

NEW CENTURY COMPANIES INC
Form 10QSB
May 15, 2007

SECURITIES EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

TRANSACTION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For Quarter Ended:
March 31, 2007

Commission File Number:
0-7722

NEW CENTURY COMPANIES, INC.
(Exact name of Registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of
Incorporation or organization)

061034587
(IRS Employer Identification
Number)

9835 Santa Fe Springs Road
Santa Fe Springs, CA 90670
(Address of Principal Executive Offices) (Zip Code)

(562) 906-8455
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes No

The number of shares of Common Stock, par value \$0.10 per share, outstanding as of March 31, 2007 was 12,264,656.

Transitional Small Business Disclosure Format (check one): Yes No

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (Unaudited)

The consolidated Financial Statements are set forth at the end of this document.

CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Balance Sheet F-1

Consolidated Statements of Operations F-2

Consolidated Statements of Cash Flows F-3

Notes to Consolidated Financial Statements F-4 - F-15

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS 3

ITEM 3. CONTROLS AND PROCEDURES 8

PART II OTHER INFORMATION 9

ITEM 1. LEGAL PROCEEDING 9

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS 9

ITEM 3. DEFAULTS UPON SENIOR SECURITIES 9

ITEM 4. SUBMISSION OF MATERS TO A VOTE OF SECURITY HOLDERS 9

ITEM 5. OTHER INFORMATION 9

ITEM 6. EXHIBITS 11

ITEM 1. FINANCIAL STATEMENTS

The consolidated Financial Statements are set forth at the end of this document.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion should be read in conjunction with the Company's consolidated financial statements and the notes thereto appearing elsewhere in this Form 10-QSB. Certain statements contained herein that are not related to historical results, including, without limitation, statements regarding the Company's business strategy and objectives, future financial position, expectations about pending litigation and estimated cost savings, are forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended (the "Securities Exchange Act") and involve risks and uncertainties. Although the Company believes that the assumptions on which these forward-looking statements are based are reasonable, there can be no assurance that such assumptions will prove to be accurate and actual results could differ materially from those discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, regulatory policies, and market and general policies, competition from other similar businesses, and market and general economic factors. All forward-looking statements contained in this Form 10-QSB are qualified in their entirety by this statement.

OVERVIEW

The Company is engaged in acquiring, re-manufacturing and selling pre-owned Computer Numerically Controlled ("CNC") machine tools to manufacturing customers. The Company provides rebuilt, retrofit and remanufacturing services for numerous brands of machine tools. The remanufacturing of a machine tool, typically consisting of replacing all components, realigning the machine, adding updated CNC capability and electrical and mechanical enhancements, generally takes two to four months to complete. Once completed, a remanufactured machine is a "like new," state-of-the-art machine with a price ranging from \$275,000 to \$1,000,000, which is substantially less than the price of a new machine. The Company also manufactures original equipment CNC large turning lathes and attachments under the trade name Century Turn.

CNC machines use commands from onboard computers to control the movements of cutting tools and rotation speeds of the parts being produced. Computer controls enable operators to program operations such as part rotation, tooling selection and tooling movement for specific parts and then store the programs in memory for future use. The machines are able to produce parts while left unattended. Because of this ability, as well as superior speed of operation, a CNC machine is able to produce the same amount of work as several manually controlled machines, as well as reduce the number of operators required; generating higher profits with less re-work and scrap. Since the introduction of CNC tooling machines, continual advances in computer control technology have allowed for easier programming and additional machine capabilities.

A vertical turning machine permits the production of larger, heavier and more oddly shaped parts on a machine, which uses less floor space when compared to the traditional horizontal turning machine because the spindle and cam are aligned on a vertical plane, with the spindle on the bottom.

The primary industry segments in which the Company's machines are utilized to make component parts are in aerospace, power generation turbines, military, component parts for the energy sector for natural gas and oil exploration and medical fields. The Company sells its products to customers located in United States, Canada and Mexico.

Over the last four years, the Company has designed and developed a large horizontal CNC turning lathe with productivity features new to the metalworking industry. The Company believes that a potential market for the Century Turn Lathe, in addition to the markets mentioned above, is aircraft landing gear.

We provide our manufactured and remanufactured machines as part of the machine tool industry. The machine tool industry worldwide is approximately a 30 billion dollar business annually. The industry is sensitive to market conditions and generally trends downward prior to poor economic conditions, and improves prior to an improvement in economic conditions.

Our machines are utilized in a wide variety of industry segments as follows: aerospace, energy, valves, fittings, oil and gas, machinery and equipment, and transportation. With the recent downturn in the aerospace industry, we have seen an increase in orders from new industries such as defense and medical industries.

OVERVIEW OF OPERATIONS

The Company's current strategy is to expand its customer sales base with its present line of machine products. The Company's growth strategy also includes strategic acquisitions in addition to growing the current business. Plans for expansion are funded through current working capital from ongoing sales. However, significant growth will require additional funds in the form of debt or equity, or a combination thereof. The Company's growth strategy also includes strategic acquisitions in addition to growing the current business. A significant acquisition will require additional financing.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2007 COMPARED TO MARCH 31, 2006.

Revenues. The Company generated revenues of \$3,185,469 for the three months ended March 31, 2007, which was a \$1,485,622 or 87% increase from \$1,699,847 for the three months ended March 31, 2006. The increase is the result of an increase in sales volume and higher selling prices of New Century machines due to a decrease in availability for competitive machines.

Gross Profit. Gross profit for the three months ended March 31, 2007, was \$1,185,239 or 37% of revenues, compared to \$403,239, or 24% of revenues for the three months ended March 31, 2006, a 194% increase. The increase in gross profit is due to the increased volume of sales and higher selling prices.

Operating Income. Operating income for the three months ended March 31, 2007, was \$465,966 compared to an operating loss of (\$51,790) for the three months ended March 31, 2006. The increase of \$517,756 or 1000% in operating income is primarily due to the increase in sales revenues.

Interest Expense. Interest expense for the three months ended March 31, 2007, was \$465,241 compared with \$395,828 for the three months ended March 31, 2006. The 18% increase in interest expense is due to a full three months of amortization in the first quarter of year 2007 compared with one and a half months in the quarter ended March 31, 2006 of following items:

- Approximately \$84,000 of interest expense on convertible note;
- Approximately \$292,000 of amortization of debt discounts from beneficial conversion feature, warrants and a conversion option;
- Approximately \$90,000 of amortization of deferred financing costs related to warrants and common stock granted to third parties as financing cost on convertible note;

all associated to \$3.5 million convertible notes payable issued on February 15, 2006.

FINANCIAL CONDITION, LIQUIDITY, CAPITAL RESOURCES

The net cash increase of the Company during the three months ended March 31, 2007 was \$264,488. The increase is due to net cash provided by operating activities of \$611,272, offset by \$346,784 net cash used in financing activities, cash used to pay down the Company's convertible notes.

For the three months ended March 31, 2007, the cash provided by operating activities was \$611,272, compared with \$788,046 cash used in operating activities in the corresponding period from 2006. The increase in cash provided by operating activities is a result of increased sales.

For the three months ended March 31, 2007, the cash used in financing activities was \$346,784, compared with \$1,075,851 cash provided by financing activities in the three months ended March 31, 2006. The decrease of cash provided by financing activities is primarily due to \$3,800,000 of proceeds from the issuance of two convertible notes in 2006, compared to no cash proceeds from debt or equity in 2007.

INFLATION AND CHANGING PRICES

The Company does not foresee any adverse effects on its earnings as a result of inflation or changing prices.

GOING CONCERN

The Company has an accumulated deficit of approximately \$7,800,000. This condition, among others, raises substantial doubt about the Company's ability to continue as a going concern. The Company intends to fund operations through anticipated increased sales along with debt and equity financing arrangements. The successful outcome of future activities cannot be determined at this time and there is no assurance that if achieved, the Company will have sufficient funds to execute its intended business plan or generate positive operating results.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America requires management to make judgments, assumptions and estimates that affect the amounts reported in our consolidated financial statements and the accompanying notes. The amounts of assets and liabilities reported on our balance sheet and the amounts of revenues and expenses reported for each of our fiscal periods are affected by estimates and assumptions, which are used for, but not limited to, the accounting for revenue recognition, accounts receivable, doubtful accounts and inventories. Actual results could differ from these estimates. The following critical accounting policies are significantly affected by judgments, assumptions and estimates used in the preparation of the financial statements:

Revenue Recognition

Service revenues are billed and recognized in the period the services are rendered.

The Company accounts for shipping and handling fees and costs in accordance with EITF 00-10 "Accounting for Shipping and Handling Fees and Costs." Such fees and costs incurred by the Company are immaterial to the operations of the Company.

In accordance with SFAS 48, "Revenue Recognition when Right of Return Exists," revenue is recorded net of an estimate of markdowns, price concessions and warranty costs. Such reserve is based on management's evaluation of historical experience, current industry trends and estimated costs.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin 101 ("SAB 101"), "Revenue Recognition," as amended by SAB No. 104 which outlines the basic criteria that must be met to recognize revenue and provides guidance for presentation of revenue and for disclosure related to revenue recognition policies in financial statements filed with the Securities and Exchange Commission. Management believes that the Company's revenue recognition policy for services and product sales conforms to SAB 101 amended by SAB 104. The Company recognizes revenue of long-term contracts pursuant to SOP 81-1.

Method of Accounting for Long-Term Contracts

The Company uses the percentage-of-completion method of accounting to account for long-term contracts and, therefore, takes into account the cost, estimated earnings and revenue to date on fixed-fee contracts not yet completed. The percentage-of-completion method is used because management considers total cost to be the best available measure of progress on the contracts. Because of inherent uncertainties in estimating costs, it is at least reasonably possible that the estimates used will change within the near term.

The amount of revenue recognized at the statement date is the portion of the total contract price that the cost expended to date bears to the anticipated final cost, based on current estimates of cost to complete. It is not related to the progress billings to customers. Contract costs include all materials, direct labor, machinery, subcontract costs and allocations of indirect overhead.

Because long-term contracts may extend over a period of time, changes in job performance, changes in job conditions and revisions of estimates of cost and earnings during the course of the work are reflected in the accounting period in which the facts that require the revision become known. At the time a loss on a contract becomes known, the entire amount of the estimated ultimate loss is recognized in the consolidated financial statements.

Contracts that are substantially complete are considered closed for consolidated financial statement purposes. Revenue earned on contracts in progress in excess of billings (under billings) is classified as a current asset. Amounts billed in excess of revenue earned (overbillings) are classified as a current liability.

Estimates

Critical estimates made by management are, among others, deferred tax asset valuation allowances, realization of inventories, collectibility of contracts receivable and the estimating of costs for long-term construction contracts. Actual results could differ from those estimates.

Classification Of Warrant Obligation

In connection with the issuance of the 12% Senior Secured Convertible Notes, the Company has an obligation to file registration statements covering the Registrable Securities underlying the warrants issued in connection with the convertible note, as defined in the Amended and 2nd Amended Registration Rights Agreements. We evaluated the warrants in accordance with SFAS 133, "Accounting for Derivative Instruments and Hedging Activities" and EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", and concluded that the warrants meet all the criteria required to be classified as equity as of March 31, 2007.

Other Significant Accounting Policies

Other significant accounting policies not involving the same level of measurement uncertainties as those discussed above, are nevertheless important to an understanding of the financial statements. The policies related to consolidation and loss contingencies require difficult judgments on complex matters that are often subject to multiple sources of authoritative guidance. Certain of these matters are among topics currently under reexamination by accounting standards setters and regulators. Although no specific conclusions reached by these standards setters appear likely to cause a material change in our accounting policies, outcomes cannot be predicted with confidence. Also see Note 1 of Notes to Consolidated Financial Statements, Summary of Significant Accounting Policies, which discusses accounting policies that must be selected by management when there are acceptable alternatives.

ITEM 3. CONTROLS AND PROCEDURES

EVALUATION OF CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including our Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) of the Exchange Act as of a date (the "Evaluation Date") within 90 days prior to filing the Company's March 31, 2007 Form 10-QSB. Based upon that evaluation, the CEO and CFO concluded that, as of March 31, 2007, our disclosure controls and procedures were not effective in timely alerting management to the material information relating to us (or our consolidated subsidiaries) required to be included in our periodic filings with the SEC.

CHANGES IN CONTROLS AND PROCEDURES

There were no significant changes made in our internal controls over financial reporting during the quarter ended March 31, 2007 that have materially affected or are reasonably likely to materially affect these controls.

LIMITATIONS ON THE EFFECTIVENESS OF INTERNAL CONTROL

The Company's management, including the CEO, does not expect that our disclosure controls and procedures or our internal control over financial reporting will necessarily prevent all fraud and material errors. An internal control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations on all internal control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, and/or by management override of the control. The design of any system of internal control is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in circumstances, and/or the degree of compliance with the policies and procedures may deteriorate. Because of the inherent limitations in a cost-effective internal control system, financial reporting misstatements due to error or fraud may occur and not be detected on a timely basis.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

During the quarter ended March 31, 2007, the Company issued 150,000 shares of common stock to Wall Street Savant, LLC, for investor marketing services, 100,000 shares of common stock to Quarum Capital Services, Inc, for financial consulting services, and 300,000 shares of common stock to Investor Relation International, for investor relation services.

The shares were issued pursuant to an exemption from the registration rights of the Securities Act of 1933, as amended, Section 4(2) of the Act.

Item 3. Defaults Upon Senior Securities

None.

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

None.

Item 5. Other Information

The Company is in process of filing a registration statement.

Item 6. Exhibits

Exhibit 31.1	Section 302 Sarbanes Oxley Certification
Exhibit 32.1	Section 906 Sarbanes Oxley Certification

**NEW CENTURY COMPANIES, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEET**

March 31, 2007

(Unaudited)

ASSETS

Current Assets

Cash	\$	317,806
Contract receivables		473,693
Inventories, net		1,333,056
Costs and estimated earnings in excess of billings on uncompleted contracts		872,335
Deferred financing costs, net		358,292
Prepaid expenses and other current assets		7,404

Total current assets		3,362,586
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Property and Equipment, net		256,529
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Deferred Financing Costs, net		328,436
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Total Assets	\$	3,947,551
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LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities

Bank Overdraft	\$	34,090
Accounts payable and accrued expenses		1,199,491
Dividends payable		362,800
Billings in excess of costs and estimated earnings on uncompleted contracts		399,710
Notes payable		12,000
Convertible notes payable, net of discount		237,223

Total current liabilities		2,245,314
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Convertible Notes Payable, net of discount		210,000
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Commitments and Contingencies

Stockholders' Equity

Cumulative, convertible, Series B preferred stock, \$1 par value,
15,000,000 shares authorized, no shares issued and

outstanding (liquidation preference of \$25 per share)	-
Cumulative, convertible, Series C preferred stock, \$1 par value, 75,000 shares authorized, 27,780 shares issued and outstanding (liquidation preference of \$933,000)	27,780
Cumulative, convertible, Series D preferred stock, \$25 par value, 75,000 shares authorized, 11,640 shares issued and outstanding (liquidation preference of \$416,000)	291,000
Common stock, \$0.10 par value, 50,000,000 shares authorized; 12,264,656 shares issued and outstanding	1,226,466
Subscriptions receivable	(462,500)
Notes receivable from stockholders	(532,402)
Deferred consulting fees	(234,092)
Additional paid-in capital	8,995,064
Accumulated deficit	(7,819,079)
Total stockholders' equity	1,492,237
Total Liabilities and Stockholders' equity	\$ 3,947,551

See accompanying notes to the consolidated financial statements.

NEW CENTURY COMPANIES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
For the Three Months Ended March 31, 2007 and 2006
(Unaudited)

	2007	2006
CONTRACT REVENUES	\$ 3,185,469	\$ 1,699,847
COST OF SALES	2,000,230	1,296,608
GROSS PROFIT	1,185,239	403,239
OPERATING EXPENSES		
Consulting and other compensation	429,363	203,058
Salaries and related	116,634	64,331
Selling, general and administrative	173,276	187,640
TOTAL OPERATING EXPENSES	719,273	455,029
OPERATING INCOME (LOSS)	465,966	(51,790)
OTHER EXPENSES		
Loss on forgiveness of debt	(11,688)	-
Derivative liability expense	-	(764,762)
Interest expense, including debt discount amortization	(465,241)	(395,828)
TOTAL OTHER EXPENSES	(476,929)	(1,160,590)
LOSS BEFORE PROVISION FOR INCOME TAXES	(10,963)	(1,212,380)
PROVISION FOR INCOME TAXES	-	-
NET LOSS	\$ (10,963)	\$ (1,212,380)
NET LOSS APPLICABLE TO COMMON STOCKHOLDERS	\$ (10,963)	\$ (924,505)
Basic and diluted net loss available to common stockholders per common share	.00	\$ (0.09)
Basic and diluted weighted average common shares outstanding	11,983,543	10,803,611

See accompanying notes to the consolidated financial statements.

F-2

NEW CENTURY COMPANIES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Three Months Ended March 31, 2007 and 2006
(Unaudited)

	2007	2006
Cash flows from operating activities:		
Net loss	\$ (10,963)	\$ (1,212,380)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization of property and equipment	28,578	39,028
Amortization of deferred financing costs	89,574	57,466
Amortization of Beneficial Conversion Features and other debt discounts	291,667	249,123
Amortization of deferred consulting fees	98,977	137,039
Estimated fair market value of common stock issued for consulting services and related change in fair value	247,500	-
Derivative liability expense	-	764,762
Changes in operating assets and liabilities:		
Contracts receivable	(170,151)	(625,005)
Inventories	(212,874)	(112,985)
Costs and estimated earnings in excess of billings on uncompleted contracts	288,333	132,622
Prepaid expenses and other current assets	12,801	(2,083)
Notes receivable from stockholders	(7,000)	-
Accounts payable and accrued expenses	8,031	(277,456)
Billings in excess of costs and estimated earnings on uncompleted contracts	(53,201)	61,823
Net cash provided (used in) operating activities	611,272	(788,046)
Cash flows from investing activities:		
Purchases of property and equipment	-	(20,000)
Net cash used in investing activities	-	(20,000)
Cash flows from financing activities:		
Restricted cash	123,898	(1,500,000)
Bank overdraft	15,318	(27,649)
Proceeds of issuance of convertible notes payable	-	3,800,000
Principal payments on notes payable	(486,000)	(774,000)
Deferred financing costs	-	(422,500)
Net cash (used in) provided by financing activities	(346,784)	1,075,851

Net increase in cash	264,488	267,805
Cash at beginning of period	53,318	-
Cash at end of period	\$ 317,806	\$ 267,805
Supplemental disclosure of non-cash activities:		
Common stock and warrants issued for deferred financing costs	\$ -	\$ 641,790
Conversion of notes payable and interest to common stock	\$ -	\$ 157,500
BCF and other debt discount on convertible notes payable	\$ -	\$ 3,800,000
Debt discount on notes payable for note extension	\$ -	\$ 18,900
Waived cumulative dividends on preferred stock	\$ -	\$ (287,875)

See accompanying notes to the consolidated financial statements.

**NEW CENTURY COMPANIES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization And Nature Of Operations

New Century Companies, Inc. and Subsidiary (collectively, the "Company"), a California corporation, was incorporated March 1996 and is located in Southern California. The Company provides after-market services, including rebuilding, retrofitting and remanufacturing of metal cutting machinery. Once completed, a remanufactured machine is "like new" with state-of-the-art computers, and the cost to the Company's customers is substantially less than the price of a new machine.

The Company currently sells its services by direct sales and through a network of machinery dealers across the United States. Its customers are generally medium to large sized manufacturing companies in various industries where metal cutting is an integral part of their businesses. The Company grants credit to its customers who are predominately located in the western United States.

The Company trades on the OTC Bulletin Board under the symbol "NCNC.OB".

Principles Of Consolidation

The consolidated financial statements include the accounts of New Century Companies, Inc. and its wholly owned subsidiary, New Century Remanufacturing (collectively, the "Company"). All significant intercompany accounts and transactions have been eliminated in consolidation.

Basis Of Presentation

The accompanying unaudited interim consolidated financial statements have been prepared by the Company, pursuant to the rules and regulations of the United States Securities and Exchange Commission (the "SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been omitted pursuant to such SEC rules and regulations; nevertheless, the Company believes that the disclosures are adequate to make the information presented not misleading. These financial statements and the notes hereto should be read in conjunction with the financial statements, accounting policies and notes thereto included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2006, filed with the SEC. In the opinion of management, all adjustments necessary to present fairly, in accordance with GAAP, the Company's financial position as of March 31, 2007, and the results of operations and cash flows for the interim periods presented, have been made. Such adjustments consist only of normal recurring adjustments. The results of operations for the three months ended March 31, 2007 are not necessarily indicative of the results for the full year ending December 31, 2007.

Going Concern

The accompanying consolidated financial statements have been prepared assuming the Company will continue as a going concern, which contemplates, among other things, the realization of assets and satisfaction of liabilities in the normal course of business. The Company has an accumulated deficit of approximately \$7,800,000. This factor, among others, raises substantial doubt about the Company's ability to continue as a going concern. The Company intends to fund operations through anticipated increased sales along with debt and equity financing arrangements which management believes may be insufficient to fund its capital expenditures, working capital and other cash requirements for the year ending December 31, 2007. Therefore, the Company will be required to seek additional funds to finance its long-term operations. The successful outcome of future activities cannot be determined at this time and there is no assurance that if achieved, the Company will have sufficient funds to execute its intended business plan or generate positive operating results.

In response to these problems, management has taken the following actions:

- The Company continues its aggressive program for selling inventory.
- The Company continues to implement plans to further reduce operating costs.
- The Company is seeking investment capital through the public and private markets.

The consolidated financial statements do not include any adjustments related to recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

Inventory

Inventories are stated at the lower of cost or net realizable value. Cost is determined under the first-in, first-out method. Inventories represent cost of work in process on units not yet under contract. Cost includes all direct material and labor, machinery, subcontractors and allocations of indirect overhead. As of March 31, 2007, the Company's inventory was determined to be approximately \$1,333,000 net, based on approximately \$197,000 cost of labor, \$825,000 cost of materials, \$121,000 cost of subcontracted services, \$476,000 overhead cost, offset by \$286,000 reserve for estimated markdowns cost of inventory.

Revenue Recognition

The Company's revenues consist of contracts with vendors. The Company uses the percentage-of-completion method of accounting to account for long-term contracts and, therefore, takes into account the cost, estimated earnings and revenue to date on fixed-fee contracts not yet completed. The percentage-of-completion method is used because management considers total cost to be the best available measure of progress on the contracts. Because of inherent uncertainties in estimating costs, it is at least reasonably possible that the estimates used will change within the near term.

Staff Accounting Bulletin ("SAB") No. 104, "Revenue Recognition" outlines the basic criteria that must be met to recognize revenue and provides guidance for presentation of revenue and for disclosure related to revenue recognition policies in financial statements filed with the SEC. Management believes that the Company's revenue recognition policy conforms to SAB No. 104. The Company recognizes revenue on contracts pursuant to SOP 81-1.

The amount of revenue recognized at the statement date is the portion of the total contract price that the cost expended to date bears to the anticipated final cost, based on current estimates of cost to complete. It is not related to the progress billings to customers. Contract costs include all materials, direct labor, machinery, subcontract costs and allocations of indirect overhead.

Because contracts may extend over a period of time, changes in job performance, changes in job conditions and revisions of estimates of cost and earnings during the course of the work are reflected in the accounting period in which the facts that require the revision become known. At the time a loss on a contract becomes known, the entire amount of the estimated ultimate loss is recognized in the consolidated financial statements.

Contracts that are substantially complete are considered closed for consolidated financial statements purposes. Costs incurred and revenue earned on contracts in progress in excess of billings (under billings) are classified as a current asset. Amounts billed in excess of costs and revenue earned (over billings) are classified as a current liability.

The Company accounts for shipping and handling fees and costs in accordance with Emerging Issues Task Force ("EITF") Issue No. 00-10 "Accounting for Shipping and Handling Fees and Costs." Shipping and handling fees and costs incurred by the Company are immaterial to the operations of the Company and are included in cost of sales.

In accordance with Statements of Financial Accounting Standards ("SFAS") No. 48, "Revenue Recognition when Right of Return Exists," revenue is recorded net of an estimate for markdowns, price concessions and warranty costs. Such reserve is based on management's evaluation of historical experience, current industry trends and estimated costs. As of March 31, 2007, the Company estimated the markdowns, price concessions and warranty costs and concluded that are immaterial and did not record any adjustment to revenues.

Basic And Diluted Loss Per Common Share

Under SFAS 128, "Earnings Per Share," basic earnings per common share is computed by dividing income (loss) available to common stockholders by the weighted-average number of common shares assumed to be outstanding during the period of computation. Diluted earnings per share is computed similar to basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive.. Common stock equivalents, representing convertible Preferred Stock, convertible debt, options and warrants totaling

approximately 8,240,816 shares at March 31, 2007 are not included in the diluted loss per share as they would be anti-dilutive. Accordingly, diluted and basic loss per share are the same for March 31, 2007. There were 2,025,451 potentially dilutive and 13,392,330 potential common shares that were excluded from the diluted earnings per share calculation.

Stock Based Compensation

Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123-R, "Share-Based Payment," ("SFAS No. 123-R"). SFAS No. 123-R requires employee stock options and rights to purchase shares under stock participation plans to be accounted for under the fair value method and requires the use of an option pricing model for estimating fair value. Accordingly, share-based compensation is measured at the grant date, based on the fair value of the award. The exercise price of options is generally equal to the market price of the Company's common stock (defined as the closing price as quoted on the Over-the-Counter Bulletin Board administered by Nasdaq) on the date of grant. \$86,400 and \$0 of share-based compensation expense was recognized in the accompanying consolidated financial statements for the three month periods ended March 31, 2007 and 2006, respectively.

From time to time, the Company's Board of Directors grants common share purchase options or warrants to selected directors, officers, employees, consultants and advisors in payment of goods or services provided by such persons on a stand-alone basis outside of any of the Company's formal stock plans. The terms of these grants are individually negotiated and generally expire within five years from the grant date.

Under the terms of the Company's 2000 Stock Option Plan, options to purchase an aggregate of 5,000,000 shares of common stock may be issued to officers, key employees and consultants of the Company. The exercise price of any option generally may not be less than the fair market value of the shares on the date of grant. The term of each option generally may not be more than five years.

Under the terms of the Company's non-statutory stock option plan, options to purchase an aggregate of 1,350,000 shares of common stock may be issued to non-employees for services rendered. These options are non-assignable and non-transferable, are exercisable over a five-year period from the date of grant, and vest on the date of grant.

On November 13, 2006, the Company granted 2,000,000 options to key employees. At March 31, 2007, the Company had 1,750,000 options available for future issuance under their equity compensation plans.

In accordance with SFAS No. 123-R, the Company's policy is to adjust share-based compensation on a quarterly basis for changes to the estimate of expected award forfeitures based on actual forfeiture experience. The effect of adjusting the forfeiture rate for all expense amortization after March 31, 2007 is recognized in the period the forfeiture estimate is changed.

At March 31, 2007, the Company estimated (using the Black Scholes pricing model) the fair value of options granted and no variance has been found. Therefore, the effect of forfeiture adjustments at the period ended March 31, 2007 was not applicable.

Options outstanding that have vested and are expected to vest as of March 31, 2007 are as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term in Years	Aggregate Intrinsic Value (1)
Vested	1,250,000	\$ 0.32	1.35	\$ --
Expected to vest	2,000,000	\$ 0.20	4.62	\$ --
Total	3,250,000			\$ --

(1) These amounts represent the difference between the exercise price and \$0.32, the closing market price of the Company's common stock on March 31, 2007 as quoted on the Over-the-Counter Bulletin Board under the symbol "NCNC.OB" for all in-the-money options outstanding.

The Company's policy for options outstanding that are expected to vest are net of estimated future forfeitures in accordance with the provisions of SFAS No. 123-R, which are estimated when compensation costs are recognized. Additional information with respect to stock option activity is as follows:

	Shares Available for Grant	Number of Shares	Outstanding Options Weighted Average Exercise	Intrinsic Value (1)
December 31, 2006	1,750,000	3,250,000	\$ 0.25	\$ 130,000
Grants	--	--	--	--
Exercises	--	--	--	--
Cancellations	--	--	--	--
March 31, 2007	1,750,000	3,250,000	\$ 0.25	\$ --
Options exercisable at:				
March 31, 2007		1,250,000	\$ 0.32	

(1) Represents the added value as difference between the exercise price and the closing market price of the Company's common stock at the end of the reporting period (as of December 31, 2006 and March 31, 2007 the market price of the Company's common stock was \$0.21 and \$0.32, respectively).

The Company follows SFAS No. 123 (R) (as interpreted by EITF Issue No. 96-18, "Accounting for Equity Instruments That Are Issued To Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services") to account for transactions involving services provided by third parties where the Company issues equity instruments as part of the total consideration. Pursuant to paragraph 7 of SFAS No. 123 (R), the Company accounts for such transactions using the fair value of the consideration received (i.e. the value of the goods or services) or the fair value of the equity instruments issued, whichever is more reliably measurable. The Company applies EITF Issue No. 96-18 to transactions when the value of the goods and/or services are not readily determinable and (1) the fair value of the equity instruments is more reliably measurable and (2) the counterparty receives equity instruments in full or partial settlement of the transactions, using the following methodology:

- a) For transactions where goods have already been delivered or services rendered, the equity instruments are issued on or about the date the performance is complete (and valued on the date of issuance).
- b) For transactions where the instruments are issued on a fully vested, non-forfeitable basis, the equity instruments are valued on or about the date of the contract.
- c) For any transactions not meeting the criteria in (a) or (b) above, the Company re-measures the consideration at each reporting date based on its then current stock value.

From time to time, the Company issues warrants to employees and to third parties pursuant to various agreements, which are not approved by the shareholders. During the three month periods ended March 31, 2007, the Company did not grant any options or warrants.

The following is a status of the warrants outstanding at March 31, 2007 and the changes during the three months ended March 31, 2007:

	Warrants	Weighted Average Price
Outstanding, December 31, 2006	6,403,728	\$ 0.57
Granted	--	--
Exercised	--	--
Cancelled/Terminated	(25,000)	(0.65)
Total Outstanding, March 31, 2007	6,378,728	\$ 0.57
Exercisable, March 31, 2007	6,378,728	0.57

F-9

Deferred Financing Costs

Direct costs of securing debt financing are capitalized and amortized over the term of the related debt. When a loan is paid in full, any unamortized financing costs are removed from the related accounts and charged to operations. During the three months ended March 31, 2007 and 2006, the Company amortized approximately \$292,000 and \$97,000, respectively, to interest expense.

Beneficial Conversion Feature Of Convertible Notes Payable

The convertible feature of certain notes payable provides for a rate of conversion that is below market value. Such feature is normally characterized as a "Beneficial Conversion Feature" ("BCF"). Pursuant to EITF Issue No. 98-5, "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratio" and EITF No. 00-27, "Application of EITF Issue No. 98-5 To Certain Convertible Instruments," the estimated fair value of the BCF is recorded in the consolidated financial statements as a discount from the face amount of the notes. Such discounts are amortized to interest expense over the term of the notes.

Classification Of Warrant Obligation

In connection with the issuance of the 12% Senior Secured Convertible Notes, the Company has an obligation to file registration statements covering the Registrable Securities underlying the warrants issued in connection with the convertible note, as defined in the Amended Registration Rights Agreement.

The obligation to file the registration statement met the criteria of an embedded derivative to be bifurcated pursuant to SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended. Under this transaction, the Company was obligated to register for resale the common shares underlying the warrants, and as a result, the embedded derivative associated with this warrant obligation did not meet the scope exception of paragraph 11(a) of SFAS No. 133. Specifically, at March 31, 2006, the Company did not have any uncommitted registered shares to settle the warrant obligation and accordingly, such obligation was classified as a liability (outside of stockholders' deficit) in accordance with EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock." The classification of the warrant obligation has been evaluated at each reporting date and reported as a liability until such time all of the criteria necessary for equity classification were met. The warrant liability was recorded originally, on February 28, 2006, the issuance date, at \$2,190,000, and adjusted market-to-market every quarter to approximately \$2,955,000, \$2,155,000, \$1,321,000 and \$695,000 at the quarter ended March 31, 2006, June 30, 2006, September 30, 2006, and December 19, 2006, correspondingly. The market-to-market adjustment was reversed to derivative liability expense.

On December 19, 2006, the Company entered into an amended agreement with the warrant holder, CAMOFI Master LDC, where by the warrant holder agreed to waive all liquidated damages incurred as a result of the Company's inability to file a registration statement to register the shares underlying the warrants. In addition, a limit was placed on the amount of liquidated damages to be incurred in the event the Company fails to have an effective registration statement within the time period required by the amended agreement. The liquidated damages would be limited to 10% of the outstanding balance of the note. As a result, the warrants met all the criteria outlined in EITF 00-19 to be classified as equity. Accordingly, the warrants were reclassified to equity at December 19, 2006, and the \$695,000 fair value of warrant liability was credited to additional paid in capital.

Management evaluated the warrants in accordance with SFAS 133, "Accounting for Derivative Instruments and Hedging Activities" and EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock", and concluded that the warrants meet all the criteria required to be classified as equity.

Income Taxes

We adopted the provisions of Financial Standards Accounting Board Interpretation No. 48 Accounting for Uncertainty in Income Taxes ("FIN 48") an interpretation of FASB Statement No. 109 ("SFAS 109") on January 1, 2007. The implementation of FIN 48 did not result in any adjustment to the Company's beginning tax positions. The Company continues to fully recognize its tax benefits which are offset by a valuation allowance to the extent that it is more likely than not that the deferred tax assets will not be realized. As of March 31, 2007, the Company did not have any unrecognized tax benefits. The Company files a consolidated federal income tax return in the U.S. The Company files a separate income tax return in the State of California. The Company is no longer subject to U.S. federal tax examinations for the years before 2004.

Significant Recent Accounting Pronouncements

On February 15, 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115." This standard permits an entity to measure many financial instruments and certain other items at estimated fair value. Most of the provisions of SFAS No. 159 are elective; however, the amendment to SFAS No. 115 ("Accounting for Certain Investments in Debt and Equity Securities") applies to all entities that own trading and available-for-sale securities. The fair value option created by SFAS No. 159 permits an entity to measure eligible items at fair value as of specified election dates. Among others, eligible items exclude (1) financial instruments classified (partially or in total) as permanent or temporary stockholders' equity (such as a convertible debt security with a non-contingent beneficial conversion feature) and (2) investments in subsidiaries and interests in variable interest entities that must be consolidated. A for-profit business entity will be required to report unrealized gains and losses on items for which the fair value option has been elected in its consolidated statements of operations at each subsequent reporting date.

The fair value option (a) may generally be applied instrument by instrument, (b) is irrevocable unless a new election date occurs, and (c) must be applied to the entire instrument and not to only a portion of the instrument. SFAS No. 159 is effective as of the beginning of the first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of the previous fiscal year provided that the entity (i) makes that choice in the first 120 days of that year, (ii) has not yet issued financial statements for any interim period of such year, and (iii) elects to apply the provisions of SFAS No. 157 ("Fair Value Measurements"). The adoption of SFAS No. 159 is not expected to have a significant impact on future financial statements.

2. CONTRACTS IN PROGRESS

Contracts in progress as of March 31, 2007 which include completed contracts not completely billed represent the following:

Cumulative costs to date	\$ 3,910,000
Cumulative gross profit to date	