January 31, 2005 and 2004.

Interest and other income and expense. Interest income was \$35 thousand in the current quarter, as compared to \$17 thousand in the quarter ended January 31, 2004. Other income was \$39 thousand in the current quarter compared to other expense of \$29 thousand in the prior year period.

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Six Months Ended January 31, 2005 and 2004

Net Revenues. Total revenues increased 32.5% to \$11.9 million in the six months ended January 31, 2005 from \$9.0 million in the six months ended January 31, 2004. The increase resulted primarily from the inclusion of Cortelco Shanghai revenues of \$4.8 million partially offset by a combined decrease in Millennium and eQueue revenues. Revenue to related parties was \$1.1 million in the six months ended January 31, 2005 compared to \$0.0 in the prior year period.

Cost of Revenues and Gross Profit. Cost of revenues consist primarily of purchases from our contract manufacturers and other suppliers and costs incurred for final assembly of our systems. Gross profit decreased 3.7% to \$5.1 million in the six months ended January 31, 2005 from \$5.3 million in the six months ended January 31, 2004, primarily due to the lower level of Millennium revenues and the inclusion of Cortelco Shanghai operations which have a lower margin. Gross margin decreased to 42.9% in the six months ended January 31, 2005 from 59.0% in the six months ended January 31, 2004, due to the inclusion of lower margin Cortelco Shanghai operations. Related party cost of goods sold was \$0.8 million in the six months ended January 31, 2005 compared to \$0.0 in the prior year period.

Selling, General and Administrative. Selling, general and administrative expenses consist primarily of salaries and benefit costs, advertising and trade show related costs, and facilities and other overhead expenses incurred to support our business. Selling, general and administrative expenses increased 10.4% to \$3.8 million in the six months ended January 31, 2005, from \$3.5 million in the six months ended January 31, 2004. The increase was primarily due the inclusion of Cortelco Shanghai expenses of \$712 thousand partially offset by a reduction in domestic spending associated with the Company's cost-cutting initiatives.

Research and Development. Research and development expenses consist primarily of personnel and related facility costs for our engineering staff. Research and development expenses increased 17.8% to \$1.6 million in the six months ended January 31, 2005 from \$1.4 million in the six months ended January 31, 2004. The increase in spending was primarily due to the company focus on product development for future generation products.

Interest and other income and expense. Interest income was \$71 thousand in the current six months, as compared to \$32 thousand in the six months ended January 31, 2004. The increase was primarily due to higher interest rates earned on investments in the current period in comparison to the prior year period. Interest expense was \$0 thousand in the current six month period compared to \$17 thousand in the prior year period. The decrease was due to the expiration of the company's obligations associated with the termination of the lease on the Memphis facility. Other income was \$30 thousand in the current six months and other expense was \$51 thousand in the prior year period.

LIQUIDITY AND CAPITAL RESOURCES

As of January 31, 2005, we had cash and cash equivalents of \$4.2 million, \$4.2 million in short term investments, and a working capital balance of \$9.6 million. Our short term investments are primarily invested in taxable auction rate securities with frequent rate resets.

Our operating activities resulted in net cash inflows of \$0.1 million in each of the six months ended January 31, 2005 and 2004. The net operating cash inflow for the current period was primarily the result of a reduction in accounts receivable partially offset by a reduction in accounts payable and a net loss for the period. The net operating cash inflow for the prior year period was primarily the result of our net income (adjusted for non-cash items) and increases in accounts payable, offset by increases in accounts receivable and inventories and a decline in accrued expenses.

Our investing activities resulted in a cash outflow of \$0.1 million for each of the six months ended January 31, 2005 and 2004. Cash used in investing activities in the current period consisted entirely of \$0.1 million in net capital expenditures. Cash used in investing activities in the prior period consisted entirely of \$0.1 million in net capital expenditures.

Our financing activities resulted in a cash outflow of \$0.4 million for the six months ended January 31, 2005, and a cash outflow of \$0.2 million for the six months ended January 31, 2004. Cash used by financing activities in the current period was primarily due to the reduction of notes payable at Cortelco Shanghai. Cash provided by financing activities in the prior period consisted of \$0.5 million in proceeds from stock option exercises and purchases under the Employee Stock Purchase Plan, offset by payments against our outstanding note payable of \$0.3 million.

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We believe that our available funds will satisfy our projected working capital and capital expenditure requirements for at least the next twelve months. To the extent future revenues are not realized or we grow more rapidly than expected, we may need additional cash to finance our operating and investing activities.

COMMITMENTS AND CONTINGENCIES

At January 31, 2005, the Company had outstanding commitments for inventory purchases under open purchase orders of approximately \$705,000.

The Company is involved in various matters of litigation, claims, and assessments arising in the ordinary course of business. In the opinion of management, the eventual disposition of these matters will not have a material adverse effect on the financial statements.

ADDITIONAL RISK FACTORS THAT MAY AFFECT FUTURE RESULTS OF OPERATIONS

The following risk factors and other information contained in this report should be carefully considered. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that are not currently known to us or that we currently deem immaterial also may impair our business operations. If any of the following risks actually occurs, our business, financial condition, and operating results could be materially adversely affected.

In addition to the other information included in this report, the following factors should be considered in evaluating our business and future prospects.

Fluctuations in our quarterly operating results could cause our stock price to decline.

Future operating results are likely to fluctuate significantly from quarter to quarter. Factors that could affect our quarterly operating results include:

- delays or difficulties in introducing new products;
- increasing expenses without commensurate revenue increases;
- variations in the mix of products sold;
- variations in the timing or size of orders from our customers;
- declining market for traditional private branch exchange (PBX) equipment;
- delayed deliveries from suppliers; and
- price decreases and other actions by our competitors.

Our quarterly operating results are also likely to fluctuate due to seasonal factors. Some of our vertical markets, such as the U.S. government, educational and retail buyers, follow seasonal buying patterns and do not make substantial purchases during the quarters ending January 31. Thus, revenues in the quarters ending January 31 are often lower than in the previous quarters. Because of these and other factors, our operating results may not meet expectations in some future quarters, which could cause our stock price to decline.

Our communications servers face intense competition from many companies that have targeted our markets.

The competitive arena for our products is changing very rapidly and we face intense competition in our markets. Well-established companies and many emerging companies are scrambling to develop products to improve customer service in e-commerce. While the industry remains fragmented, it is rapidly moving toward consolidation, driven by both emerging companies' desires to expand product offerings and resources and established companies' attempts to acquire new technology and reach new market segments. A number of emerging companies have completed initial public offerings, while many more remain private. More established competitors, as well as those emerging companies that have completed initial public offerings, currently have greater resources and market presence than we do. Additionally, a number of our current and potential competitors have recently been acquired by larger companies who seek to enter our markets.

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We expect competition to intensify as competitors develop new products, new competitors enter the market, and companies with complementary products enter into strategic alliances.

Our current and potential competitors can be grouped into the following categories:

- contact center vendors, such as Avaya, Nortel Networks, Aspect Communications, and Rockwell;
- data communication equipment suppliers, such as Cisco Systems and 3COM;
- email management and web center software suppliers, such as eGain, Kana Communications, and Live Person;
- voice communications equipment suppliers, such as Nortel Networks, Avaya, Mitel, NEC, Toshiba, and Siemens and
- optical transmission suppliers, such as Huawei, Alcatel, Optel, Zhongxing and Datang

Many of our current and potential competitors have significantly greater financial, technical, marketing, customer service and other resources, greater name and brand recognition and a larger installed customer base than we do. Therefore, our competitors may be able to respond to new or emerging technologies and changes faster than we can. They may also be able to devote greater resources to the development, promotion and sale of their products.

Actions by our competitors could result in price reductions, reduced margins and loss of market share, any of which would damage our business. We cannot assure you that we will be able to compete successfully against these competitors.

If we cannot expand our indirect sales channel to sell our eQueue products, our ability to generate revenue would be harmed.

We sell our eQueue communications servers both directly and indirectly through dealers and value added resellers that have experience in data as well as voice communications. We may not be able to expand this indirect sales channel. In addition, new distribution partners may devote fewer resources to marketing and supporting our products than to our competitors' products and could discontinue selling our products at any time in favor of our competitors' products or for any other reason.

The lengthy sales cycles of some of our products and the difficulty in predicting the timing of our sales may cause fluctuations in our quarterly operating results.

The uncertainty of our sales cycle makes the timing of sales difficult to predict and may cause fluctuations in our quarterly operating results. Our sales cycles generally vary from four to twelve months for our eQueue products and from one to six months for our Millennium voice switching platform. The purchase of our products may involve a significant commitment of our customers' time, personnel, and financial and other resources. Also, it is difficult to predict the timing of indirect sales because we have little control over the selling activities of our dealers and value added resellers.

We incur substantial sales and marketing expenses and spend significant management time before customers place orders with us, if at all. Revenues from a specific customer may not be recognized in the quarter in which we incur related sales and marketing expense, which may cause us to miss our revenues or earnings expectations.

Unanticipated difficulties in integrating our recent acquisition of Cortelco Shanghai could harm our business.

On June 1, 2004 eOn purchased a controlling interest in Cortelco Shanghai. Cortelco Shanghai provides telecommunications products in China, including fiber optic transmission equipment, data communications systems, and network management software. eOn's future operating results may be adversely affected if we are not able to realize operating efficiencies and sales opportunities as a result of this acquisition.

We face many risks from expanding into foreign markets.

The Company expects to increase sales to customers outside of the United States and establish additional distribution channels in Asia. However, foreign markets for our products may develop more slowly than currently anticipated. eOn may not be able to successfully establish international distribution channels, or may not be able to hire the additional personnel necessary to support such distribution channels.

Our future results could be harmed by economic, political, regulatory and other risks associated with international sales and operations.

Because our growth initiatives include expansion into foreign markets, we are subject to the risks of conducting business outside of the United States, including:

- changes in a specific country's or region's political or economic conditions;

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- trade protection measures and import or export licensing requirements;
- potentially negative consequences from changes in tax laws;
- difficulty in managing widespread sales and customer service operations; and
- less effective protection of intellectual property.

Our products must respond to rapidly changing market needs and integrate with changing protocols to remain competitive.

The markets for our products are characterized by rapid technological change, frequent new product introductions, uncertain product life cycles and changing customer requirements. If we are not able to rapidly and efficiently develop new products and improve existing products to meet the changing needs of our customers and to adopt changing communications standards, our business, operating results and financial condition would be harmed.

Key features of our products include integration with standard protocols, computer telephony integration and automatic call distribution applications and protocols, operating systems and databases. If our products cannot be integrated with third-party technologies or if they do not respond to changing market needs, we could be required to redesign our products. Redesigning any of our products may require significant resources and could harm our business, operating results and financial condition.

If we are not able to sustain our Millennium voice switching platform revenues, our business, operating results and financial condition could be harmed.

We may not be able to sustain our Millennium revenues because the traditional private branch exchange (PBX) market, which accounts for a substantial portion of our Millennium revenues, is declining. One reason for the decline of the traditional PBX market is the emergence of voice switching platforms based on standard PCs. If we are not able to grow or sustain our Millennium voice switching platform revenues, our business, operating results and financial condition could be harmed.

In addition, a significant portion of Millennium revenues are derived from dealers and value added resellers who have no obligation to sell our products. Therefore, dealers and value added resellers could discontinue selling our products at any time in favor of our competitors' products or for any other reason. A reduction or loss of orders from our dealers and value added resellers could harm our business, operating results and financial condition.

Delayed deliveries of components from our single source suppliers or third-party manufacturers could reduce our revenues or increase our costs.

We depend on sole source suppliers for certain components, digital signal processors and chip sets, and voice processor boards. Interruptions in the availability of components from our key suppliers could result in delays or reductions in product shipments, which could damage our customer relationships and harm our operating results. Finding alternate suppliers or modifying product designs to use alternative components may cause delays and expenses. Further, a significant increase in the price of one or more third-party components or subassemblies could reduce our gross profit.

We depend upon our primary contract manufacturers ACT Electronics, Innovative Circuits, and Clover Electronics. We may not be able to deliver our products on a timely basis if any of these manufacturers fail to manufacture our products and deliver them to us on time. In addition, it could be difficult to engage other manufacturers to build our products. Our business, results of operations and financial condition could be harmed by any delivery delays.

We may be unable to hire and retain engineering and sales and marketing personnel necessary to execute our business strategy.

Competition for highly qualified personnel is intense due to the limited number of people available with the necessary technical skills, and we may not be able to attract, assimilate or retain such personnel. If we cannot attract, hire and retain sufficient qualified personnel, we may not be able to successfully develop, market and sell new products.

Our business could be harmed if we lose principal members of our management team.

We are highly dependent on the continued service of our management team. The loss of any key member of our management team may substantially disrupt our business and could harm our business, results of operations and financial condition. In addition, replacing management personnel could be costly and time consuming.

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We are effectively controlled by our principal stockholders and management, which may limit your ability to influence stockholder matters.

As of January 31, 2005, our executive officers, directors and principal stockholders and their affiliates beneficially owned 3,676,296 shares, or 28.6% of the outstanding shares of common stock. Thus, they effectively control us and direct our affairs, including the election of directors and approval of significant corporate transactions. This concentration of ownership may have the effect of delaying, deferring or preventing a change in control of our company and some transactions may be more difficult or impossible without the support of these stockholders. The interests of these stockholders may conflict with those of other stockholders. We also conduct transactions with businesses in which our principal stockholders maintain interests. We believe that these transactions have been conducted on an arm's length basis, but we cannot assure you that these transactions would have the same terms if conducted with unrelated third parties.

We may not be able to protect our intellectual property, and any intellectual property litigation could be expensive and time consuming.

Our business and competitive position could be harmed if we fail to adequately protect our intellectual property. Although we have filed patent applications, we are not certain that our patent applications will result in the issuance of patents, or that any patents issued will provide commercially significant protection to our technology. In addition, as we grow and gain brand recognition, our products are more likely to be subjected to infringement litigation. We could incur substantial costs and may have to divert management and technical resources in order to respond to, defend against, or bring claims related to our intellectual property rights. In addition, we rely on a combination of patent, trademark, copyright and trade secret laws and contractual restrictions to establish and protect our proprietary rights. These statutory and contractual arrangements may not provide sufficient protection to prevent misappropriation of our technology or to deter independent third-party development of similar technologies. Any litigation could result in our expenditure of funds, management time and resources.

Our products may have undetected faults leading to liability claims, which could harm our business.

Our products may contain undetected faults or failures. Any failures of our products could result in significant losses to our customers, particularly in mission-critical applications. A failure could also result in product returns and the loss of, or delay in, market acceptance of our products. In addition, any failure of our products could result in claims against us. Our purchase agreements with our customers typically contain provisions designed to limit our exposure to potential product liability claims. However, the limitation of liability provisions contained in our purchase agreements may not be effective as a result of federal, state or local laws or ordinances or unfavorable judicial decisions in the United States or other countries. We maintain insurance to protect against certain claims associated with the use of our products, but our insurance coverage may not adequately cover all possible claims asserted against us. In addition, even claims that ultimately are unsuccessful could be expensive to defend and consume management time and resources.

Our charter contains certain anti-takeover provisions that may discourage take-over attempts and may reduce our stock price.

Our board of directors has the authority to issue up to 10,000,000 shares of preferred stock and to determine the preferences, rights and privileges of those shares without any further vote or action by the stockholders. The rights of the holders of common stock may be harmed by the rights of the holders of any preferred stock that may be issued in the future. Certain provisions of our certificate of incorporation and bylaws may make it more difficult for a third party to acquire control of us without the consent of our board of directors, even if such changes were favored by a majority of the stockholders. These include provisions that provide for a staggered board of directors, prohibit stockholders from taking action by written consent and restrict the ability of stockholders to call special meetings.

Future sales of shares may decrease our stock price.

Sales of substantial amounts of our common stock in the public market, including shares issued upon the exercise of outstanding options, or the perception that such sales could occur, could reduce the market price of our common stock. These sales also might make it more difficult for us to raise funds through future offerings of common stock.

ITEM 3. QUALITATIVE AND QUANTITATIVE DISCLOSURE ABOUT MARKET RISK.

The majority of our cash equivalents and marketable securities are invested in variable rate instruments with frequent rate resets. Because these securities have short effective maturities, we believe the market risk for such holdings is insignificant.

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ITEM 4. DISCLOSURE CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures. As evidenced by the restatement of the press release filed on Form 8-K/A for the quarter ending January 31, 2005 and based on our management's evaluation (with the participation of our principal executive officer and principal financial officer), as of the end of the period covered by this report, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, (the "Exchange Act")) were inadequate to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. The Company determined that there was a material weakness in the functioning of the disclosure controls and procedures, especially controls over consolidation and expense review. The Company lacked controls relating to the monitoring and investigation of intercompany balances and related differences and elimination of intercompany balances in the consolidation process.

Changes in internal control over financial reporting. The principal executive officer and principal financial officer have commenced a detailed evaluation of the reporting processes, controls and responsibilities and will report recommendations to the Board and Audit Committee on April 5, 2005 to ensure that the Company meets all reporting obligations. In addition, as part of our ongoing plan to improve internal controls at Cortelco Shanghai we implemented the following internal controls during the first quarter: 1) all balance sheet accounts are reconciled on a monthly basis, 2) management has implemented numerous control reports that are approved by the controller and CFO on a monthly basis, and 3) management has begun the process of documenting all policies and procedures for the Cortelco Shanghai operations. While this is an ongoing process we believe that the above mentioned measures will improve the reliability of Cortelco Shanghai's internal control structure. Except for the foregoing, there was no change in our internal control over financial reporting during our second fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

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

The Company scheduled the 2004 Annual Meeting of Stockholders on November 30, 2004 at our offices located at 185 Martinvale Lane, San Jose, CA 95119. The meeting was adjourned until December 21, 2004 due to insufficient votes to obtain a quorum. The meeting on December 21, 2004 was adjourned until January 14, 2005 due to insufficient votes to obtain a quorum. At that meeting, a majority of stockholders voted to elect Robert P. Dilworth and David S. Lee to serve as directors for a term of three years. Stephen R. Bowling, Frederick Gibbs, and W. Frank King are continuing directors who were not up for election at the meeting.

In addition, stockholders ratified the appointment of Grant Thornton LLP as our independent registered accountants for the fiscal year ending July 31, 2005. Stockholders also approved the addition of 500,000 shares of common stock to be made available to the Employee Stock Purchase Plan.

Item 6. Exhibits.

(A) Exhibits.

<u>Exhibit No.</u>	<u>Description</u>
31	Officers' Certification of Periodic Report pursuant to Section 302 of Sarbanes-Oxley Act of 2002
32	Officers' Certification of Periodic Report pursuant to Section 906 of Sarbanes-Oxley Act of 2002

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SIGNATURE

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

EON COMMUNICATIONS CORPORATION

Date: March 17, 2005

\ Stephen R. Bowling

Stephen R. Bowling
Vice President, Chief Financial Officer
(Duly Authorized Officer, Principal Financial and
Accounting Officer)

CERTIFICATIONS OF PERIODIC REPORT
PURSUANT TO SECTION 302 OF SARBANES-OXLEY ACT OF 2002

I, David S. Lee, certify that:

1. I have reviewed this quarterly report on Form 10-Q of eOn Communications Corporation (“Registrant”);
2. Based on my knowledge, this annual 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 officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;
 - (b) Evaluated the effectiveness of the Registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the Registrant’s internal control over financial reporting that occurred during the Registrant’s second fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant’s internal control over financial reporting; and
5. The Registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant’s auditors and the audit committee of the Registrant’s board of directors:
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant’s ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant’s internal control over financial reporting.

Date: March 17, 2005

/s/ David S. Lee

David S. Lee
Chief Executive Officer

I, Stephen R. Bowling, certify that:

1. I have reviewed this quarterly report on Form 10-Q of eOn Communications Corporation (“Registrant”);
2. Based on my knowledge, this annual 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 officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;
 - (b) Evaluated the effectiveness of the Registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the Registrant’s internal control over financial reporting that occurred during the Registrant’s second fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant’s internal control over financial reporting; and
5. The Registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant’s auditors and the audit committee of the Registrant’s board of directors:
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant’s ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant’s internal control over financial reporting.

Date: March 17, 2005

/s/ Stephen R. Bowling

Stephen R. Bowling
Chief Financial Officer

CERTIFICATIONS OF PERIODIC REPORT
PURSUANT TO SECTION 906 OF SARBANES-OXLEY ACT OF 2002

In connection with this quarterly report on Form 10-Q of eOn Communications Corporation (“Registrant”) I, David S. Lee, Chief Executive Officer of Registrant, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in this report fairly presents, in all material respects, the financial condition and results of operations of Registrant.

Date: March 17, 2005

/s/ David S. Lee

David S. Lee
Chief Executive Officer

In connection with this quarterly report on Form 10-Q of eOn Communications Corporation (“Registrant”) I, Stephen R. Bowling, Chief Financial Officer of Registrant, certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in this report fairly presents, in all material respects, the financial condition and results of operations of Registrant.

Date: March 17, 2005

/s/ Stephen R. Bowling

Stephen R. Bowling
Chief Financial Officer