PROFILE TECHNOLOGIES INC
Form 10QSB
February 14, 2002

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

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

For the quarterly period ended December 31, 2001

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

For the transition period from ________________ to ______________

Commission file number 0-21151

PROFILE TECHNOLOGIES, INC.
(Exact name of small business issuer as specified in its charter)

DELAWARE	91-1418002
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
Two Park Avenue, Suite 201, Manhasset, NY	11030
(Address of principal executive offices)	(Zip Code)

516-365-1909
(Issuer's telephone number)

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

Applicable only to corporate issuers

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: On February 7, 2002, there were 4,957,092 shares of common stock outstanding.

Transitional Small Business Disclosure Format (Check one): Yes [ ] No [X]

PART I-- FINANCIAL INFORMATION

Item 1. Financial Statements.

PROFILE TECHNOLOGIES, INC.
Condensed Balance Sheets
(unaudited)

Assets	December 31, 2001	June 3 2001
Current assets:		
Cash and cash equivalents	$ 125,641	$ 306
Accounts receivable	171,982	32
Contract work-in-progress	--	17
Prepaid expenses and other current assets	11,276	31
Total current assets	308,899	388
Equipment, net	196,919	212
Patents, net	188,196	230
Other assets	12,108	11
Total assets	$ 706,122	$ 842
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable - stockholder	$ --	$ 3
Other accounts payable	70,799	52
Accrued liabilities	72,569	21
Total current liabilities	143,368	77
Stockholders' equity:		
Common stock, $0.001 par value. Authorized 10,000,000 shares; issued an outstanding 4,949,592 shares at December 31, 2001 and 4,285,092 at June 30, 2001	4,950	4
Additional paid-in capital	7,943,623	7,585
Accumulated deficit	(7,385,819)	(6,825
Total stockholders' equity	562,754	764
Total liabilities and stockholders' equity	$ 706,122	$ 842

See accompanying notes to condensed financial statements.

PROFILE TECHNOLOGIES, INC.
Condensed Statements of Operations
(unaudited)

	For the three months ended December 31, 2001	For the three months ended December 31, 2000	For the D 2001
Revenue	$ 63,365	$ 31,329	$ 404,5
Cost of revenue	112,464	102,989	254,0
Gross profit (loss)	(49,099)	(71,660)	150,5
Operating Expenses:			
Research and development	98,720	93,741	171,5
Selling, general and administrative	249,545	283,469	540,3
Total operating expenses	348,265	377,210	711,9
Loss from operations	(397,364)	(448,870)	(561,4
Interest income	167	17,665	9
Net loss	$ (397,197)	$ (431,205)	$ (560,4
Basic and diluted net loss per share	$ (0.08)	$ (0.10)	$ (0.
Shares used to calculate basic and diluted net loss per share	4,773,904	4,285,092	4,655,

See accompanying notes to condensed financial statements.

PROFILE TECHNOLOGIES, INC.
Condensed Statements of Cash Flows
(unaudited)

	For the six months December 31, 2001
Cash flows from operating activities:	
Net loss	$ (560,457)
Adjustments to reconcile net loss to net cash used in	

operating activities:	
Depreciation and amortization	84,701
Stock compensation expense	--
Changes in certain assets and liabilities:	
Accounts receivable	(139,853)
Contract work-in-progress	17,850
Prepaid expenses and other current assets	20,693
Other assets	(1,100)
Accounts payable - stockholder	(3,262)
Other accounts payable	18,275
Accrued liabilities	51,058
Net cash used in operating activities	(512,095)
Cash flows from investing activities-purchases of equipment	(26,780)
Cash flows from financing activities- issuance of common stock and warrants, net of offering costs	358,458
Net decrease in cash and cash equivalents	(180,417)
Cash and cash equivalents at beginning of the period	306,058
Cash and cash equivalents at end of the period	$ 125,641

See accompanying notes to condensed financial statements.

PROFILE TECHNOLOGIES, INC
December 31, 2001
Notes to Unaudited Condensed Financial Statements

1. Description of Business

Profile Technologies, Inc. (the "Company") is in the business of developing and commercializing potential processes for the nondestructive, noninvasive testing of both above ground and buried pipelines for the effectiveness of pipeline cathodic protecting systems and coating integrity. The Company's future revenues are currently dependent upon the market's acceptance of its sole developed process.

2. Basis of Presentation

The unaudited interim condensed financial statements and related notes of the Company have been prepared pursuant to the instructions to Form 10-QSB. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted pursuant to such instructions. The condensed financial statements and related notes should be read in conjunction with the audited financial statements and notes thereto included in the Company's annual report on form 10-KSB for the year ended June

30, 2001 (filed September 28, 2001). The information furnished reflects, in the opinion of management, all adjustments, consisting of only normal recurring items necessary for fair presentation of the results of the interim periods presented. Interim results are not necessarily indicative of results for a full year.

3. Net Loss Per Share

Basic loss per share is computed by dividing the net loss by the weighted average number of common shares outstanding during the period. Diluted loss per share is computed by dividing the net loss by the weighted average number of common and dilutive common equivalent shares outstanding during the period. As the Company had a net loss attributable to common shareholders in each of the periods presented, basic and diluted net loss per share is the same.

Excluded from the computation of diluted loss per share for the three and six months ended December 31, 2001 are options and warrants to acquire approximately 2,295,000 shares of common stock with a weighted-average exercise price of $3.03 because their effect would be antidilutive. Excluded from the computation of diluted loss per share for the three and six months ended December 31, 2000 are options and warrants to acquire approximately 1,381,000 shares of common stock with a weighted-average exercise price of $4.19 because their effect would be antidilutive.

4. Sale of Common Stock

During the six months ended December 31, 2001, the Company raised gross proceeds of $398,700 from the sale of 664,500 shares of common stock and issued one warrant in connection with each share of common stock sold. The warrants are exercisable at $1.00 per share until September, 2006. Each share of common stock and warrant was sold for a total of $0.60. Directors and related parties to the directors purchased a total of apaproximately 300,000 shares of common stock.

5. Liquidity

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. The Company incurred cumulative losses of $7,385,819 through December 31, 2001 and has working capital of $165,531 as of December 31, 2001. The Company has expended a significant amount of cash in developing its technology and patented processes. Management recognizes that in order to meet the Company's ongoing operating and capital requirements, additional financing will be necessary over the next two to three months to continue as a going concern. The Company is evaluating alternative sources of financing to improve its cash position and is undertaking efforts to raise capital. If the Company is unable to raise additional capital or secure additional revenue contracts and generate positive cash flow, there can be no assurance that the Company will be able to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

To reduce cash outflows, certain of the Company's employees, officers and directors have agreed to defer a portion of their salaries and consulting fees from August 2001 through December 2001 until the Company has sufficient resources to pay the amounts owed. At December 31, 2001, the Company accrued approximately $70,000 related to the deferred payment of the salaries and consulting fees which is included under accrued liabilities.

6. NASDAQ Delisting

On June 27, 2001, the Company announced that it received a Nasdaq Staff Determination on June 20, 2001, indicating that the Company failed to comply with the minimum bid price and net tangible asset/shareholder equity requirements of the Nasdaq Marketplace Rules for continued listing set forth in Marketplace Rule 4310(c)(4), and that its securities were, therefore, subject to delisting from the Nasdaq SmallCap Market. On August 10, 2001, the Nasdaq Stock Market suspended trading in the Company's common stock. Effective Monday, August 13, 2001, the Company began trading on the Over the Counter Bulletin Board under the symbol PRTK.

7. New Accounting Pronouncements

In July 2001, the FASB issued Statement No. 141, "Business Combinations", and Statement No. 142, "Goodwill and Other Intangible Assets". Statement No. 141 requires business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting, and specifies criteria for recognizing intangible assets acquired in a business combination. Statement No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead be tested for impairment at least annually. Intangible assets with definite useful lives, such as the Company's patents, which have a net book value of $188,196 as of December 31, 2001, will continue to be amortized over their respective estimated useful lives. The Company is required to adopt the provisions of Statement No. 141 immediately and Statement No. 142 effective July 1, 2002. The impact of adopting Statement No. 141 was not material. The adoption of Statement No. 142 is not expected to have a material impact on the Company's financial statements.

In October, 2001 the FASB issued FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. While Statement No. 144 supersedes FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", it retains many of the fundamental provisions of that Statement. Statement No. 144 also supersedes the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations--Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions", for the disposal of a segment of a business. However, it retains the requirement in Opinion No. 30 to report separately discontinued operations and extends that reporting to a component of an entity that either has been disposed of (by sale, abandonment, or in a distribution to owners) or is classified as held for sale. The Company is required and plans to adopt the provisions of Statement No. 144 for the fiscal year beginning July 1, 2002. The adoption of this statement is not expected to have a material impact on the Company's financial statements.

Item 2. Management's Discussion and Analysis or Plan of Operation.

GENERAL

Since its inception in 1988, Profile Technologies, Inc. (the "Company"), a Delaware corporation, has been engaged in the business of researching and developing a high speed scanning process, which is nondestructive and noninvasive, to test remotely buried and insulated pipelines for corrosion. The Company's electromagnetic wave inspection process, referred to as EMW, is a patented process of analyzing the waveforms of electrical impulses in a way that extracts point-to-point information along a segment of pipeline to illustrate the integrity of the entire pipeline. This process involves sending an electrical pulse along the pipe being tested from each of two locations toward varying intersecting points between the two locations. At least one of the modified pulses is analyzed to determine whether an anomaly exists at the intersecting location.

This process is designed to detect external corrosion of pipelines without the need for taking the line out of service, physically removing the insulation, or uncovering the pipe, and then visually inspecting the outside of the pipe for corrosion. Often the Company can inspect the pipelines by using various access points to the pipeline that already exist for other reasons. Where such access is not already available, the Company's technology permits inspection of pipelines with only a very minimal amount of disturbance of the covering or insulation that is present on the pipeline. Finally, the Company's technology permits an inspection of the entire pipeline, as opposed to other technologies which only conduct inspections at the points selected for the testing.

Sales

We derive revenue from the sale of the EMW inspection service and from research and development activities that have been sponsored by large multinational oil companies and large utilities. The Company relies upon several employees, including the Chief Executive Officer, the Chief Operating Officer and the Vice President - Field Operations, for the Company's sales functions. The Company relies solely upon the employees of the Company to conduct its sales activities.

During the six months ended December 31, 2001 and 2000, all of the Company's sales were attributable to four and five customers, respectively. Two of the Company's customers individually accounted for 36% and 52% of net sales for the six months ended December 31, 2001, and one customer accounted for 89% of net sales for the six months ended December 30, 2000.

Marketing

The Company's sales and marketing strategy includes positioning the Company's EMW as the method of choice to detect pipeline corrosion where the pipelines are either inaccessible to other inspection tools or much more costly to inspect with tools other than the Company's EMW inspection. The Company does not have a designated sales force, but currently relies upon several employees, including the Chief Executive Officer, the Chief Operating Officer and the Vice President - Field Operations, for the Company's sales functions.

RESULTS OF OPERATIONS

Revenue increased to $63,365 for the three months and $404,573 for the six months ended December 31, 2001, compared to $31,329 for the three months and $277,750 for the six months ended December 31, 2000. This increase was primarily due to additional work performed on the North Slope of Alaska. The Company's revenues have historically been fairly seasonal with revenues lowest during the winter months.

Cost of revenue increased to $112,464 for the three months and $254,072 for the six months ended December 31, 2001, compared to $102,989 for the three months and $253,539 for the six months ended December 31, 2000.

Gross loss was $49,099 for the three months and gross profit was $150,501 for the six months ended December 31, 2001, compared to a gross loss of $71,660 for the three months and gross profit of $24,211 for the six months ended December 31, 2000. The increase in gross profit for the six months ended December 31, 2001 as compared to the same period in the prior year is primarily due to efficiencies in the testing services performed and certain fixed costs that do not fluctuate based on revenue.

Research and development expenses increased to $98,720 for the three months and $171,563 for the six months ended December 31, 2001, compared to $93,741 for the three months and $126,221 for the six months ended December 31, 2000. The increase for the six month period ended December 31, 2001, compared to the six month period ended December 31, 2000, was due to certain employees spending more time on research and development and less time on revenue generating contracts.

General and administrative expenses decreased to $249,545 for the three months and $540,378 for the six months ended December 31, 2001, compared to $283,469 for the three months and $533,714 for the six months ended December 31, 2000. The decrease for the three months ended December 31, 2001 is due to the Company incurring higher recruiting and training costs in the prior year related to the Company's efforts to increase the size of its operations.

Loss from operations decreased to $397,364 for the three months and $561,440 for the six months ended December 31, 2001, compared to $448,870 for the three months and $635,724 for the six months ended December 31, 2000. The decrease for the three months ended December 31, 2001 compared to the same period in the prior year is due to higher revenues. As a result of the Company's cost structure including a significant amount of fixed costs, fluctuations in revenue will significantly impact the Company's gross margin and loss from operations.

Interest income decreased to $167 for the three months and $983 for the six months ended December 31, 2001, down from $17,665 for the three months and $39,829 for the six months ended December 31, 2000. This decrease was the result of declining cash and cash equivalent balances as the Company used such resources to sustain its commercial operations and research and development activities and lower rates of return on invested funds.

LIQUIDITY AND CAPITAL RESOURCES

Net cash used in operating activities was $512,095 for the six months ended December 31, 2001, compared with $609,344 for the six months ended December 31, 2000. The decrease in the cash used in operating activities is primarily as a result of an agreement by certain employees, officers and directors of the Company to defer the payment of a portion of their salaries and consulting fees until the Company has sufficient resources to pay the amounts accrued. At December 31, 2001, the Company has accrued approximately $70,000 related to the deferred payment of the salaries and consulting fees which is included under accrued liabilities.

Net cash used in investing activities was $26,780 for the six months ended December 31, 2001, compared with $16,530 for the six months ended December 31, 2000. The Company's investing activities consisted of the purchase of additional office and field equipment.

Net cash from financing activities was $358,458 for the six months ended December 31, 2001, compared to $0 for the six months ended December 31, 2000. The net cash provided by financing activities was due to the sale of common stock and warrants.

The Company's cash and cash equivalents as of December 31, 2001 were $125,641, compared to $306,058 as of June 30, 2001 and $1,118,158 as of December 31, 2000, and the Company had no material long-term commitments or material commitments for capital expenditures.

Management is currently directing the Company's activities towards obtaining additional service contracts, which will necessitate the Company attracting, hiring, training and outfitting qualified technicians. The Company's intention is to purchase such equipment for its field crews for the foreseeable future, until such time as the scope of operations may require alternate sources of financing equipment. There can be no assurance that the Company's process will gain widespread commercial acceptance within any particular time frame, or at all. The Company will incur additional expenses as it hires and trains field crews and support personnel related to the successful receipt of commercial contracts. At the present time the Company anticipates that it may need one additional crew to service future contracts, but it cannot be certain until contract negotiations are complete.

Capital will be expended to support operations until the Company can generate sufficient cash flows from operations. In order for the Company to generate cash flows from operations, the Company must secure additional revenue generating contracts. The Company expects that accounts receivable and contract work-in-progress will continue to increase to the extent revenues rise. Any such increase that occurs at the same time or at a greater rate than an increase in revenue can be expected to reduce cash. Additionally, the Company anticipates that cash will be used to meet capital expenditure requirements necessary to develop infrastructure to support the future growth. There can be no assurance that the Company will be able to secure additional revenue generating contracts to provide sufficient cash.

The Company has incurred cumulative losses of $7,385,819 through December 31, 2001 and had working capital of only $165,531 as of December 31, 2001. During the six months ended December 31, 2001, the Company used $512,095 of cash in operating activities. With working capital of only $165,531 at December 31, 2001, the Company will need additional financing over the next two to three months to be able to continue as a going concern. Management recognizes that in order to meet the Company's on-going capital and operating expense requirements, additional financing, in addition to the net proceeds of $145,750 raised from October 1, 2001 through December 31, 2001 will be necessary. The Company is evaluating alternative sources of financing, including seeking industry-partner investment through joint venture or other possible arrangements, to improve its cash position and is also undertaking efforts to raise capital from more conventional sources. Further, the Company is making on-going efforts to reduce its on-going expense requirements including payroll. If the Company is unable to raise additional capital or secure additional revenue contracts and generate positive cash flow, there can be no assurance that the Company will be able to continue as a going concern.

FORWARD-LOOKING STATEMENTS

Some of the statements under "Management's Discussion and Analysis of Financial Condition and Results of Operations," and elsewhere in this Report and in the Company's periodic filings with the Securities and Exchange Commission constitute forward-looking statements. These statements involve known and unknown risks, significant uncertainties and other factors that may cause actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements.

In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "could," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "potential" or "continue" or the negative of such terms or other comparable terminology.

The forward-looking statements herein are based on current expectations that involve a number of risks and uncertainties. Such forward-looking statements are based on assumptions that the Company will obtain or have access to adequate financing for each successive phase of its growth, that the Company will market and provide products and services on a timely basis, that there will be no material adverse competitive or technological change in condition of the Company's business, that demand for the Company's products and services will significantly increase, that the Company's executive officers will remain employed as such by the Company, that the Company's forecasts accurately anticipate market demand and that there will be no material adverse change in the Company's operations, business or governmental regulation affecting the Company or its customers. The foregoing assumptions are based on judgments with respect to, among other things, future economic, competitive and market conditions, and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond the Company's control.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of such statements.

PART II-- OTHER INFORMATION

Item 1. Legal Proceedings.

The Company is not a party to any pending or threatened legal proceedings.

Item 2. Changes in Securities.

In connection with a confidential offering memorandum dated July 9, 2001, as supplemented, the Company raised, between October 1, 2001 and the date of this filing $145,750 through stock subscriptions for 242,833 shares of our common stock and warrants to acquire 242,833 shares of our common stock in a private placement of securities. The warrants have an exercise price of $1.00 and can be exercised prior to November 30, 2006. The shares and the warrants were offered directly by the Company, the Talisman Group and R.F. Lafferty. The Talisman Group and R.F. Lafferty did not place any of the shares and warrants. All of the investors were accredited investors. We relied on Section 4(2) of the Securities Act and on Rule 506 of Regulation D in selling the shares and warrants without registering the offering under the Securities Act.

Item 3. Defaults Upon Senior Securities.

None.

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

(a) The annual meeting of the Company's shareholders was held on November 13, 2001.

(b) At such annual meeting, the stockholders of the Company elected G. L. Scott, Henry E. Gemino, Murphy Evans, John Tsungfen Kuo, Charles Christenson and William A. Krivsky as directors for one-year terms. The elections were approved by the following votes:

Directors	For	Withheld
G. L. Scott	3,652,999	259,712
Henry E. Gemino	3,628,999	283,712
Murphy Evans	3,639,999	272,712
John Tsungfen Kuo	3,062,799	849,912
Charles Christenson	3,653,799	258,912
William A. Krivsky	3,653,799	258,912

Item 5. Other Information.

Effective January 1, 2002, Dr. John T. Kuo retired as Chief Technology Officer. However, Dr. Kuo will remain on the Company's Board as Vice Chairman and, in that capacity, will help guide the further development of the Company's technology. In this connection, the Company has retained Dr. Marcus Zahn of M.I.T. to model the Company's data interpretation process mathematically in what it is hoped will be the first step in a successful automation of that process.

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits.

None

(b) Reports on Form 8-K

None

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.

/s/ PROFILE TECHNOLOGIES, INC.
(Registrant)

Date: February 14, 2002

/s/ Henry E. Gemino
Henry E. Gemino
Chief Executive Officer;
Chief Financial Officer