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WIDEPOINT CORP
Form 10QSB/A
August 17, 2005

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB/A No. 2

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

Amendment No. 2 to Quarterly Report on Form 10-QSB for the quarter ended March 31, 2005

WIDEPOINT CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

000-23967

52-2040275

(State or other jurisdiction of
incorporation or organization)

(Commission File Number)

(IRS Employer Identification No.)

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

60181

(Address of principal executive offices)

(Zip Code)

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

The undersigned registrant hereby amends the following items, financial statements, exhibits or other portions of its Quarterly Report on Form 10-QSB for the quarter ended March 31, 2005, as previously amended by Amendment No. 1 filed on June 17, 2005, as set forth in the pages attached hereto:

- | | | |
|---------|--------|---|
| Part I | Item 1 | Condensed Consolidated Financial Statements |
| | Item 2 | Management's Discussion and Analysis or Plan of Operation |
| | Item 3 | Controls and Procedures |
| Part II | Item 6 | Exhibits |

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

WidePoint Corporation

Date: August 17, 2005

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

WIDEPOINT CORPORATION

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PART 1. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

**WIDEPOINT CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS**

	March 31,	Restated December 31,
	2005	2004
	(unaudited)	(unaudited)
<i>Assets</i>		
<i>Current assets:</i>		
Cash and cash equivalents	\$ 255,506	\$ 463,525
Accounts receivable	2,279,506	3,007,590
Prepaid expenses and other assets	157,528	203,126
	<hr/>	<hr/>
Total current assets	2,692,540	3,674,241
	<hr/>	<hr/>
Property and equipment, net	75,013	80,652
Goodwill	2,806,440	2,806,440
Intangibles	3,260,935	3,190,927
Other assets	212,400	161,148
	<hr/>	<hr/>
Total assets	\$ 9,047,328	\$ 9,913,408
	<hr/>	<hr/>
<i>Liabilities and stockholders' equity</i>		
<i>Current liabilities:</i>		
Accounts payable	\$ 995,822	\$ 1,342,759
Accrued expenses	780,169	859,345
Income taxes payable	190,709	79,177
Short-term portion of deferred rent	3,038	2,720

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	<u>March 31,</u>	<u>Restated December 31,</u>
Short-term borrowings	1,383,493	1,592,408
Financial instruments	5,652,308	6,648,571
	<hr/>	<hr/>
Total current liabilities	9,005,539	10,524,980
	<hr/>	<hr/>
Long-term portion of deferred rent	6,138	7,058
Deferred income tax liability	110,979	221,959
	<hr/>	<hr/>
Total liabilities	9,122,656	10,753,997
Stockholders' (deficit) equity:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized; 2,045,714 shares issued and outstanding, respectively	2,046	2,046
Common stock, \$0.001 par value; 110,000,000 shares authorized; 21,125,393 shares issued and outstanding, respectively	21,125	21,125
Stock warrants	14,291	14,291
Related party notes receivable	(61,100)	(81,100)
Additional paid-in capital	43,484,997	43,515,382
Accumulated deficit	(43,536,687)	(44,312,333)
	<hr/>	<hr/>
Total stockholders'(deficit) equity	(75,328)	(840,589)
	<hr/>	<hr/>
Total liabilities and stockholders' (deficit) equity	\$ 9,047,328	\$ 9,913,408
	<hr/>	<hr/>

The accompanying notes are an integral part of these consolidated statements.

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WIDEPOINT CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended March 31,	
	Restated 2005	2004
	(unaudited)	
Revenues, net	\$ 2,669,532	\$ 723,083
Cost of sales	1,847,163	565,766
	<hr/>	<hr/>
Gross profit	822,369	157,317
Sales and marketing	176,370	101,881
General & administrative	727,808	150,063
Depreciation & amortization	88,945	1,789
	<hr/>	<hr/>
Loss from operations	(170,754)	(96,416)
Other income, net:		
Interest income	770	1,862

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	Three Months Ended March 31,	
	<hr/>	
Interest expense	(52,783)	(115)
Gain from financial instrument	996,263	--
Other	2,150	--
	<hr/>	
Net income/(loss)	\$ 775,646	\$ (94,669)
	<hr/>	
Basic net income/(loss) per share	\$ 0.04	\$ (0.01)
	<hr/>	
Basic weighted average shares outstanding	21,125,393	15,579,913
	<hr/>	
Diluted net income/(loss) per share	\$ 0.01	\$ (0.01)
	<hr/>	
Diluted weighted average shares outstanding	51,983,931	15,579,913
	<hr/>	

The accompanying notes are an integral part of these consolidated statements.

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WIDEPOINT CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended March 31,	
	<hr/>	
	Restated 2005	2004
	<hr/>	
	(unaudited)	
	<hr/>	
Cash flows from operating activities:		
Net income/(loss)	\$ 775,646	\$ (94,669)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation Expense	6,900	1,789
Amortization expense	97,326	--
Deferred income taxes	(110,980)	--
Deferred financing costs	3,573	--
(Gain) from financial instruments	(996,263)	--

	Three Months Ended March 31,	
	<hr/>	
Changes in assets and liabilities		
Accounts receivable	728,084	91,543
Prepaid expenses and other assets	45,597	15,234
Other assets	(54,825)	3,748
Accounts payable and accrued expenses	(325,433)	(7,256)
	<hr/>	
Net cash provided by operating activities	\$ 169,625	\$ 10,389
	<hr/>	
Net cash flows from investing activities:		
Purchase of property and equipment	(1,261)	--
Intangible development costs	(167,333)	--
	<hr/>	
Net cash flows used in investing activities	\$ (168,594)	\$ --
	<hr/>	
Net cash used in financing activities		
Borrowings on notes payable	158,866	--
Payments on notes payable	(367,781)	--
Collections on related party notes	20,000	--
APIC expenses	(30,385)	--
Proceeds from exercise of stock options	10,250	--
	<hr/>	
Net cash used in financing activities	\$ (209,050)	\$ --
	<hr/>	
Net (decrease) increase in cash	\$ (208,019)	\$ 10,389
	<hr/>	
Cash and equivalents, beginning of period	\$ 463,525	\$ 949,612
	<hr/>	
Cash and equivalents, end of period	\$ 255,506	\$ 960,001
	<hr/>	
Cash paid for interest	\$ 26,723	\$ --
	<hr/>	

The accompanying notes are an integral part of these consolidated statements.

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

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

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WidePoint Corporation (WidePoint or the Company) is an information technology (IT) services firm with established competencies in federal government and commercial sector IT consulting services, including planning, managing and implementing IT solutions, software and secure authentication processes, and specialized outsourcing arrangements. Our staff consists of business and computer specialists who help customers augment and expand their resident technologic skills and competencies, drive technical innovation, and help develop and maintain a competitive edge in today s rapidly changing technological environment in business.

In 2004, WidePoint acquired Chesapeake Government Technologies, Inc. (Chesapeake) and Operational Research Consultants, Inc. (ORC) as part of WidePoint s strategy to refocus our business development initiatives toward the substantial increase in government spending on infrastructure and automation that has been accelerated by recent geopolitical events that have created an unprecedented need for systems and process expertise across most government markets, federal, state and local. WidePoint intends to capitalize on the expected growth in its target markets through strategic acquisitions, continue rollout of ORC s Public Key Infrastructure (PKI) initiative, and continue to implement our project based enterprise strategy emphasizing industry-wide best practices disciplines. The Company intends to continue to leverage the synergies between its newly acquired operating subsidiaries and cross sell its technical capabilities into each separate marketplace serviced by its respective subsidiaries.

The Company has physical locations in Oakbrook Terrace, Illinois, Fairfax, Virginia, Alexandria, Virginia, and Chesapeake, Virginia. The Company employees work at various client locations throughout the upper Midwest, Texas, and Mid Atlantic areas of the United States.

In addition, most of the Company s current costs consist primarily of the salaries and benefits paid to the Company s technical, marketing and administrative personnel and as a result of its plan to expand its operations through a combination of internal growth initiatives and merger and acquisition opportunities, the Company expects such costs to increase. The Company s profitability also depends upon both the volume of services performed and the Company s ability to manage costs. As a significant portion of the Company s costs is labor related, the Company must effectively manage these costs to achieve and grow its profitability. To date, the Company has attempted to maximize its operating margins through efficiencies achieved by the use of the Company s proprietary methodologies, and by offsetting increases in consultant salaries with increases in consultant fees received from its clients. The uncertainties relating to its ability to achieve and maintain profitability, obtain additional funding to fund its growth strategy and provide the necessary investment to continue to upgrade its management reporting systems to meet the continuing demands of the present regulatory changes affect the comparability of the information reflected in the selected consolidated financial information presented above. The Company believes that its cash on hand, and available senior lending facility are adequate to finance operations through 2005.

Restatement.

At December 31, 2004, the financial instrument, loss on financial instrument, and retained deficit were adjusted from previously reported amounts to properly reflect the recording of the financial instrument at fair value at December 31, 2004. The impact of this accounting error was to understate the recorded value of the financial instrument and net loss by \$2,865,621 at December 31, 2004. The effect of this restatement of the \$2,865,621 at December 31, 2004 on the Company s financial statements resulted in a change from a loss on financial instrument to a gain on financial instrument for the three month period ending March 31, 2005. The loss on financial instrument for the three month period ending March 31, 2005 was previously reported as \$1,869,356. The restated results for the three month period ending March 31, 2005 resulted in a gain on financial instrument of \$996,263. As a result of the restatement at December 31, 2004, the net loss for the three month period ending March 31, 2005 changed from a net loss of \$2,089,974 to a net income of \$775,645. For the quarter ended March 31, 2005 the restatement decreased the basic net loss per share by \$0.14 from a basic net loss per share of \$0.10, as previously stated, to a restated basic net income per share of \$0.04. For the quarter ended March 31, 2005 the restatement decreased the diluted net loss per share by \$0.11, as previously stated, to a restated diluted net income per share of \$0.01.

2. Significant Accounting Policies

Principles of Consolidation

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

Use of Estimates

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

Cash and Cash Equivalents

Investments purchased with original maturities of three months or less are considered cash equivalents for purposes of these consolidated financial statements. The Company maintains cash and cash equivalents with various major financial institutions. At times, cash balances held at financial institutions were in excess of federally insured limits. The Company places its temporary cash investments with high-credit, quality financial institutions, and as a result, the Company believes that no significant concentration of credit risk exists with respect to these cash investments.

Accounts Receivable

The majority of the Company's accounts receivable are due from either United States federal agencies or established companies in the following industries: manufacturing, consumer product goods, direct marketing, healthcare and financial services. Credit is extended based on evaluation of a customer's financial condition and, generally, collateral is not required. Accounts receivable are due within 30 to 60 days and are stated at amounts due from customers net of an allowance for doubtful accounts. Accounts outstanding longer than the contractual payment terms are considered past due.

The Company determines its allowance for doubtful accounts by considering a number of factors, including the length of time trade accounts receivable are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes-off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts.

Description	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions	Balance at End of Period
For the quarter ended March 31, 2004, Allowance for doubtful accounts	\$ 18,819	\$ 14	\$ 14	\$ 18,819
For the quarter ended March 31, 2005, Allowance for doubtful accounts	\$ --	\$ --	\$ --	\$ --

Unbilled accounts receivable on time-and-materials contracts represent costs incurred and gross profit recognized near the period-end but not billed until the following period. Unbilled accounts receivable on fixed-price contracts consist of amounts incurred that are not yet billable under contract terms. At March 31, 2005 and December 31, 2004, unbilled accounts receivable totaled \$12,869 and \$0, respectively.

Revenue Recognition

The majority of the Company's revenues are derived from cost-plus, or time-and-materials contracts. Under cost-plus contracts, revenues are recognized as costs are incurred and include an estimate of applicable fees earned. For time-and-material contracts, revenues are computed by multiplying the number of direct labor-hours expended in the performance of the contract by the contract billing rates and adding other billable direct costs. In the event of a termination of a contract, all billed and unbilled amounts associated with those task orders where work has been performed would be billed and collected. The termination provisions of the contract would be accounted for at the time of termination. Any deferred and/or amortization cost would either be billed or expensed depending upon the termination provisions of the contract. Further, the Company has had no history of losses nor has it identified any specific risk of loss at March 31, 2005 or on December 31, 2004 due to termination provisions and thus has not recorded provisions for such events.

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The Company's other revenues are derived from the delivery of non-customized software. In such cases revenue is recognized when there is persuasive evidence that an arrangement exists (generally a purchase order has been received or contract signed), delivery has occurred, the charge for the software is fixed or determinable, and collectibility is probable.

Significant Customers

For the quarter ended March 31, 2005, two customers, Tangible Software and The Department of Homeland Security, individually represented approximately 15% and 14% of revenues, respectively, and we therefore are materially dependent upon such customers. Due to the nature of our business and the relative size of certain contracts which are entered into in the ordinary course of business, the loss of any single significant customer, including the above customers, would have a material adverse effect on results. For the quarter ended March 31, 2004, four customers, Abbot Laboratories, Spencer Stuart, Manpower, and Baxter Healthcare, individually represented 18%, 14%, 13%, and 13% of revenue, respectively.

Fair value of financial instruments

The Company's financial instruments include cash equivalents, accounts receivable, accounts payable, short-term debt and other financial instruments associated with the issuance of the common stock warrants attributable to the preferred stock capital investment in the Company in October of 2004. The carrying values of cash equivalents, accounts receivable and accounts payable approximate their fair value because of the short maturity of these instruments. The carrying amounts of the Company's bank borrowings under its credit facility approximate fair value because the interest rates are reset periodically to reflect current market rates.

The Company's financial instruments also include a financial instrument in which a valuation for the warrants issued by the Company under the Barron Partners, LP preferred financing agreement contained a registration rights agreement which contained a liquidating damages provision. Accordingly, a Black Scholes calculation was used to determine the fair value of those warrants which are classified as a financial instrument. The Financial Instrument was marked to market at March 31, 2005.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to credit risk consist of cash and cash equivalents and accounts receivable. As of March 31, 2005, two customers, Tangible Software and The Department of Homeland Security accounted for approximately 25% and 18%, respectively of accounts receivable. As of December 31, 2004, two customers, The Department of Homeland Security and Tangible Software, individually represented 24% and 13% of accounts receivable, respectively.

Income Taxes

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

Property and Equipment

Property and equipment are stated at cost, net of accumulated depreciation and amortization. Property and equipment consisted of the following:

	<u>March 31,</u>	<u>December 31,</u>
	<u>2005</u>	<u>2004</u>
Computers, equipment and software	\$ 91,290	\$ 90,029
Less- Accumulated depreciation and amortization	(16,277)	(9,377)
	<u>\$ 75,013</u>	<u>\$ 80,652</u>

Depreciation expense is computed using the straight-line method over the estimated useful lives of three years.

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In accordance with the American Institute of Certified Public Accountants Statement of Position 98-1 Accounting for the Costs of Computer Software Developed or Obtained for Internal Use, the Company capitalizes costs related to software and implementation in connection with its internal use software systems.

Software Development Costs

WidePoint accounts for software development costs related to software products for sale, lease or otherwise marketed in accordance with Statement of Financial Accounting Standards (SFAS) No. 86, Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed. For projects fully funded by the Company, significant development costs are capitalized from the point of demonstrated technological feasibility until the point in time that the product is available for general release to customers. Once the product is available for general release, capitalized costs are amortized based on units sold, or on a straight-line basis over a six-year period or other such shorter period as may be required. WidePoint recorded approximately \$14,000 of amortization expense for the period ending March 31, 2005. WidePoint recorded approximately \$9,700 of amortization expense for the year ended December 31, 2004. Capitalized software costs included in Other Intangibles at March 31, 2005 and December 31, 2004 were approximately \$0.7 and \$0.6 million, respectively.

Goodwill, Other Intangible Assets, and Long-Lived Assets

Goodwill represents costs in excess of fair values assigned to the underlying net assets acquired. The Company has adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets*. These standards require the use of the purchase method of accounting for business combinations, set forth the accounting for the initial recognition of acquired intangible assets and goodwill and describe the accounting for intangible assets and goodwill subsequent to initial recognition. Under the provisions of these standards, goodwill is not subject to amortization and annual review is required for impairment. The impairment test under SFAS No. 142 is based on a two-step process involving (i) comparing the estimated fair value of the related reporting unit to its net book value and (ii) comparing the estimated implied fair value of goodwill to its carrying value. Impairment losses are recognized whenever the implied fair value of goodwill is less than its carrying value. The Company's annual impairment testing date is December 31.

The Company recognizes an acquired intangible apart from goodwill whenever the intangible arises from contractual or other legal rights, or when it can be separated or divided from the acquired entity and sold, transferred, licensed, rented or exchanged, either individually or in combination with a related contract, asset or liability. Such intangibles are amortized over their useful lives. Impairment losses are recognized if the carrying amount of an intangible subject to amortization is not recoverable from expected future cash flows and its carrying amount exceeds its fair value.

The Company reviews its long-lived assets, including property and equipment, identifiable intangibles, and goodwill annually or whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine recoverability of its long-lived assets, the Company evaluates the probability that future undiscounted net cash flows will be less than the carrying amount of the assets.

Basic and Diluted Net Loss Per Share

Basic income or loss per share includes no dilution and is computed by dividing net income or loss by the weighted-average number of common shares outstanding for the period. Diluted income or loss per share includes the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. The treasury stock effect of the conversion of preferred stock to common stock, options, and warrants to purchase 30,858,538 shares of common stock outstanding at March 31, 2005 has been included in the calculation of the fully diluted net income per share as such effect would have been dilutive. The treasury stock effect of the options and warrants to purchase 2,112,000 shares of common stock outstanding at March 31, 2004 has not been included in the calculation of the net loss per share as such effect would have been anti-dilutive.

Stock-based compensation

The Company accounts for stock-based employee compensation arrangements using the intrinsic value method in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and complies with the disclosure provisions of SFAS No. 123 Accounting for Stock-Based Compensation. Under APB Opinion No. 25, compensation cost is generally recognized based on the difference, if any, on the date of grant between the fair value of the Company's common stock and the amount an employee must pay to acquire the stock. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement 123, *Accounting for Stock-Based Compensation*, using the assumptions described in Note 8, to its stock-based employee plans.

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	Three Months ended March 31,	
	Restated	
	2005	2004
Net income/(loss), as reported	\$ 775,645	\$ (94,669)
Add: Total stock-based employee compensation expense determined under fair value based method for awards granted, modified, or settled, net of related tax effects	(250,813)	(87,712)
	<hr/>	<hr/>
Pro forma net income/(loss)	\$ 524,832	\$ (182,381)
Net income/(loss) per share:		
Basic - as reported	\$ 0.04	\$ (0.01)
Diluted - as reported	\$ 0.01	\$ (0.01)
Basic - pro forma	\$ 0.02	\$ (0.01)
Diluted - pro forma	\$ 0.01	\$ (0.01)

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

For purposes of determining the effect of these options, the fair value of each option is estimated on the date of grant based on the Black-Scholes single-option pricing model assuming the following for the three months ended March 31, 2005:

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Dividend yield	--
Risk-free interest rate (%)	2.70-4.13%
Volatility factor (%)	156%
Expected life in years	5

3. Debt

	March 31, 2005	December 31, 2004
<i>Borrowings under WidePoint's Senior Debt Agreement:</i>	\$ 1,383,493	\$ 1,592,408

On October 25, 2004, the Company executed a senior lending agreement with RBC-Centura. The Agreement initially provides for a \$2.5 million revolving credit facility. The maturity date of the credit facility is October 25, 2005.

The maximum available borrowing under revolving credit facility at March 31, 2005 and December 31, 2004 was \$1.8 million and \$2.2 million, respectively. Borrowings under the Agreement are collateralized by the Company's eligible contract receivables, inventory, all of its stock in certain of our subsidiaries and certain property and equipment, and bear interest at the Prime Rate which was 5.75% and 5% on March 31, 2005 and December 31, 2004, respectively.

WidePoint's credit facility requires that the Company maintain specified financial covenants relating to fixed charge coverage, interest coverage, and debt coverage, and maintain a certain level of consolidated net worth. The weighted average borrowings under the revolving portion of the facility and the prior agreement for the quarter ended March 31, 2005 and during the year ended December 31, 2004, were \$1.5 and \$1.5 million, respectively. In conjunction with the execution of the credit facility, the Company recorded \$0.1 million in loan origination costs, included in other assets, which have been amortized ratably over the term of the credit facility which commenced in October of 2004 and will expire in October of 2005.

The total interest and finders' fees paid was approximately \$34,000 for the year ended December 31, 2004. The total interest fees paid for the quarter ended March 31, 2005 was approximately \$20,000.

4. Goodwill and Intangible Assets

Effective January 1, 2002, WidePoint adopted SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS 142 requires, among other things, the discontinuance of goodwill amortization. Under SFAS 142, goodwill is to be reviewed at least annually for impairment. The Company has elected to perform this review on December 31st of each calendar year. These reviews have resulted in no adjustments in goodwill.

During 2004, WidePoint completed the acquisitions of Chesapeake Government Technologies, Inc. and Operational Research Consultants, Inc. As a result of these acquisitions the Company has acquired goodwill and intangibles. The following details the components of goodwill and intangibles:

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	As of March 31, 2005	
	Gross Carrying Amount	Accumulated Amortization
	<u> </u>	<u> </u>
Amortized intangible assets		
(1) ORC Intangible (Includes customer relationships and PKI business opportunity purchase accounting preliminary valuations)	\$ 1,145,523	\$ (92,115)
(2) Chesapeake Intangible	1,540,319	(45,845)
(3) PKI-I Intangible (Related to internally generated software)	334,672	(24,250)
	<u> </u>	<u> </u>
Total	\$ 3,020,514	\$ (162,210)
	<u> </u>	<u> </u>
Unamortized intangible assets		
(4) Other (PKI-II Intangible)	\$ 403,000	
	<u> </u>	
Total	\$ 403,000	
	<u> </u>	
<u>Aggregate Amortization Expense:</u>		
For quarter ended 3/31/05	\$ 97,326	
<u>Estimated Amortization Expense:</u>		
For year ended 12/31/05	\$ 389,305	
For year ended 12/31/06	\$ 389,305	
For year ended 12/31/07	\$ 389,305	
For year ended 12/31/08	\$ 389,305	
For year ended 12/31/09	\$ 307,803	

- (1) The ORC intangible is made up of the estimated preliminary purchase accounting associated with the valuation assigned by the Company to ORC's customer relationships and PKI business opportunity. The PKI business opportunity intangible has an estimated life of 6 years and ORC's customer relationships have an estimated life of 5 years. The PKI business opportunity was estimated based upon the contractual life assigned to the authority to issue PKI certificates by the federal government. The fair value of the PKI business

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opportunity was estimated using the expected present value of future cash flows estimated by the Company for ORC's PKI business opportunity. ORC's customer relationship intangible was estimated based upon an analysis of the historic life of ORC's present customer relationships and their present contract opportunities. A fair value was estimated using the expected present value of the estimated future cash flows generated from those relationships. The weighted average life of this intangible asset class is 5.5 years.

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- (2) The Chesapeake intangible is related to the ORC purchase. Chesapeake was materially responsible for the acquisition of ORC by WidePoint. As a result, Chesapeake's intangible value was assigned an estimated life of 14 years or the historic life of ORC. The weighted average life of this intangible class is 13.5 years.
 - (3) The PKI-I intangible is related to internally generated software that was associated with ORC's PKI-I development of its phase 1 software offerings. ORC commenced sales of its PKI-I service in August of 2004. It has a weighted average life of 5 years and is based upon the contractual life assigned to the authority to issue PKI certificates by the federal government.
 - (4) The PKI-II intangible is related to a secondary PKI software development effort by ORC which is still ongoing. Therefore, no amortization expense has been incurred.

The total weighted average life of all of the intangibles is approximately 7.5 years.

There were no amounts of research and development assets acquired during the quarter ending March 31, 2005 nor any written off in the period.

There were no changes in the carrying amount of goodwill for the quarter ended March 31, 2005.

The goodwill acquired is associated with the acquisition of ORC in October of 2004. No impairment was required as of March 31, 2005.

5. Income Taxes

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

The Company has determined that its net deferred tax asset did not satisfy the recognition criteria set forth in SFAS No. 109 and, accordingly, established a valuation allowance for 100 percent of the net deferred tax asset, less the deferred liability related to the Section 481(a) adjustment.

As of December 31, 2004 the Company had net operating loss carry forwards of approximately \$17,025,000 to offset future taxable income. These carry forwards expire between 2010 and 2024. Under the provision of the Tax Reform Act of 1986, when there has been a change in an entity's ownership of 50 percent or greater, utilization of net operating loss carry forwards may be limited. As a result of WidePoint's equity transactions, the Company's net operating losses will be subject to such limitations and may not be available to offset future income for tax purposes.

6. Stockholders Equity

The Company is authorized to issue 110,000,000 shares of common stock, \$.001 par value per share. As of March 31, 2005 and December 31, 2004, there were 21,125,393 shares of common stock outstanding. As of March 31, 2005, 5,555,556 additional common shares have been issued and placed into escrow with none of those shares yet having been earned under a purchase agreement between WidePoint and ORC. The rights, preferences and privileges of holders of common stock are subject to, and may be adversely affected by the rights of the holders of shares Series A Convertible Preferred Stock and of any additional series of preferred stock that may be designated and issued in the future.

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Preferred Stock

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Our certificate of incorporation authorizes the Company to issue up to 10,000,000 shares of preferred stock, \$0.001 par value per share, of which 2,045,714 shares are outstanding.

Pursuant to the Certificate of Designation of Preferences, Rights and Limitations of Series A Convertible Preferred Stock, filed with the Secretary of State of the State of Delaware on November 9, 2004, 2,045,714 shares of the Company's preferred stock are designated as Series A Convertible Preferred Stock having the following rights:

Each share of Series A Convertible Preferred Stock has a conversion rate equal to \$0.175 per share and is convertible into ten shares of common stock.

The conversion of the Series A Convertible Preferred Stock is subject to the following conditions:

Subject to waiver, holders of Series A Convertible Preferred Stock do not have the right to convert any portion of the preferred stock to the extent that after giving effect to such conversion, the holder (together with any affiliates of the holder), would beneficially own in excess of 4.99% of the number of shares of the common stock outstanding immediately after giving effect to such conversion. In the event the converted shares when issued and combined with all other shares of common stock beneficially owned by the holder and its affiliates equals, at any time, more than 4.99% of the total number of then outstanding shares of common stock, then for so long as such holder and its affiliates beneficially owns more than 4.99% of the total number of then outstanding shares of common stock, the holder of the converted shares and its affiliates shall have no more than 22% of the total voting power of all outstanding shares of common stock at any time.

Holders of WidePoint's Series A Convertible Preferred Stock are entitled to receive a liquidation preference equal to \$1.75 per share in the event of the liquidation, dissolution, or winding up of the Company's business.

Holders of Series A Convertible Preferred Stock are not entitled to voting rights. However, unless approved by the holders of the outstanding Series A Convertible Preferred Stock, the Company cannot: (a) alter or change adversely the powers, preferences or rights given to the Series A Convertible Preferred Stock or alter or amend the certificate of designation relating to the Series A Convertible Preferred Stock, (b) authorize or create any class of stock ranking as to dividends or distribution of assets upon a liquidation senior to or otherwise *pari passu* with the Series A Convertible Preferred Stock, (c) amend the certificate of incorporation or other charter documents in breach of the certificate of designations, or (d) increase the authorized number of shares of Series A Convertible Preferred Stock.

Dividends are not payable with respect to the Series A Convertible Preferred Stock.

Shares of Series A Convertible Preferred Stock are subject to automatic conversion generally under the following circumstances: (i) a change in control of WidePoint, (ii) the consummation of a public offering (with a value of at least \$5 million or more) of our common stock, (iii) upon receipt of the consent of all holders of the Series A Convertible Preferred Stock, or (iv) in the event that the fair market value of the outstanding shares of our common stock exceeds \$100 million.

As a result of the issuance of a registration rights agreement that contained a liquidated damages clause, the Company is required to follow EITF 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock by the Company (see footnote 7). In light of the required accounting treatment under EITF 00-19, the entire proceeds of the issuance were allocated to warrants and as such no proceeds have been allocated to the preferred stock issuance as of December 31, 2004.

Common Stock

On October 25, 2004, WidePoint completed the acquisition of Operational Research Consultants, Inc., or ORC, a privately held IT and engineering firm providing mission-critical sensitive and strategic information security solutions to the United States Government. Pursuant to the terms of a Purchase Agreement entered into on October 25, 2004, between the Company and the ORC shareholders, the Company issued 5,555,556 common shares of the Company's common stock and placed it into an escrow to be released to the ORC shareholders in the event they attain certain performance parameters in 2004 and 2005. As of March 31, 2005, no common shares were earned.

On April 30, 2004, the Company closed upon the acquisition of all the issued and outstanding shares of Chesapeake, pursuant to the terms of an Agreement and Plan of Merger, dated as of March 24, 2004. WidePoint issued 4,082,980 shares of its common stock to stockholders of Chesapeake in consideration for all of the issued and outstanding shares of Chesapeake owned by them. In conjunction with this closing, the sole stockholders also entered into an escrow agreement and deposited 3,266,384 shares of the 4,082,980 newly issued shares of WidePoint common stock into escrow. The 3,266,384 shares of common stock placed into escrow will be released to the Chesapeake Shareholders in the event of the

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satisfaction of certain conditions set forth in the merger agreement, which provides that during the period commencing after the closing of the merger and ending on December 31, 2005, the 3,266,384 shares of common stock will be released to the Chesapeake shareholders in a ratio based on the amount of revenues actually received by the Company from the business acquired from Chesapeake. The December 31, 2005 escrow expiration date may be extended for one additional year in the event it is determined that Chesapeake has achieved certain performance levels in the latter part of 2005. In the event that WidePoint does not receive certain levels of revenues from the business acquired from Chesapeake, then any of the 3,266,384 shares of common stock to which the Chesapeake shareholders have not become entitled to receive will be returned to the Company. For the period ending March 31, 2005, the Company released 544,397 shares from escrow to the Chesapeake shareholders upon the filing of the Company's Annual Report on Form 10-K for the year ended December 31, 2004 with the Securities and Exchange Commission.

Pursuant to an agreement on April 30, 2004 between the Company and Tripoint Capital Advisors, LLP, the company issued 500,000 shares of its common stock without registration under the Securities Act of 1933 for services rendered in association with the Chesapeake acquisition. These shares were reported at the fair value at the date of issuance.

Pursuant to stock purchase agreements entered into on July 8, 2002, between the Company and each of Steve L. Komar, James T. McCubbin and Mark M. Mirabile, the Company privately sold 865,000 shares of its common stock to each such person without registration under the Securities Act of 1933, pursuant to the private offering exemption under Section 4(2) thereof, in consideration of a three-year full-recourse note.

Stock Warrants

On October 27, 2004 and November 22, 2004, the Company issued warrants to purchase 30,612 and 5,556 shares of common stock, respectively to Liberty Capitol as part of a consulting agreement in which Liberty Capitol assisted the Company in arranging its senior debt financing with RBC-Centura. The warrants have a term of 5 years. The Company used a fair-value option pricing model to value these stock warrants at approximately \$14,291. This value has been reflected as part of stock warrants in the stockholders' equity section of the consolidated balance sheet and are being amortized over the life of the debt as interest expense.

Related Party Notes

Pursuant to stock purchase agreements entered into on July 8, 2002, between the Company and each of Steve L. Komar, James T. McCubbin and Mark M. Mirabile, the Company privately sold 865,000 shares of its common stock to each such person without registration under the Securities Act of 1933, pursuant to the private offering exemption under Section 4(2) thereof, in consideration of a three-year full-recourse, 5% interest bearing promissory note with equal annual principal payments due, issued by each such person to the Company in the principal amount of \$60,550.00, or \$181,650.00 in the aggregate (which equals \$0.07 per share, being the closing price of the Company's common stock on July 8, 2002). Amounts outstanding under these notes are reflected as a reduction to stockholders' equity until paid.

7. Financial Instrument

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In October of 2004, the Company issued warrants to purchase 10,228,571 shares of common stock to Barron Partners, LP as part of a preferred stock financing. The warrants have a term of 5 years. The value of these warrants has been reflected as a financial instrument in the short-term liabilities section of the consolidated balance sheet as a result of the issuance of a registration rights agreement that included a liquidated damages clause, which is linked to an effective registration of such securities. Accordingly, the Company applied EITF 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock* and accounted for the warrants as a liability. In light of the required accounting treatment under EITF 00-19, the Company is also required to value the fair market price of the financial instrument as of March 31, 2005. The Company utilized a Black-Scholes calculation to determine the fair valuation of the financial instrument on March 31, 2005. We used a volatility input of 101% and a risk free interest rate of 4.18% and a warrant exercise price of \$0.40 per common share. The fair value utilizing this calculation produced a computed result for the financial instrument of \$5,652,308. As of December 31, 2004, the value of the financial instrument was \$6,648,571. The difference between the measured fair value marked to market at December 31, 2004 and March 31, 2005 resulted in the gain from financial instrument of \$996,263.

8. Litigation

As of December 31, 2004, ORC was the defendant in a lawsuit entitled *Fleurette v. ORC*, C.A. No. 1:04-cv-1054, in the Eastern District of Virginia, in which Renee Fleurette Gallagher, a former employee of ORC, alleged that ORC wrongfully terminated her employment with ORC. The plaintiff sought an unspecified amount of damages from ORC. Prior administrative and judicial proceedings instituted by Ms. Gallagher against ORC have been dismissed or found to be without merit. ORC did not believe that it had committed any wrong against Ms. Gallagher and

therefore vigorously defended itself in the lawsuit filed by Ms. Gallagher. As part of the agreements entered into between WidePoint, ORC and the former stockholders of ORC at the time of WidePoint's acquisition of ORC, the former stockholders of ORC agreed to indemnify WidePoint and ORC from any liability involving the claims by Ms. Gallagher against ORC, including the above-captioned lawsuit. In February of 2005, a settlement was reached between the parties and the complaints were dismissed.

Other than as described above, the Company is not involved in any material legal proceedings.

9. Subsequent events

In April and May of 2005, Barron Partners LP converted 300,000 preferred shares into 3,000,000 common shares and subsequently sold the 3,000,000 common shares in private transactions to three institutional investors. Barron Partners LP also exercised warrants to purchase 2,000,000 common shares and subsequently sold the 2,000,000 common shares in private transactions to two institutional investors. As a result of the exercise of the 2,000,000 warrants, gross proceeds of \$800,000 were realized by the Company.

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

The following discussion and analysis of the financial condition and results of operations of the Company should be read in conjunction with the financial statements and the notes thereto which appear elsewhere in this quarterly report and the Company's Annual Report on Form 10-K for the year ended December 31, 2004.

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

Overview

WidePoint is an information technology (IT) services firm with established competencies in federal government and commercial sector IT consulting services, including planning, managing and implementing IT solutions, software and secure authentication processes, and specialized outsourcing arrangements. Our staff consists of business and computer specialists who help customers augment and expand their resident technologic skills and competencies, drive technical innovation, and help develop and maintain a competitive edge in today's rapidly changing technological environment in business.

In 2004, WidePoint acquired Chesapeake Government Technologies, Inc. (Chesapeake) and Operational Research Consultants, Inc. (ORC) as part of WidePoint's strategy to refocus the Company's business development initiatives toward the substantial increase in government spending on infrastructure and automation that has been accelerated by recent geopolitical events that have created an unprecedented need for systems and process expertise across most government markets, federal, state and local. This market is also growing due to the fact that many government legacy systems and processes are approaching the end of their technologically useful lives, indicating the need for significant upgrade and enhancement. WidePoint intends to capitalize on the expected growth in its target markets through its strategic acquisitions, continuing rollout of the ORC Public Key Infrastructure (PKI) initiative, and by continuing to implement our project based enterprise strategy emphasizing industry-wide best practices disciplines.

With the addition of the customer base and the increase in revenues attributable from the ORC acquisition, WidePoint's opportunity to leverage and expand further into the federal marketplace has improved dramatically. ORC's past client successes, top security clearances in their facilities and with their personnel, and additional breadth of management talent have expanded the Company's reach into markets that previously were not accessible to WidePoint. WidePoint intends to continue to leverage the synergies between the newly acquired operating subsidiaries and cross sell those technical capabilities into each separate marketplace serviced by its respective subsidiaries. Further, WidePoint is continuing to actively search out new synergistic acquisitions that we believe will further enhance the present base of business, which has been augmented by

our recent acquisitions and internal growth initiatives.

As a result of these actions WidePoint's revenues for the period ending March 31, 2005 increased by approximately 385% from approximately \$0.7 million for the period ending March 31, 2004 to \$2.7 million for the period ending March 31, 2005. This increase was materially due to the additional revenues generated by WidePoint's acquisition of ORC in October 2004. Due to our recent acquisition of ORC we presently derive a relatively larger base of revenue from contracts with U.S. government agencies and U.S. government contractors that are focused on national security. Funding for these programs and services are generally linked to trends in U.S. government spending in the areas of defense, intelligence and homeland security. Leading up to and following the terrorist events of September 11, 2001, the U.S. government substantially increased its overall defense, intelligence and homeland security budgets. Because of the increasing focus on national security, ORC's client relationships in this sector, and ORC's PKI initiative we anticipate that quarterly revenues will continue at these levels or higher levels in future quarters.

A number of factors, including the progress of contracts, revenues earned on contracts, the number of billable days in a quarter, the timing of the pass-through of other direct costs, the commencement and completion of contracts during any particular quarter, the schedule of the government agencies for awarding contracts, the term of each contract that we have been awarded and general economic conditions may subject our revenues and operating results to significant variation from quarter to quarter. Because a significant portion of our expenses, such as personnel and facilities costs, are fixed in the short term, successful contract performance and variation in the volume of activity as well as in the number of contracts commenced or completed during any quarter may cause significant variations in operating results from quarter to quarter.

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With our recent acquisition of ORC we rely upon a larger portion of our revenues from the Federal Government directly or as a subcontractor. The Federal Government's fiscal year ends September 30. If a budget for the next fiscal year has not been approved by that date, our clients may have to suspend engagements that we are working on until a budget has been approved. Such suspensions may cause us to realize lower revenues in the fourth quarter and/or first quarter of the year. Further, a change in presidential administrations and in senior government officials may negatively affect the rate at which the Federal Government purchases the services which we offer.

As a result of the factors above, period-to-period comparisons of our revenues and operating results may not be meaningful. You should not rely on these comparisons as indicators of future performance as no assurances can be given that quarterly results will not fluctuate, causing a possible material adverse effect on our operating results and financial condition.

In addition, most of WidePoint's current costs consist primarily of the salaries and benefits paid to WidePoint's technical, marketing and administrative personnel. As a result of our plan to expand WidePoint's operations through a combination of internal growth initiatives and merger and acquisition opportunities, WidePoint expects such costs to increase. WidePoint's profitability also depends upon both the volume of services performed and the Company's ability to manage costs. As a significant portion of the Company's cost is labor related, WidePoint must effectively manage these costs to achieve and grow its profitability. To date, the Company has attempted to maximize its operating margins through efficiencies achieved by the use of its proprietary methodologies, and by offsetting increases in consultant salaries with increases in consultant fees received from its clients. The uncertainties relating to the ability to achieve and maintain profitability, obtain additional funding to partially fund the Company's growth strategy and provide the necessary investment to continue to upgrade its management reporting systems to meet the continuing demands of the present regulatory changes affect the comparability of the information reflected in the selected consolidated financial information presented above.

Results of Operations

Three Months Ended March 31, 2005 as Compared to Three Months Ended March 31, 2004

Revenue. Revenue for the three month period ended March 31, 2005 was approximately \$2,670,000 as compared to approximately \$723,000 for the three month period ended March 31, 2004. The increase in revenue was primarily attributable to a full quarter of revenues from our acquisition of ORC in October 2004.

Cost of sales. Cost of sales for the three month period ended March 31, 2005, was approximately \$1,847,000, or 70% of revenues, an increase of approximately \$1,281,000 over cost of sales of approximately \$566,000, or 78% of revenues, for the three month period ended March 31, 2004. The percentage decrease in cost of sales was primarily attributable to lower cost of sales associated with the performance of revenues at ORC. The absolute increase in cost of sales was materially attributable to higher revenues and cost of sales as a result of our acquisition of ORC in October 2004.

Gross profit. As a result of the above, gross profit for the three month period ended March 31, 2005, was approximately \$822,000, or 30% of revenues, an increase of approximately \$665,000 over gross profit of approximately \$157,000, or 22% of revenues, for the three month period ended March 31, 2004.

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Sales and marketing. Sales and marketing expense for the three month period ended March 31, 2005, was approximately \$176,000, or 7% of revenues, an increase of approximately \$74,000, as compared to approximately \$102,000, or 14% of revenues, for the three month period ended March 31, 2004. The increase was materially attributable to the increase in sales and marketing expenses from our acquisition of ORC in October 2004.

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General and administrative. General and administrative expenses for the three month period ended March 31, 2005, were approximately \$728,000, or 27% of revenues, an increase of approximately \$578,000, as compared to approximately \$150,000, or 21% of revenues, incurred by the Company for the three month period ended March 31, 2004. The increase in general and administrative expenses for the three months ended March 31, 2005, was primarily attributable to an increase of approximately \$578,000 in additional general and administrative expenses associated with our acquisition of ORC in October 2004, other general and administrative costs associated with the integration of ORC with WidePoint, increases in our accounting and legal fees associated with our requisite filings with the Securities and Exchange Commission, and WidePoint's mergers and acquisitions efforts currently underway.

Depreciation and amortization. Depreciation and amortization expenses for the three month period ended March 31, 2005, was approximately \$89,000, or 3% of revenues, an increase of \$87,000, as compared approximately \$1,800 of such expenses, or less than 1% of revenues, recorded by the Company for the three month period ended March 31, 2004. The increase in depreciation and amortization expenses for the three month period ended March 31, 2005, was primarily attributable to greater amounts of depreciable assets as a result of the acquisition of ORC in October 2004 and an increase in amortization expense associated with the purchase accounting related to the purchase of ORC in October 2004.

Interest income. Interest income for the three month period ended March 31, 2005, was \$770, or less than 1% of revenues, a decrease of \$1,092 as compared to \$1,862, or less than 1% of revenues, for the three month period ended March 31, 2004. The decrease in interest income for the three month period ended March 31, 2005, was primarily attributable to lesser amounts of cash and cash equivalents along with lower short term interest rates that were available to the Company on investments in overnight sweep accounts.

Interest expense. Interest expense for the three month period ended March 31, 2005, was \$52,783, or 2% of revenues, an increase of \$52,668 as compared to \$115, or less than 1% of revenues, for the three month period ended March 31, 2004. The increase in interest expense for the three month period ended March 31, 2005 was primarily attributable to WidePoint's increase in interest expense associated with its recent secured senior lending facility with RBC-Centura which was utilized in association with the purchase of ORC.

Gain on Financial instrument. The gain on financial instrument for the three month period ended March 31, 2005, was approximately \$996,000. The gain on financial instrument represents the decrease during the three months ended March 31, 2005 in the estimated fair value of the warrants issued to Barron Partners, L. P. in connection with the preferred stock financing. The estimated fair value of the warrants decreased principally because the estimated volatility of the Company's stock declined. This decline in turn resulted from the relatively narrow trading range of the Company's stock in the quarter as compared to past history. A less volatile stock provides a lower probability that the warrant holder will be able to eventually realize a gain on exercise. The effect of the decreased estimated volatility was partially offset by the increase in the value of the Company stock underlying the warrants, as well as the increased market interest rates during the quarter which have an upward effect on the warrant value.

Other. Other income for the three month period ended March 31, 2005, was \$2,150, or less than 1% of revenues. Other income was primarily attributable to finder's fees. There were no other income for the three month period ended March 31, 2004.

Net income. As a result of the above, the net income for the three month period ended March 31, 2005, was approximately \$776,000 as compared to the net loss of approximately \$95,000 for the three months ended March 31, 2004.

Liquidity and Capital Resources

The Company has, since inception, financed its operations and capital expenditures through the sale of preferred and common stock, seller notes, convertible notes, convertible exchangeable debentures, senior secured loans and the proceeds from the exercise of the warrants related to a convertible exchangeable debenture. During 2004 and the quarter ended March 31, 2005, operations were materially financed with working capital, senior debt and the proceeds from a convertible preferred stock issuance.

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Cash provided by operating activities for the quarter ended March 31, 2005, was approximately \$169,600 as compared to cash provided by operating activities of approximately \$10,400 for the quarter ended March 31, 2004. The decrease in cash balances available for operating activities for the quarters ended March 31, 2005 and 2004, respectively, were primarily a result of investments in which we expanded our sales

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and general and administrative cost structure to implement our growth strategy. Capital expenditures in property and equipment were approximately \$1,000 for the quarter ended March 31, 2005, as compared to capital expenditures in property and equipment of no material amount for the quarter ended March 31, 2004.

As of March 31, 2005, the Company had a net working capital deficit of approximately \$6.3 million. Excluding the impact of the financial instruments associated with the issuance of the common stock warrants attributable to the preferred stock capital investment by Barron Partners, LP in the Company in October 2004 and discussed below, the working capital deficit would be reduced by approximately \$5.7 million, resulting in an adjusted net working capital deficit of approximately \$0.8 million.

WidePoint's primary source of liquidity consists of approximately \$0.3 million in cash and cash equivalents and approximately \$2.3 million of accounts receivable. The increase in accounts receivable was primarily the result of the Company's acquisition of ORC and is attributable to slower processing and collection times associated with the normal billing and collecting cycle of ORC as compared to WidePoint. Current liabilities include approximately \$2.0 million in accounts payable and accrued expenses; \$1.4 million in a line of credit with RBC Centura Bank; and \$5.7 million in financial instruments which may be converted to equity upon the extinguishment of the Company's liquidated damages clause within the registration rights agreement entered into with Barron Partners, LP. The material increase in liabilities is predominately the result of the acquisition of ORC and the increase in the computed valuation of the financial instrument as of March 31, 2005.

The Company's business environment is characterized by rapid technological change, experiences times of high growth and contraction and is influenced by material events such as mergers and acquisitions that can substantially change the Company's outlook.

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

On October 25 and 29, 2004, WidePoint completed financings with Barron Partners L.P. (Barron), a private equity fund that engages in investing primarily in private investments in publicly traded entities, for an aggregate amount of \$3,580,000, under a preferred stock purchase agreement and related agreements. Net proceeds from the financing after costs and expenses, including fees of finders and agents, were approximately \$3,030,000. WidePoint issued an aggregate of 2,045,714 shares of its Series A Convertible Preferred Stock that are convertible into an aggregate of 20,457,143 shares of its Common Stock at a conversion rate equal to \$0.175 per share. In addition, WidePoint issued to Barron warrants to purchase up to an additional 10,228,571 shares of its Common Stock at an exercise price of \$0.40 per common share. In April and May, 2005, Barron exercised warrants for 2,000,000 shares of common stock, providing \$800,000 in gross proceeds to the Company.

Pursuant to the registration rights agreement, between Barron and WidePoint, related to the stock issuances described in the preceding paragraph, WidePoint filed a registration statement on January 5, 2005, covering the resale of the shares of common stock issuable upon conversion and/or exercise of the Series A Convertible Preferred Stock and the warrants issued to Barron. If our registration statement is not declared effective by the Securities and Exchange Commission by April 23, 2005 and thereafter kept effective through October 20, 2007, subject to permissible blackout periods and registration maintenance periods, then WidePoint may be required to pay Barron a maximum penalty of up to \$20,000 for each month the registration statement is not effective. As of May 16, 2005, the registration statement has not been made effective.

WidePoint believes that its current cash position and line of credit is sufficient to meet capital expenditure and working capital requirements for the near term. From a current trend perspective, WidePoint believes that the adjusted net working capital deficit of \$0.8 Million (excluding the impact of the Financial Instrument) will improve modestly, as the investment costs of software development programs are substantially reduced and additional proceeds are realized from the exercise of Warrants by investors; both of which will be partially offset by incremental working capital needs associated with the projected Revenue growth of the business. WidePoint is unaware of any additional known trends or uncertainties not described herein that are reasonably likely to result in liquidity increasing or decreasing in any material way. However, the growth and technological change of the market make it difficult to predict future liquidity requirements with certainty. Over the longer term, the Company must successfully execute its plans to increase revenue and income streams that will generate significant positive cash flows if it is to sustain adequate liquidity without impairing growth or requiring the infusion of additional funds from external sources. Further, our failure to comply with the restrictive covenants under our revolving credit facilities could result in an event of default, which, if not cured, amended, or waived, could result in us being required to repay these borrowings before their due date. To date any covenants that we have not been compliant with have either been amended or waived and we continue to work with RBC-Centura to structure appropriate covenants that match our present business condition and environment. Although we currently are not in compliance with two of our covenants, which includes our ebitda to debt ratio covenant and our net income covenant, RBC-Centura has waived such violations until such time as the Company delivers to RBC-Centura the Company's financial statements for the quarter ended June 30, 2005 evidencing that the Company is in compliance with the above covenants. If we are forced to refinance these borrowings on less favorable terms, our results of operations and financial condition could be adversely affected due to the increased cost and interest rate. Additionally, a major expansion, such as occurred with the acquisition of ORC or any other

major new subsidiaries, might require external financing that could include additional debt or equity capital. The Company obtained a one year senior line of credit from RBC-Centura Bank in October 2004 for up to \$2.5 million dollars, collateralized against accounts receivables, that also allows for the expansion of this line of credit up to \$5.0 million upon the successful completion of an additional acquisition. The interest rate on the line of credit is variable, and is based upon the prime lending rate. Approximately \$1.2 million dollars of the senior line of credit was utilized in the acquisition of ORC. In addition, the Company raised approximately \$3.6 million dollars in connection with the aforementioned equity investments by Barron Partners, LP, that were used in the acquisition of ORC. There can be no assurance that additional financing, if required, will be available on acceptable terms, if at all, for future acquisitions and/or growth initiatives.

Off-Balance Sheet Arrangements

The Company has no existing off-balance sheet arrangements as defined under SEC regulations.

ITEM 3. CONTROLS AND PROCEDURES.

Disclosure Controls and Procedures

The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms, and include controls and procedures designed to ensure that such information is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, to allow timely decisions regarding required disclosure. Based on the evaluation of the effectiveness of the Company's disclosure controls and procedures as of March 31, 2005 required by Rule 13a-15(b) under the Securities Exchange Act of 1934 and conducted by the Company's principal executive and principal financial officers, such officers concluded that the Company's disclosure controls and procedures were not effective as of March 31, 2005. That conclusion was based on the existence of the material weakness in our internal control over financial reporting discussed below.

Changes in Internal Control Over Financial Reporting

In connection with the evaluation by the Company's principal executive and principal financial officers required by Rule 13a-15(d) under the Securities Exchange Act of 1934, such officers determined that the following change in the Company's internal control over financial reporting occurred during the quarter ended March 31, 2005, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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We identified a material weakness in our internal control over financial reporting in the first quarter of 2005 that related to insufficient technical accounting expertise within our accounting function to resolve non-routine or complex accounting and tax matters that occurred in connection with (i) our recent material acquisition of Operational Research Consultants, Inc. in October 2004; and (ii) determination of the proper accounting treatment of the financial instrument relating to the warrants issued by the Company in October 2004. The material weakness in internal controls resulted in (i) our late filing on April 19, 2005 (four days after the extended due date) of our Annual Report on Form 10-K for the year ended December 31, 2004, and (ii) the need to restate the recorded amount of the financial instrument at December 31, 2004 and March 31, 2005 due to the failure to mark-to-market such instrument at December 31, 2004. In an effort to remediate that material weakness, we engaged a consulting firm in January 2005 with the requisite accounting expertise, and are continuing to use the services of that firm in connection with such complex accounting matters.

PART II.

OTHER INFORMATION

ITEM 6. EXHIBITS.

(a) Exhibits

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

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

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