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WIDEPOINT CORP  
Form 10-Q/A  
January 19, 2006

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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**FORM 10-Q/A No. 2**

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Amendment No. 2 to Quarterly Report on Form 10-Q for the quarter ended September 30, 2004

WIDEPOINT CORPORATION

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(Exact name of registrant as specified in its charter)

Delaware

000-23967

52-2040275

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(State or other jurisdiction of  
incorporation or organization)

(Commission File Number)

(IRS Employer Identification No.)

One Lincoln Centre, 18W140 Butterfield Road, Suite 1100, Oakbrook Terrace, Ill

60181

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(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (630) 629-0003

The undersigned registrant hereby amends the following items, financial statements, exhibits or other portions of its Quarterly Report on Form 10-Q for the quarter ended September 30, 2004, as previously amended by Amendment No. 1 filed on November 17, 2004, as set forth in the pages attached hereto:

Part I	Item 1	Condensed Consolidated Financial Statements
	Item 2	Management's Discussion and Analysis of Financial Condition and Results of Operations
	Item 4	Controls and Procedures
Part II	Item 6	Exhibits

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

WidePoint Corporation

Date: January 19, 2006

By: /s/ James T. McCubbin  
James T. McCubbin  
Vice President and Chief Financial Officer

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INTRODUCTORY NOTE

This Amendment No. 2 of the Company's Quarterly Report on Form 10-Q has been revised as a result of certain Restatements made by the Company, which are further described in the Financial Statements, note No. 1.

WIDEPOINT CORPORATION

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**PART 1. FINANCIAL INFORMATION****ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.****WIDEPOINT CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS**

	<b>As Restated September 30, 2004</b>	<b>December 31, 2003</b>
	<b>(unaudited)</b>	<b>(unaudited)</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 598,111	\$ 949,612
Accounts receivable, net of allowance of \$0 and 18,819, respectively	511,527	405,662
Prepaid expenses and other assets	42,361	49,645
Total current assets	1,151,999	1,404,919
Property and equipment, net	7,858	6,990
Other assets	71,867	60,639
Total assets	\$ 1,231,724	\$ 1,472,548
<b>LIABILITIES &amp; SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 94,155	\$ 52,382
Accrued expenses	300,111	238,902
Short-term portion of deferred rent	2,407	--

	<u>As Restated September 30, 2004</u>	<u>December 31, 2003</u>
Total current liabilities	396,673	291,284
Long-term portion of deferred rent	7,764	--
Total Liabilities	\$ 404,437	\$ 291,284
Shareholders' equity		
Preferred stock, \$0.001 par value, 10,000,000 shares authorized, None issued and outstanding	\$ --	\$ --
Common stock, \$0.001 par value, 50,000,000 shares authorized, 16,896,509 and 15,579,913 shares issued and outstanding as of September 30, 2004 and December 31, 2003, respectively	16,897	15,580
Related party notes receivable	(121,100)	(121,100)
Additional paid-in capital	42,566,865	42,110,539
Accumulated deficit	(41,635,375)	(40,823,755)
Total shareholders' equity	827,287	1,181,264
Total liabilities & shareholders' equity	\$ 1,231,724	\$ 1,472,548

The accompanying notes are an integral part of these statements.

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## WIDEPOINT CORPORATION AND SUBSIDIARIES

### CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>As Restated 2004</u>	2003	<u>As Restated 2004</u>	2003
	(unaudited)			
Revenues, net	\$ 906,685	\$ 759,262	\$ 2,470,992	\$ 2,497,145
Operating expenses:				
Cost of sales	666,544	562,107	1,850,528	1,834,534
Sales and marketing	147,068	101,021	377,238	338,748
General & administrative	197,877	167,535	1,055,922	516,404
Depreciation	883	3,386	3,322	10,025
Loss from operations	(105,687)	(74,787)	(816,018)	(202,566)
Interest income (expenses), net	814	2,045	4,398	9,976
Net loss	\$ (104,873)	\$ (72,742)	\$ (811,620)	\$ (192,590)

	Three Months Ended September 30,		Nine Months Ended September 30,	
Basic and diluted net loss per share	\$ (0.01)	\$ (0.00)	\$ (0.05)	\$ (0.01)
Basic and diluted weighted average shares outstanding	16,896,509	15,579,913	16,336,990	15,579,913

The accompanying notes are an integral part of these statements.

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## WIDEPOINT CORPORATION AND SUBSIDIARIES

### CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended September 30,		Nine Months Ended September 30,	
	<u>As Restated</u> 2004	2003	<u>As Restated</u> 2004	2003
	(unaudited)			
Cash flows from operating activities:				
Net loss	\$ (104,873)	\$ (72,742)	\$ (811,620)	\$ (192,590)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities				
Depreciation expense	883	3,386	3,322	10,025
Stock compensation expense	--	--	501,749	--
Changes in assets and liabilities				
Accounts receivable	(55,166)	102,621	(105,865)	78,948
Prepaid expenses	1,031	11,119	7,284	29,993
Other assets	(5,423)	64,852	(55,334)	60,311
Accounts payable and accrued expenses	(7,082)	(79,083)	98,511	(92,513)
Net cash (used in) provided by operating activities	\$ (170,630)	\$ 30,153	\$ (361,953)	\$ (105,826)
Cashflows from investing activities:				
Purchase of property and equipment	(4,190)	--	(4,190)	(7,802)

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	Three Months Ended September 30,		Nine Months Ended September 30,	
Net cash used in investing activities	\$ (4,190)	\$ --	\$ (4,190)	\$ (7,802)
Cashflows from financing activities:				
Net (payments) borrowings on notes payable	(7,093)	(7,579)	14,642	15,663
Net payments on long-term obligations	--	(648)	--	(6,421)
Net cash (used in) provided by financing activities	\$ (7,093)	\$ (8,227)	\$ 14,642	\$ 9,242
Net (decrease) increase in cash	\$ (181,913)	\$ 21,926	\$ (351,501)	\$ (104,386)
Cash, beginning of period	\$ 780,024	\$ 1,082,348	\$ 949,612	\$ 1,208,660
Cash, end of period	\$ 598,111	\$ 1,104,274	\$ 598,111	\$ 1,104,274

The accompanying notes are an integral part of these statements.

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**WIDEPOINT CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. Basis of Presentation, Organization and Nature of Operations:**

The accompanying unaudited financial statements have been prepared in accordance with Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America ( US GAAP ) for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation have been included. These financial statements should be read in conjunction with the financial statements of WidePoint Corporation, as of December 31, 2003, and the notes thereto included in the Annual Report on Form 10-K filed by the Company. The results of operations for the three and nine months ended September 30, 2004, are not necessarily indicative of the results that may be expected for the year ending December 31, 2004.

WidePoint Corporation is a consulting services firm specializing in planning, managing and implementing Information Technology ( IT ) solutions. Its staff consists of business and technical specialists that help customers augment and expand their technical capabilities, drive new technical innovations and help maintain a competitive edge in today s rapidly changing technological environment. The Company, through a concerted mergers and acquisition strategy is focused on expanding its IT public market segment and has acquired two enterprises since December 31, 2003. The Company is having discussions with other enterprises which may or may not lead to further mergers and acquisitions.

During 2003, the Company witnessed a negative economic environment within the commercial IT sector due to constrained business investment and an excessive supply of IT Consultants which as a result reduced gross margins and decreased demand for the IT services that the Company provided to its customers.

In its efforts to expand its revenue streams, the Company continued to implement and refine a strategic plan that has included: the launch of a federal business initiative in 2003, the continued development of new technologies and capabilities focused within wireless technologies, the

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development of various other practice areas, the initiation and expansion of several alliances to expand the Company's ability to provide expanded services and reach to a wider group of new customers, and an expansion of both management talent and reach through its focused efforts to acquire additional business assets and revenue streams through targeted merger and acquisition activities in 2004.

On March 24, 2004 the Company entered into a merger agreement to acquire the stock of Chesapeake Government Technologies, Inc. ( CGT ), a Delaware corporation. The Company closed on the transaction on April 30, 2004 through a reverse triangular merger between Chesapeake Acquisition Corporation, Chesapeake Government Technologies, Inc. and WidePoint Corporation with Chesapeake Government Technologies, Inc. becoming a wholly owned subsidiary of WidePoint Corporation. The consideration included the issuance of stock and the assumption of debt as further described within a Form 8-K filed on May 14, 2004. The executive management expertise of the Company was greatly expanded through this transaction and further augmented the reach and expertise of the Company. CGT additionally brings to WidePoint several additional alliances, relationships, and targeted companies that CGT is in various phases of discussion in regards to merger and acquisition opportunities with CGT and WidePoint. The Company continues its efforts to expand the operations of WidePoint through mergers and acquisitions. The Company has entered into several letters of intent to acquire companies that, if consummated, are expected to materially expand the public sector segment of the Company. The Company closed on one of those transactions on October 25, 2004, with the acquisition of Operational Research Consultants, Inc. ( ORC ) through a stock purchase. The consideration included the issuance of stock, the assumption of debt, and provision of cash as further described in a Form 8-K filed on October 29, 2004. The management of the Company was further expanded through this transaction and future revenue as a result of this transaction are expected to increase.

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Most of the Company's current costs consist primarily of the salaries and benefits paid to the Company's technical, marketing and administrative personnel. As a result of its plan to expand its operations through new internal initiatives and merger and acquisition related activities, the Company expects these costs to increase. The Company's profitability depends upon both the volume of services performed and the Company's ability to manage costs. Because a significant portion of the Company's cost structure is labor related, the Company must effectively manage these costs to achieve profitability. To date, the Company has attempted to maximize its operating margins through efficiencies achieved by the use of the Company's proprietary methodologies and by offsetting increases in consultant salaries with increases in consultant fees received from clients. The current business environment has witnessed an increase in the competitive environment for the Company's services. The Company anticipates that this trend may continue.

### *Restatement*

Management of the Company determined that we had not correctly accounted for the Chesapeake acquisition as 1) it should not have resulted in the recognition of an intangible asset; 2) Company shares that were placed in escrow for release only upon the achievement of certain future revenue should not have been recognized immediately, but instead, only upon the achievement of certain contingencies; and 3) as a result of timing differences between the actual issuance by the Company of shares earned and issued, the Company should have recorded those shares earned during the period ending June 30, 2004 as common stock issuable and not as common stock as those shares were not issued until July 13, 2004.

While the Company's management believes that the Company did acquire assets in a business sense when it acquired the stock of Chesapeake, these assets, consisting primarily of Chesapeake's relationships with various sources of potential business opportunities, did not meet the criteria for recognition as assets under Statement of Financial Accounting Standards No. 141 ( SFAS 141 ). Additionally, the acquisition could not give rise to goodwill because Chesapeake was in the development stage at the time of acquisition and therefore not considered a business.

As a consequence of these determinations, previously issued financial statements have been restated to eliminate the intangible asset associated with the Chesapeake acquisition, reverse related amortization expense, and expense as consulting fees the cost of the transaction attributable to the cost of issuance of the non-escrowed shares and other related direct costs at the time of acquisition. Further, the basic and diluted weighted average shares outstanding have been adjusted to allow only for the recordation of the shares attributable to the issuance of the non-escrowed shares, which had been earned at the time of the transaction. This resulted in a reduction of basic and diluted weighted average shares outstanding from 20,162,893 and 18,160,920 for the three and nine month periods ending June 30, 2004, respectively, to 16,896,509 and 16,336,990 for the same periods.

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The effect of the above mentioned restatements are presented as follows:

Balance Sheet:

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	Previously Reported	As Restated
	September 30, 2004	September 30, 2004
Goodwill and other intangibles	1,540,319	--
Total assets	\$ 2,772,043	\$ 1,231,724
Common stock	20,163	16,897
Additional paid-in capital	43,674,169	42,566,865
Accumulated deficit	(41,205,626)	(41,635,375)
Total shareholders equity	2,367,606	827,287
Total liabilities & shareholders equity	\$ 2,772,043	\$ 1,231,724

Statement of Operations:

	Previously Reported		As Restated	
	Three Months Ended	Nine Months Ended	Three Months Ended	Nine Months Ended
	September 30, 2004	September 30, 2004	September 30, 2004	September 30, 2004
General & administrative	197,877	626,173	197,877	1,055,922
Loss from operations	(105,687)	(386,269)	(105,687)	(816,018)
Net loss	(104,873)	(381,871)	(104,873)	(811,620)
Basic and diluted net loss per share	\$ (0.01)	\$ (0.02)	\$ (0.01)	\$ (0.05)
Basic and diluted weighted average shares outstanding	20,162,893	18,160,920	16,896,509	16,336,990

## Statement of Cashflows:

	Previously Reported	As Restated
	Nine Months Ended	Nine Months Ended
	September 30, 2004	September 30, 2004
Net loss	(381,871)	(811,620)
Stock compensation expense	72,000	501,749

**2. Significant Accounting Policies:***Principles of Consolidation*

The accompanying consolidated financial statements include the accounts of the acquired entities since their respective dates of acquisition. All significant intercompany amounts have been eliminated.

*Use of Estimates*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

*Cash and Cash Equivalents*

Investments purchased with original maturities of three months or less are considered cash equivalents for purposes of these condensed consolidated financial statements. The Company maintains cash and cash equivalents with various major financial institutions. At September 30, 2004 and December 31, 2003, cash and cash equivalents included \$150,987 and \$250,144, respectively, on investments in interest bearing accounts. At times, cash balances held at financial institutions were in excess of federally insured limits. The Company places its temporary cash investments with high-credit, quality financial institutions, and as a result, the Company believes that no significant concentration of credit risk exists with respect to these cash investments.

*Accounts Receivable*

The majority of the Company's accounts receivable are due from established companies in the following industries: manufacturing, consumer product goods, direct marketing, healthcare and other service companies.

Credit is extended based on evaluation of a customer's financial condition and, generally, collateral is not required. Accounts receivable are due within 30 to 45 days and are stated at amounts due from customers net of an allowance for doubtful accounts. Accounts outstanding longer than the contractual payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company and the condition of the general economy and the industry as a whole. The Company writes-off accounts receivable when they become uncollectible and payments subsequently received on such receivables are credited to the allowance for doubtful accounts. The following table sets forth the rolling forward balances of the Allowance for doubtful accounts of the Company.

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Description	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions	Balance at End of Period
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**2. Significant Accounting Policies:**



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For the year ended December 31, 2003, Allowance for doubtful accounts	\$ 1,800	\$ 17,319	\$ 300	\$ 18,819
For the quarter ended September 30, 2004, Allowance for doubtful accounts	\$ --	\$ --	\$ --	\$ --

Unbilled accounts receivable on time-and-materials contracts represent costs incurred and gross profit recognized near the period-end but not billed until the following period. Unbilled accounts receivable on fixed-price contracts consist of amounts incurred that are not yet billable under contract terms. Unbilled accounts receivable totaled \$0 and \$6,207 at September 30, 2004 and December 31, 2003, respectively.

*Concentrations of Credit Risk*

Financial instruments that potentially subject the Company to credit risk consist of cash and cash equivalents and accounts receivable. As of September 30, 2004, three customers represented 24%, 23%, and 13% of accounts receivable, respectively. As of December 31, 2003, three customers individually represented 26%, 11%, and 10% of accounts receivable.

*Fair Value of Financial Instruments*

WidePoint financial instruments consist of cash, accounts receivable, accounts payable and accrued expenses. The fair value of these financial instruments approximates their carrying value as of September 30, 2004, due to their short-term nature.

*Revenue Recognition*

Revenue on time-and-materials contracts is recognized based upon hours incurred at contract rates plus direct costs. Revenue on fixed-price contracts is recognized on the percentage-of-completion method based on costs incurred in relation to total estimated costs. Anticipated losses are recognized as soon as they become known. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined. Out of pocket expenses for billable work are recognized as revenues and such out of pocket expenses are expensed in Cost of Revenues.

*Significant Customers*

During the third quarter of 2004, three customers individually represented 19%, 18%, and 13% of revenue. During the third quarter of 2003, four customers individually represented 19%, 16%, 16%, and 11% of revenue.

*Income Taxes*

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 109, Accounting for Income Taxes. Under SFAS No.109, deferred tax assets and liabilities are computed based on the difference between the financial statement and income tax bases of assets and liabilities using the enacted marginal tax rate. SFAS No. 109 requires that the net deferred tax asset be reduced by a valuation allowance if, based on the weight of available evidence, it is more likely than not that some portion or all of the net deferred tax asset will not be realized. The Company continues to reduce its net deferred taxes by a 100% valuation allowance.

*Stock-based compensation*

The Company accounts for stock-based employee compensation arrangements using the intrinsic value method in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and complies with the disclosure provisions of SFAS No. 123 Accounting for Stock-Based Compensation. Under APB Opinion No. 25, compensation cost is generally recognized based on the difference, if any, on the date of grant between the fair value of the Company's common stock and the amount an employee must pay to acquire the stock. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement 123, Accounting for Stock-Based Compensation, using the assumptions described below, to its stock-based employee plans.

Three Months ended September 30,		Nine Months ended September 30,	
As Restated 2004	2003	As Restated 2004	2003

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	Three Months ended September 30,		Nine Months ended September 30,	
Net loss, as reported	\$ 104,873	\$ 72,742	\$ 811,620	\$ 192,590
Add: Total stock-based employee compensation expense determined under fair value based method for awards granted, modified, or settled, net of related tax effects	87,712	152,364	263,136	457,091
Pro forma net loss	\$ 192,585	\$ 225,106	\$ 1,074,756	\$ 649,681
Earnings per share:				
Basic and diluted - as reported	\$ (0.01)	\$ (0.00)	\$ (0.05)	\$ (0.01)
Basic and diluted - pro forma	\$ (0.01)	\$ (0.01)	\$ (0.07)	\$ (0.04)

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The pro forma disclosure is not likely to be indicative of pro forma results which may be expected in future years because of the fact that options vest over several years, pro forma compensation expense is recognized as the options vest and additional awards may also be granted.

For purposes of determining the effect of these options, the fair value of each option is estimated on the date of grant based on the Black-Scholes single-option pricing model assuming the following for the three and nine months ended September 30, 2004 and 2003:

	2004 & 2003
Dividend yield	--
Risk-free interest rate (%)	2.70-4.13%
Volatility factor (%)	156%
Expected life in years	5
Non-employee based compensation:	

The Company accounts for stock-based non-employee compensation arrangements using the fair value recognition provisions of FASB Statement 123, *Accounting for Stock-Based Compensation* and Emerging Issues Task Force EITF 96-18, *Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services*.

#### *Stock Based Performance Warrants*

The Company has entered into several stock performance incentive arrangements utilizing warrants with members of the Company's management team. These warrants are accounted for as variable plans under APB 25 because vesting of the warrants are tied to specific performance parameters which cannot be determined until such performance has been achieved. Presently, no warrants have satisfied any performance requirements.

#### *Basic and Diluted Net Loss Per Share*

Basic income or loss per share includes no dilution and is computed by dividing net income or loss by the weighted-average number of common shares outstanding for the period. Diluted income or loss per share includes the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. The treasury stock effect of options and warrants to purchase 5,378,384 and 1,816,000 shares of common stock outstanding at September 30, 2004 and 2003, respectively, has not been included in the calculation of the net loss per share as such effect would have been anti-dilutive. As a result of these items, the basic and diluted loss per share for all periods presented is identical.

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#### *Reclassifications*

Certain amounts in prior years' financial statements have been reclassified to conform with the current year presentation.

## 2. Significant Accounting Policies:

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### 3. Promissory Notes:

#### 3. Promissory Notes

Pursuant to stock purchase agreements entered into on July 8, 2002, between the Company and each of Steve L. Komar, James T. McCubbin and Mark M. Mirabile, the Company privately sold 865,000 shares of its common stock to each such person without registration under the Securities Act of 1933, pursuant to the private offering exemption under Section 4(2) thereof, in consideration of a three (3) year full-recourse, five percent (5%) interest bearing promissory note with equal annual principal payments due, issued by each such person to the Company in the principal amount of \$60,550, or \$181,650 in the aggregate (which equals \$0.07 per share, being the closing price of the Company's common stock on July 8, 2002). The individuals have repaid to date \$21,500 individually, or \$64,500 in aggregate to the Company.

### 4. Commitments and Contingencies:

#### *Litigation*

The Company is periodically a party to disputes arising from normal business activities. In the opinion of management, resolution of these matters will not have a material adverse effect upon the financial position or future operating results of the Company and adequate provision for any potential losses has been made in the accompanying consolidated financial statements.

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

The following discussion and analysis of the financial condition and results of operations of the Company should be read in conjunction with the financial statements and the notes thereto which appear elsewhere in this quarterly report and the Company's Annual Report on Form 10-K for the year ended December 31, 2003.

The information set forth below includes forward-looking statements. Certain factors that could cause results to differ materially from those projected in the forward-looking statements are set forth below. Readers are cautioned not to put undue reliance on forward-looking statements. The Company disclaims any intent or obligation to update publicly these forward-looking statements, whether as a result of new information, future events or otherwise.

### Overview

WidePoint Corporation is a consulting services firm specializing in planning, managing and implementing Information Technology (IT) solutions. Its staff consists of business and technical specialists that help customers augment and expand their technical capabilities, drive new technical innovations and help maintain a competitive edge in today's rapidly changing technological environment.

Since 1996, WidePoint has focused on leveraging leading edge technologies, methodologies and consultants to help clients improve their business performance. This focus continues to tie together the Company's service offerings and future direction. WidePoint's clients are increasingly looking to harness the power of the Internet and leading IT technologies by integrating these technologies with their existing systems as they transition, expand, and refine their business environments.

During 2003, the Company witnessed a negative economic environment within the commercial IT sector due to constrained business investment and an excessive supply of IT consultants which as a result reduced gross margins and decreased demand for the IT services that the Company provided to its customers.

In its efforts to expand its revenue streams, the Company continued in 2004 to implement and refine a strategic plan which included: the launch of a federal business initiative in 2003, the continued development of new technologies and capabilities focused within wireless technologies, the development of various other practice areas, the initiation and expansion of several alliances to expand the Company's ability to provide expanded services and reach to a wider group of new customers, and an expansion of both management talent and reach through its focused efforts to acquire additional business assets and revenues streams through targeted merger and acquisition activities in 2004.

On March 24, 2004 the Company entered into a merger agreement to acquire the stock of Chesapeake Government Technologies, Inc. (CGT), a Delaware corporation. The Company closed on the transaction on April 30, 2004 through a reverse triangular merger between Chesapeake Acquisition Corporation, Chesapeake Government Technologies, Inc. and WidePoint Corporation with Chesapeake Government Technologies, Inc. becoming a wholly owned subsidiary of WidePoint Corporation. The consideration included the issuance of stock and the assumption of debt as further described within a Form 8-K filed on May 14, 2004. The executive management expertise of the Company was greatly expanded

through this transaction and further augmented the reach and expertise of the Company. CGT additionally brings to WidePoint several additional alliances, relationships, and targeted companies that CGT is in various phases of discussion in regards to merger and acquisition opportunities with CGT and WidePoint.

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The Company continues its efforts to expand the operations of WidePoint through merger and acquisitions. The Company entered into a non-binding letter of intent to acquire all of the stock of Operational Research Consultants, Inc. ( ORC ), a Virginia based corporation, on July 7, 2004. ORC business expertise resides in specialized IT based software and services predominately within the federal marketplace. This transaction was completed on October 25, 2004. The Company is also presently exploring several other transactions designed to further expand the public sector segment of the Company.

For the three months ended September 30, 2004, revenue was approximately \$907,000 as compared to revenue of approximately \$759,000 for the quarterly period ended September 30, 2003. For the nine months ended September 30, 2004, revenue was approximately \$2,471,000, as compared to revenue of approximately \$2,497,000 for the nine-month period ended September 30, 2003. The increase in revenues in the three months ended September 30, 2004, was attributable to an increase in additional hours billed as a result of a higher win rate associated with the Company's sales and marketing efforts. The decrease in revenues for the nine months ended September 30, 2004, was attributable to fewer hours billed and a lower average bill rate in the quarter ended March 31, 2004 than in the prior year's first quarter. The Company has witnessed a stabilization and slight increase in billable hours worked during the second and third quarters of 2004 while pricing pressures within the industry continued to place pressure on average billable rates as compared to the third quarter of 2003, but presently the Company has witnessed a stabilization of these pricing pressures. The instability within the IT marketplace continues to create an increase in competitiveness that creates a more difficult environment to expand revenues internally for the Company. The Company anticipates these trends may stabilize in the fourth quarter of 2004. The Company further anticipates that if it is successful in executing its business strategy to expand into the government marketplace through mergers and acquisitions that revenue growth can be expected to expand materially in the future. With the acquisition completed in October of 2004 of ORC the Company anticipates that its revenues derived from this acquisition will materially expand the Company's revenues in the fourth quarter of 2004.

Most of the Company's current costs consist primarily of the salaries and benefits paid to the Company's technical, marketing and administrative personnel and depreciation expenses related to property and equipment. Consistent with the development of a new focused strategic direction, the Company expects to expand its operations through internal growth and by potential acquisition of new personnel and assets. Therefore, the Company anticipates these costs will increase.

The Company's profitability depends upon both the volume of services performed and the Company's ability to manage costs. Because a significant portion of the Company's cost structure is labor related, the Company must effectively manage these costs to achieve profitability. To date, the Company has attempted to manage its operating margins by offsetting increases in consultant salaries with increases in consultant fees received from clients and by effectively managing general overhead costs. During the economic slowdown within the IT marketplace the Company has witnessed a degradation of its operating margins and continues to experience margin pressures for the services that the Company offers. To be successful the Company must continue to win new business, expand its revenues, and manage its operating margins along with its general overhead costs to mitigate the Company's losses and restore positive cashflow and earnings growth.

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The Company restated its financials for the three and nine months ended September 30, 2004 when the Company's management determined that we had not correctly accounted for the Chesapeake acquisition as 1) it should not have resulted in the recognition of an intangible asset; 2) Company shares that were placed in escrow for release only upon the achievement of certain future revenue should not have been recognized immediately, but instead, only upon the achievement of certain contingencies; and 3) as a result of timing differences between the actual issuance by the Company of shares earned and issued, the Company should have recorded those shares earned during the period ending June 30, 2004 as common stock issuable and not as common stock as those shares were not issued until July 13, 2004.

While the Company's management believes that the Company did acquire assets in a business sense when it acquired the stock of Chesapeake, these assets, consisting primarily of Chesapeake's relationships with various sources of potential business opportunities, did not meet the criteria for recognition as assets under Statement of Financial Accounting Standards No. 141 ( SFAS 141 ). Additionally, the acquisition could not give rise to goodwill because Chesapeake was in the development stage at the time of acquisition and therefore not considered a business.

As a consequence of these determinations, previously issued financial statements have been restated to eliminate the intangible asset associated with the Chesapeake acquisition, reverse related amortization expense, and expense as consulting fees the cost of the transaction attributable to the cost of issuance of the non-escrowed shares and other related direct costs at the time of acquisition. Further, the basic and diluted weighted average shares outstanding have been adjusted to allow only for the recordation of the shares attributable to the issuance of the non-escrowed shares, which had been earned at the time of the transaction. This resulted in a reduction of basic and diluted weighted average shares

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outstanding from 20,162,893 and 18,160,920 for the three and nine month periods ending June 30, 2004, respectively, to 16,896,509 and 16,336,990 for the same periods. For further information related to the quantitative effects of the restatement, see note 1 of the Company's financial statements.

### Results of Operations

#### Three Months Ended September 30, 2004 as Compared to Three Months Ended September 30, 2003

*Revenue.* Revenue for the three month period ended September 30, 2004 was approximately \$907,000 as compared to approximately \$759,000 for the three month period ended September 30, 2003. The revenue increase was attributable to an increase in billable hours for its consultants in the Quarter ending September 30, 2004 as a result of improvements in results from the Company's sales and marketing efforts in this period as compared to the Quarter ended September 30, 2003.

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*Gross profit.* Gross profit for the three month period ended September 30, 2004, was approximately \$240,000, or 26% of revenues, an increase of approximately \$43,000 from gross profit of approximately \$197,000, or 26% of revenues, for the three month period ended September 30, 2003. The increase in gross profit was materially attributable to greater revenues as a direct result of an increase in billable hours and a stabilization in gross margins associated with these revenues.

*Sales and marketing.* Sales and marketing expenses for the three month period ended September 30, 2004, were approximately \$147,000, or 16% of revenues, an increase of approximately \$46,000, as compared to approximately \$101,000, or 13% of revenues, for the three month period ended September 30, 2003. The increase was materially attributable to an increase in sales payroll for sales and marketing efforts instituted by the Company.

*General and administrative.* General and administrative expenses for the three month period ended September 30, 2004, were approximately \$198,000, or 22% of revenues, an increase of approximately \$30,000, as compared to approximately \$168,000, or 22% of revenues, incurred by the Company for the three month period ended September 30, 2003. The increase in general and administrative expenses for the three months ended September 30, 2004, was primarily attributable to monthly expenses associated with the mergers and acquisitions efforts currently underway.

*Depreciation.* Depreciation expenses for the three month period ended September 30, 2004, was \$883, or less than 1% of revenues, a decrease of \$2,503, as compared to \$3,386 of such expenses, or less than 1% of revenues, incurred by the Company for the three month period ended September 30, 2003. The decrease in depreciation expenses for the three month period ended September 30, 2004, was primarily attributable to a lesser amount of depreciable assets as a result of the reduced equipment requirements of a smaller consultant base.

*Other income (expense).* Interest income (expense), net for the three month period ended September 30, 2004, was \$814, or less than 1% of revenues, a decrease of \$1,231 as compared to \$2,045, or less than 1% of revenues, for the three month period ended September 30, 2003. The decrease in interest income for the three month period ended September 30, 2004, was primarily attributable to lesser amounts of cash and cash equivalents along with lower short term interest rates that were available to the Company on investments in overnight sweep accounts.

*Net loss.* As a result of the above, the net loss for the three month period ended September 30, 2004, was approximately \$105,000 as compared to the net loss of approximately \$73,000 for the three months ended September 30, 2003.

#### Nine Months Ended September 30, 2004 as Compared to Nine Months Ended September 30, 2003

*Revenue.* Revenue for the nine month period ended September 30, 2004 was approximately \$2,471,000 as compared to approximately \$2,497,000 for the nine month period ended September 30, 2003. The revenue decrease was attributable to a lower average bill rate by consultants and fewer billable hours in the nine months ending September 30, 2004 as compared to the nine months ended September 30, 2003. This decrease in revenue was materially due to lower levels of billable hours in the first quarter of 2004 as compared to the same period in 2003.

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*Gross profit.* Gross profit for the nine month period ended September 30, 2004, was approximately \$620,000, or 25% of revenues, a decrease of approximately \$43,000 from gross profit of approximately \$663,000, or 27% of revenues, for the nine month period ended September 30, 2003. The decline of gross profit was materially attributable to a reduction in gross margin as a result of negative pricing pressures that were present within the current IT marketplace for the Company's services within the first quarter comparative periods.

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*Sales and marketing.* Sales and marketing expenses for the nine month period ended September 30, 2004, were approximately \$377,000, or 15% of revenues, an increase of approximately \$38,000, as compared to approximately \$339,000, or 14% of revenues, for the nine month period ended September 30, 2003. The increase was materially attributable to an increase in sales payroll for sales and marketing efforts instituted by the Company.

*General and administrative.* General and administrative expenses for the nine month period ended September 30, 2004, were approximately \$1,056,000, or 43% of revenues, an increase of approximately \$540,000, as compared to approximately \$516,000, or 21% of revenues, incurred by the Company for the nine month period ended September 30, 2003. The increase in general and administrative expenses for the nine months ended September 30, 2004, was primarily attributable to the issuance of stock for services associated with the Company's mergers and acquisitions activities. Approximately \$72,000 of this expense was associated with a stock issuance for services associated with the Company's mergers and acquisitions efforts. Approximately \$430,000 was associated with compensation expense related to our CGT acquisition in the 2<sup>nd</sup> quarter of 2004.

*Depreciation.* Depreciation expenses for the nine month period ended September 30, 2004, was \$3,322, or less than 1% of revenues, a decrease of \$6,703, as compared to \$10,025 of such expenses, or less than 1% of revenues, incurred by the Company for the nine month period ended September 30, 2003. The decrease in depreciation expenses for the nine month period ended September 30, 2004, was primarily attributable to a lesser amount of depreciable assets as a result of the reduced equipments requirements of a smaller consultant base.

*Other income (expense).* Interest income (expense), net for the nine month period ended September 30, 2004, was \$4,398, or less than 1% of revenues, a decrease of \$5,578 as compared to \$9,976, or less than 1% of revenues, for the nine month period ended September 30, 2003. The decrease in interest income (expense), net for the nine month period ended September 30, 2004, was primarily attributable to lesser amounts of cash and cash equivalents along with lower short term interest rates that were available to the Company on investments in interest-bearing accounts.

*Net loss.* As a result of the above, the net loss for the nine month period ended September 30, 2004, was approximately \$812,000 as compared to the net loss of approximately \$193,000 for the nine months ended September 30, 2003.

### Liquidity and Capital Resources

The Company has, since inception, financed its operations and capital expenditures through the sale of stock, seller notes, convertible notes, convertible exchangeable debentures and the proceeds from the exchange offer and exercise of the warrants related to a convertible exchangeable debenture. During 2004 and 2003 the Company has materially financed its operations with its working capital.

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Cash used in operating activities for the quarter ended September 30, 2004, was approximately \$171,000 as compared to cash provided by operating activities of approximately \$30,000 for the quarter ended September 30, 2003. The decrease in cash used by operations during the third quarter of 2004 as compared to the third quarter ending 2003 was primarily a result of an increase in days sales outstanding in accounts receivable and cash investments in its strategy to expand its revenues through targeted mergers and acquisition activities. Capital expenditures in property and equipment was approximately \$4,000 for the quarter ended September 30, 2004, while there was no material amount of capital expenditures on property for the quarter ended September 30, 2003.

As of September 30, 2004, the Company had net working capital of approximately \$0.8 million. The Company's primary source of liquidity consists of approximately \$0.6 million in cash and cash equivalents and approximately \$0.5 million of accounts receivable. The Company's current liabilities include approximately \$0.4 million in accounts payable and accrued expenses.

The market for the Company's services is experiencing an environment of constrained technology investment as a result of an economic slowdown that has reduced new technology initiatives. As a result of this negative environment, the demand for IT consultants ranging from software programmers to network engineers has been negatively affected. This has reduced demand for the Company's consultants as well as created an increase in competition from both domestic and foreign firms for the diminished amount of new and ongoing IT initiatives. The Company anticipates in the future a reversal of these negative events as economic growth is restored, the constrained environment in new technology initiatives ebb, and the Company executes its current mergers and acquisitions strategy. Therefore, the Company's business environment is characterized by rapid technological changes, experiences times of high growth and contraction, and material events such as mergers and acquisitions can materially change the profile of the Company.

Since 2002, the Company has embarked upon several new initiatives to counter the current negative environment within our industry and expand our capacity to restore revenue growth. The Company requires substantial working capital to fund the future growth of its business, particularly to finance accounts receivable, sales and marketing efforts, and capital expenditures. The Company currently has no commitments for capital expenditures. The Company's future capital requirements will depend on many factors including the rate of revenue growth, if any, the timing

and extent of spending for new product and service development, technological changes and market acceptance of the Company's services.

The Company believes that its current cash position is sufficient to meet its capital expenditure and working capital requirements for the near term, however, the growth and technological change of the market make it difficult for the Company to predict future liquidity requirements with certainty. Over the longer term, the Company must successfully execute its plans to increase revenue and income streams that will generate significant positive cash flows if it is to sustain adequate liquidity without impairing growth or requiring the infusion of additional funds from external sources. Additionally, a major expansion, such as occurred with the acquisition of ORC and any other major new subsidiaries, might require external financing that could include additional debt or equity capital. The Company obtained a one year senior line of credit from RBC-Centura in October 2004 for up to \$2.5 million dollars, collateralized against the assets of the Company, which also allows for the expansion of this line of credit up to \$5.0 million upon the successful completion of an additional acquisition by the Company. Approximately \$1.2 million dollars of the senior line of credit was utilized in its acquisition of ORC. The Company additionally raised approximately \$3.6 million dollars in equity investments by Barron Partners, LP, as discussed in the Form 8-K filed by the Company on October 29, 2004, as amended on November 2, 2004, and in the Form 8-K filed by the Company on November 4, 2004, that were used in the acquisition of ORC. There can be no assurance that additional financing, if required, will be available on acceptable terms, if at all, for the Company's future acquisitions and growth strategy.

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## Other

Inflation has not had a significant effect on the Company's operations, as increased costs to the Company have generally been offset by increased prices of services sold.

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

This report contains forward-looking statements setting forth the Company's beliefs or expectations relating to future revenues, profitability, and performance. Statements that contain words such as believes, expects, anticipates, intends, estimates, or similar expressions are forward-looking statements. Forward-looking statements involve risks and uncertainties that could cause actual results to differ materially from those expressed or implied by such forward-looking statements. Actual results may differ materially from projected or expected results due to changes in the demand for the Company's products and services, uncertainties relating to the results of operations, dependence on its major customers, risks associated with rapid technological change and the emerging services market, potential fluctuations in quarterly results, its dependence on key employees, its ability to successfully effect acquisitions of and mergers with other companies, and other risks and uncertainties affecting the technology industry generally. The Company disclaims any intent or obligation to up-date publicly these forward-looking statements, whether as a result of new information, future events or otherwise.

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## ITEM 4. CONTROLS AND PROCEDURES

### Disclosure Control and Procedures

An evaluation was carried out under the supervision and with the participation of the Company's management, including our Chief Executive Officer and Chief Financial Officer, regarding the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(c) under the Securities Exchange Act of 1934) as of September 30, 2004. Just before the filing of this Form 10-Q, the Company's management discovered that the agent it had engaged during 2003 to Edgarize and file the Company's definitive proxy statement, dated November 17, 2003 and used in connection with the Company's Annual Meeting of Shareholders held on December 18, 2003, and the Company's 2003 Annual Report to Shareholders, did not in fact make such filings. Furthermore, the Company subsequently identified a material weakness in its internal control over financial reporting and the need for certain restatements referred to below under Changes in Internal Control Over Financial Reporting. As a result, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were not effective as of September 30, 2004 to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and

forms.

Changes in Internal Control Over Financial Reporting

The Company reported in its original Form 10-Q that there had been no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2004, that materially affected or was reasonably likely to materially affect, the Company's internal control over financial reporting. However, in connection with the subsequent evaluation by the principal executive officer and principal financial officer of the Company required by Rule 13a-15(d) under the Securities Exchange Act of 1934, such officers subsequently determined that the following change had occurred that materially affected the Company's internal control over financial reporting relating to the quarter ending September 30, 2004.

During the fourth quarter of 2004, in connection with the Company's preparation of an S-1 filing, the Company identified a material weakness in the design of its internal control over financial reporting related to insufficient technical accounting expertise within our accounting function to resolve non-routine or complex accounting matters that occurred in connection with our acquisition of Chesapeake Government Technologies, Inc. and the inaccurate determination of the proper accounting treatment related to this acquisition. The material weakness in internal controls resulted in the need to restate our financial results for the three and nine month periods ended September 30, 2004.

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In order to remediate that material weakness, we engaged a consulting firm in January 2005 with the requisite accounting expertise, and are continuing to use the services of that firm in connection with such complex accounting matters. That action constituted a change in the Company's internal control over financial reporting that occurred during the first quarter of 2005. To date, the Company has not expended any material costs, nor does it estimate it will expend any material costs associated with engaging the accounting consultancy firm the Company hired to assist it in its technical accounting requirements. The accounting consultancy firm does not have any relationship with our current independent auditors.

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**PART II.**

**OTHER INFORMATION**

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

(a) Exhibits

31.1A Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2A Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32A Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.



