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NORTHSTAR ELECTRONICS INC

Form 10-Q

November 14, 2002

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

For the quarterly period ended September 30, 2002

TRANSITION REPORT UNDER SECTION 13 OR 15 (d) OF THE EXCHANGE ACT

For the transition period from n/a to n/a

333-90031

Commission file number

Northstar Electronics, Inc.

Exact name of small business issuer as specified in its charter

Delaware

State or other jurisdiction of organization

#33-0803434

IRS Employer Identification No.

Suite # 1455- 409 Granville Street,  
Vancouver, British Columbia,  
Canada V6C 1T2

Address of principal executive offices

(604) 685-0364

Issuer's telephone number

Not Applicable

Former name, former address and former fiscal year, if changed since last  
report

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY

PROCEEDINGS DURING THE PRECEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be  
filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of  
securities under a plan confirmed by a court.

Yes  No  Not Applicable

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Unaudited

Prepared by management

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### PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

NORTHSTAR ELECTRONICS, INC.

Consolidated Balance Sheets

Unaudited

U.S. Dollars

	September 30	December 31
	2002	2001
<b>ASSETS</b>		
Current		
Cash	\$87,568	\$39,699
Receivables	149,188	139,453
Recoverable expense and tax credits	158,200	-
Inventory and work in progress	200,223	107,257
Prepaid expenses	22,784	5,398
<b>Total Current Assets</b>	<b>617,963</b>	<b>291,807</b>
Due from a Director	1,510	-
Property and Equipment	85,820	91,903
<b>Total Assets</b>	<b>\$705,293</b>	<b>\$383,710</b>
<b>LIABILITIES</b>		
Current		
Accounts payable and accrued liabilities	\$301,538	\$325,075
Loans payable	-	6,778
Current portion of long term debt	199,320	211,208
<b>Total Current Liabilities</b>	<b>500,858</b>	<b>543,061</b>
Long Term Debt	492,524	364,549
Deferred Revenue	-	64,259
Due to Cabot Management Limited	57,600	56,249
Due to Director	-	24,401
<b>Total Liabilities</b>	<b>1,050,982</b>	<b>1,052,519</b>
<b>STOCKHOLDERS' EQUITY</b>		
Common Stock		
Authorized		
100,000,000 shares of common stock with a par value of \$0.0001 each		
20,000,000 shares of preferred stock with a par value of \$0.0001 each		
Issued and outstanding		
10,930,807 shares of common stock	1,093	794
(7,942,009 - 2001)		
Additional Paid in Capital	1,837,623	1,146,447
Other Comprehensive Income	15,492	37,308

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Deficit	(2,199,897)	(1,853,358)
Total Stockholders' Equity (Deficit)	(345,689)	(668,809)
Total Liabilities and Stockholders' Equity	\$705,293	\$383,710

### NORTHSTAR ELECTRONICS, INC.

#### Consolidated Statements of Operations

Three Months and Nine Months Ended September 30

Unaudited

U.S. Dollars

	Three Months		Nine Months	
	2002	2001	2002	2001
Sales	\$274,347	\$285,546	\$639,125	\$840,515
Cost of goods sold	63,551	89,985	271,691	220,039
Gross margin	210,796	195,561	367,434	620,476
Other income	(53)	946	45	15,661
	210,743	196,507	367,479	636,137
<b>Operating Expenses</b>				
Salaries	(14,765)	128,199	205,260	387,723
Consulting	43,761	0	98,284	0
Professional fees	48,252	81,172	61,538	149,063
Investor relations	14,518	0	47,885	0
Value of Director's uncompensated services	0	0	0	37,700
Advertising and marketing	(750)	22,523	34,798	54,727
Rent	19,086	9,558	59,209	53,009
Research and development	140,157	6,858	203,857	42,376
Office	23,996	27,471	45,745	52,360
Travel and business development	34,638	16,158	46,581	47,065
Interest on debt	8,215	6,945	28,087	23,220
Heat, light and telephone	7,237	4,383	21,490	14,769
Amortization	2,493	1,760	5,254	4,719
Repairs and maintenance	1,215	0	4,980	0
Transfer agent	1,301	0	2,079	0
Proposal costs	151	0	7,171	0
Total operating expenses	329,505	305,027	872,218	866,731
Net income (loss) from operations	\$(118,762)	\$(108,520)	\$(504,739)	\$(230,594)
Due from AQUACOMM	122,100	0	122,100	0
Research tax credits receivable	36,100	0	36,100	0
Net income (loss) for the period	\$ 39,438	\$(108,520)	\$(346,539)	\$(230,594)
Net income (loss) per share	\$ 0.004	\$(0.014)	\$(0.035)	\$(0.030)
<b>Weighted average number of shares</b>				
Outstanding	10,222,397	7,871,409	9,886,360	7,770,782

### NORTHSTAR ELECTRONICS, INC.

#### Consolidated Statement of Changes in Stockholders' Equity

Nine Months Ended September 30, 2002

Unaudited

U.S. Dollars

		Additional	Other	Accumu-	Total
Shares	Amount	Paid in	Compre-	lated	Stockholder
		Capital	hensive	Deficit	Equity
			Income		Deficit)

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Balance Dec. 31, 2001	7,942,009	\$ 794	\$1,146,447	\$37,308	\$(1,853,358)	\$(668,809)
Net loss for nine months	-	-	-	-	(346,539)	(346,539)
Fair value of options granted	-	-	10,186	-	-	10,186
Other comprehensive credits (debits)	-	-	-	(21,816)	-	(21,816)
Issuance of common stock for services	580,272	58	213,442	-	-	213,500
Issuance of common stock for cash	2,330,403	233	780,765	-	-	780,998
Share issuance Cost	-	-	(313,217)	-	-	(313,217)
Exercise of stock option	78,123	8	-	-	-	8
-----						
Balance September 30, 2002	10,930,807	\$1,093	\$1,837,623	\$15,492	\$(2,199,897)	\$(345,689)
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NORTHSTAR ELECTRONICS, INC.  
Consolidated Statement of Cash Flows  
Nine Months Ended September 30, 2002  
Unaudited  
U.S. Dollars

	September 30	
	2002	2001
Operating Activities		
Net income (loss)	\$(346,539)	\$(230,594)
Adjustments to reconcile net income (loss) to net cash used by operating activities		
Amortization	5,254	4,719
Issuance of common stock for services	213,500	67,341
Value of options granted	10,186	0
Uncompensated services	0	37,700
Changes in operating assets and liabilities	(368,579)	33,535
Net cash provided by (used by) operating activities	(486,178)	(87,299)
Investing Activity		
Acquisition of property and equipment	(3,220)	(22,606)
Financing Activities		
Issuance of common stock for cash - net	467,556	0
Increase (repayment) of long term debt	116,087	74,029
Due to Cabot Management Limited	1,351	(3,320)
Advances from (repayment to) director	(25,911)	(15,528)
Net cash (used by) provided by financing activities	559,083	55,181

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Effect of foreign currency translation on cash	(21,816)	3,284
Inflow (outflow) of cash	47,869	(51,440)
Cash, beginning of period	39,699	125,602
Cash, end of period	\$87,568	\$74,162
Supplemental information		
Interest paid	\$28,087	\$23,220
Shares issued for services	580,272	205,203
Corporate income taxes paid	\$0	\$0

NORTHSTAR ELECTRONICS, INC.

Notes to Consolidated Financial Statements

Nine Months Ended September 30, 2002

Unaudited

U.S. Dollars

### 1. ORGANIZATION AND BASIS OF PRESENTATION

These financial statements include the accounts of Northstar Electronics, Inc. ("the Company") and its wholly owned subsidiaries Northstar Technical Inc. ("NTI") and Northstar Network Ltd. ("NN"). All inter company balances and transactions are eliminated. The Company was incorporated May 11, 1998 under the laws of the State of Delaware and acquired NTI January 26, 1999 in a reverse takeover for the issuance of 4,901,481 shares of common stock from treasury. The Company's business activities are conducted principally in Canada but these financial statements are prepared with all figures translated into United States dollars.

These unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information, are condensed and do not include all disclosures required for annual financial statements. The organization and business of the Company, accounting policies followed by the Company and other information are contained in the notes to the Company's audited consolidated financial statements filed as part of the Company's December 31, 2001 Form 10-KSB.

In the opinion of the Company's management, these consolidated financial statements, prepared by management without audit, reflect all adjustments necessary to present fairly the Company's consolidated financial position at September 30, 2002 and the consolidated results of operations and the consolidated statement of cash flows for the nine months then ended. The results of operations for the nine months ended September 30, 2002 are not necessarily indicative of the results to be expected for the entire fiscal year.

### 2. COMMON STOCK

During the nine months ended September 30, 2002, the following shares of common stock were issued:

For services	580,272 shares valued at \$213,500
For cash	2,330,403 shares valued at \$780,998
Exercise of stock option	78,123 shares valued at \$8
Total	2,988,798

The above common shares issued for services received represent value to the Company at the market value of those services.

During the three month period, 315,000 stock options were granted to consultants, lawyers and employees, the valuation of which resulted in additional legal fees of \$5,784, consulting fees of \$4,402. Had

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compensation expense been determined for 800,000 options to acquire shares as provided in SFAS 123 using the Black-Scholes option pricing model, the pro forma effect on the Company's net loss would be to increase the net loss for the nine months ended September 30, 2002 by \$(234,800) to \$(581,339) and to increase the net loss per share to \$(0.059)

Item 2. Management's Discussion and Analysis or Plan of Operation. The following discussion should be read in conjunction with the accompanying unaudited consolidated financial statements prepared by management for the nine month periods ended September 30, 2002 and September 30, 2001 and the audited consolidated financial statements for the twelve months ended December 31, 2001 as presented in the Company's Form 10KSB.

Although the Company has experienced a net loss at September 30, 2002, it has expended considerable effort in developing new business in new markets for NetMind and for new design and contract manufacturing work.

Funding has been provisionally approved for the AQUACOMM sonar technology development program by the Canadian federal government. The AQUACOMM project funding will be received over a period of three years. The first progress payment is now expected to be received in December, which will include partial reimbursement for work done over the past year.

### Special Note Regarding Forward Looking Statements

Certain statements in this report and elsewhere (such as in other filings by the company with the Securities and Exchange Commission ("SEC"), press releases, presentations by the company of its management and oral statements) may constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," and "should," and variations of these words and similar expressions, are intended to identify these forward-looking statements. Actual results may materially differ from any forward-looking statements. Factors that might cause or contribute to such differences include, among others, competitive pressures and constantly changing technology and market acceptance of the company's products and services. The company undertakes no obligation to publicly release the result of any revisions to these forward-looking statements, which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

### The Company's Services

The Company, through its subsidiaries, is a Multiple Applications underwater sonar technology developer, a defense electronics manufacturer and a defense systems integrator.

The Company's operations currently are those of its wholly owned subsidiaries Northstar Technical Inc. (NTI) and Northstar Network Ltd (NN) and it is in this context that the company's services are described.

### Underwater Sonar Products and Technologies

#### a - The NETMIND System

The Company's first underwater sonar product based on our core technology was the NETMIND system. NETMIND's market is the world's commercial fishing industry and government oceanic research agencies. One of our largest customers has been the United States National Oceanic and Atmospheric Administration (NOAA).

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NETMIND is both a conservation tool as well as an efficiency tool. Electronic sensors attached to a fishing trawl measure the height and width of the net opening, the water temperature, the depth of the net and the amount of fish caught plus other parameters. The sensor information is transmitted via a wireless communications link back to the ship.

NETMIND helps prevent over fishing and allows fishermen to catch fewer fish and still make profits. This gives regulators flexibility in reducing quotas when attempting to conserve limited fish stocks.

Sales for NETMIND have been somewhat slower than expected during this Nine months period. Sales have not expanded in Europe as we had anticipated. However, an upswing in activity over the next six months is expected.

### b - The AQUACOMM Project

The AQUACOMM project involves the development of new, leading edge multiple application sonar technologies and products for a variety of industries. These include defense, offshore oil and gas, commercial fishing, oceanography, marine environment and marine transportation. The Company's funding for AQUACOMM totaling US\$2,394,000 includes \$2,040,000 from the Canadian federal government comprising \$1,420,000 from the Atlantic Innovation Fund (announced July 9,2002), \$230,000 from the National Research Council (announced August 14,2002) and \$390,000 from Scientific Research tax credits (cash refunds made after each fiscal year end based on eligible research and development expenses). The balance is being funded through equity financing. The AQUACOMM development is scheduled to last three years.

At September 30, 2002, the company recorded \$122,100 in expenses and \$36,100 in tax credits recoverable pursuant to the AQUACOMM project.

The Company intends to use its Venture Technology Business Model to maximize the success of the new AQUACOMM technologies. In this model, our core technology is invested in partnerships with established companies in the different industry sectors.

One example of our modus operandi would be the co-development of a military underwater communications system. We would develop the 'wet' end and a large defense contractor would develop the 'dry' end. The defense contractor, being well established in the field, would be responsible for product introduction, marketing and sales. Another example is the development of a mooring line monitoring system for the offshore oil and gas industry. We expect to have such a system ready for commercial sale by the second quarter of 2003 and we intend to market it through a strategic alliance with an international oil field company.

Should our Venture Technology Business Model prove to be successful, we intend to provide up to ten new products arising from the AQUACOMM project to be sold by established companies in their sectors of influence.

### c - Defense Sonar System

During this quarter the Company secured a contract to design and construct prototype sonar hardware for a defense protection system. It is designed for the protection of navy ships, ports and harbors.

We expect that Homeland Security and Anti Terrorism will become a major part of our business over the next five years with production of these and other systems.

Electronic Contract Manufacturing

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In the fall of 1999 we signed a contract with Lockheed Martin, Manassas, Virginia to fabricate and test control consoles for Navy submarines. This contract was successfully completed in early 2001. A follow-on contract was received and completed in the fall of 2001. Further console contracts are expected in the future.

We are attempting to expand our electronic contract manufacturing business with our current customers, as well as with customers in the offshore oil and gas, transportation and communication industries.

### Systems Integration

The Company is developing its approach to securing and executing large defense contracts by bringing together affiliate companies. The overall capability, which is substantial, is presented to the prime contractors. To date, a memorandum of understanding has been signed with Lockheed Martin Canada to jointly pursue the \$2.0 billion Maritime Helicopter Project.

The aforementioned defense sonar system is an example of how Systems Integration will work for us. In this project, we have four subcontractors who carry out various tasks, with Northstar bringing all the component parts together for final assembly, testing, quality control and delivery to the customer.

### Subsequent Events

Subsequent to September 30, 2002 the Company issued 109,930 shares of common stock for cash of \$40,735.

### Results of Operations

Comparison of the three and nine months ended September 30, 2002 with the three and nine months ended September 30, 2001.

Revenue for the three months ended September 30, 2002 was \$274,347 compared to \$285,546 of revenue recorded during the same period of the prior year. Revenue for the nine months ended September 30, 2002 was \$639,125 compared to \$840,515 of revenue during the same period of the prior year. The decrease between the two nine month periods was created by the absence of the Lockheed Martin contract, which was completed during the first quarter of 2001. Gross profits decreased from \$620,476 (74%) in the prior period to \$367,434 (57%) in the current period. The percentage decrease was created by a higher percentage of sales being attributable to NETMIND, which lost some profit margin to competitive pricing and to increased dealer discounts. The Company continues to negotiate for subsequent material contracts with Lockheed Martin and others.

The Company experienced a net loss from operations for the three and nine month periods ended September 30, 2002 of \$(118,762) and \$(504,739) compared to a net loss from operations for the three and nine month periods ended September 30, 2001 of \$(108,520) and \$(230,594)], respectively. This loss resulted from increased costs of salaries, professional fees, and expenses incurred in developing the Company's Northstar Network business plan. To date, Northstar Network has expended \$265,000 in business development. The company also increased its NETMIND marketing efforts through advertising, trade shows and by offering a more attractive commission structure to its dealers. The Company increased its loss position by investing further into the development and promotion of a broader market for its core underwater communications technology.

During the quarter, the Company categorized \$203,857 as research and development costs, reclassifying \$179,535 from salaries, \$12,800 from rent, \$4,545 from heat light and telephone and \$6,977 from office expenses, reducing each category by the respective amount, to more properly reflect



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the expenditures as research and development. At September 30, 2002, the company recorded \$122,100 in expenses recoverable and \$36,100 in tax credits recoverable pursuant to the AQUACOMM project, resulting in net income for the three month period ended September 30, 2002 of \$39,438 after taking into account the recoveries, and reduced the nine months loss from operations of \$(504,739) to a net loss of \$(346,539).

Comparison of Financial Position at September 30, 2002 with September 30, 2001

The Company's working capital position remained positive at September 30, 2002 with current assets of \$617,963 in excess of current liabilities of \$500,858 by \$117,105. At December 31, 2001 the Company had a working capital deficiency of \$(251,254).

### Liquidity and Capital Resources

For the Company to continue its expenditures at the current rate it must increase sales, increase its debt or raise equity.

## PART II - OTHER INFORMATION

### Item 1. Legal Proceedings.

No change since previous filing.

### Item 2. Changes in Securities.(during period)

Options Granted	Date	Exercise Price	Expiry Date
175,000	June 25, 2002	\$0.50	June 25, 2007
125,000	June 25, 2002	\$0.75	June 25, 2007
815,000	July 05, 2002	\$0.50	July 05, 2007

Total options outstanding at September 30, 2002: 2,719,000

Common Stock Issued	Date	Consideration
21,759	January, 2002	\$ 7,949
186,704	February, 2002	\$ 56,012
769,400	March, 2002	\$259,510
383,514	April, 2002	\$131,385
308,278	May, 2002	\$ 88,408
496,438	June, 2002	\$102,331
280,000	July, 2002	\$ 87,888
80,910	July, 2002	services
85,800	August, 2002	\$ 26,930
86,430	August, 2002	services
254,900	September, 2002	\$ 80,008
34,665	September, 2002	services

### Item 3. Defaults Upon Senior Securities.

No change since previous filing.

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

No change since previous filing.

### Item 5. Other Information.

No change since previous filing.

### Item 6. Exhibits and Reports on form 8-K.

No change since previous filing.

## SIGNATURES

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

November 12, 2002

Northstar Electronics, Inc.

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(Registrant)

By: /s/ Wilson Russell  
Wilson Russell, PhD  
President  
Principal Financial Officer

CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER PURSUANT TO 18 W.S.C. SECTION 1350 AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002, the undersigned Chief Executive Officer and chief Financial Officer, or persons fulfilling similar functions, each certify:

- (i) That the financial information included in this Quarterly Report fairly presents in all material respects the financial condition and results of operations of the Company as of September 30, 2002 and for the periods presented in the report; and
- (ii) That the Quarterly Report fully complies with the requirements of Sections 13(a) or 15(d) of the Securities exchange Act of 1934

By: /s/ Wilson Russell  
Title: Chief Executive Officer  
And Chief Financial Officer

Date: November 12, 2002  
And Chief Financial Officer

Date: November 12, 2002