

ION NETWORKS INC  
Form 10QSB  
November 14, 2006

**U.S. SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-QSB**

**[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934**

For the quarterly period ended September 30, 2006

OR

**[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No.: 0-13117

**ION NETWORKS, INC.**

(Exact Name of Small Business Issuer in Its Charter)

Delaware

22-2413505

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(State or Other Jurisdiction of  
Incorporation or Organization)

(IRS Employer Identification Number)

120 Corporate Boulevard, South Plainfield, NJ 07080

(Address of Principal Executive Offices)

(908) 546-3900

(Issuer'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 proceeding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days:

Yes  No .

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

There were 32,785,565 shares of Common Stock outstanding as of November 13, 2006.

**Transitional Small Business Disclosure Format:**

Yes  No



**ION NETWORKS, INC. AND SUBSIDIARY**

**FORM 10-QSB**

**FOR THE QUARTER ENDED SEPTEMBER 30, 2006**

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**PART I. FINANCIAL INFORMATION**

**ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

The condensed consolidated financial statements included herein have been prepared by the registrant without audit pursuant to the rules and regulations of the Securities and Exchange Commission. Although the registrant believes that the disclosures are adequate to make the information presented not misleading, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. It is suggested that these financial statements be read in conjunction with the audited financial statements and the notes thereto included in the registrant's report on Form 10-KSB for the year ended December 31, 2005 as filed with the Securities and Exchange Commission.

**ION NETWORKS, INC. AND SUBSIDIARY****CONDENSED CONSOLIDATED BALANCE SHEET**

As of September 30, 2006

(Unaudited)

**Assets**

Current assets	
Cash and cash equivalents	\$ 61,388
Accounts receivable, less allowance for doubtful accounts of \$16,275	427,341
Inventories, net	598,881
Prepaid expenses and other current assets	29,554
Total current assets	1,117,164
Property and equipment, net	33,169
Capitalized software, net	1,107,682
Deferred financing costs, net	33,148
Other assets	22,996
Total assets	\$ 2,314,159

**Liabilities and Stockholders Equity**

Current liabilities	
Accounts payable	\$ 236,638
Revolving credit facility	200,000
Accrued expenses	169,596
Accrued payroll and related liabilities	60,680
Current portion of long-term debt	2,488
Deferred income	157,401
Other current liabilities	10,000
Total current liabilities	836,803
Long-term liabilities	



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Accrued interest related party	15,814
Long-term debt, net of current portion	2,645
Total long-term liabilities	18,459
Total liabilities	855,262
Commitments and contingencies	
Stockholders' Equity	
Preferred stock par value \$.001 per share; authorized 1,000,000 shares; 200,000 shares designated Series A; 155,557 shares issued and outstanding (aggregate liquidation preference \$280,003)	156
Common stock par value \$.001 per share; authorized 50,000,000 shares; 32,785,565 shares issued and outstanding	32,786
Additional paid-in capital	45,638,307
Accumulated deficit	(44,212,352)
Total stockholders' equity	1,458,897
Total liabilities and stockholders' equity	\$ 2,314,159

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

## ION NETWORKS, INC. AND SUBSIDIARY

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	For the Three Months Ended September 30, 2006	For the Three Months Ended September 30, 2005	For the Nine Months Ended September 30, 2006	For the Nine Months Ended September 30, 2005
Net sales	\$ 872,945	\$ 1,158,928	\$ 2,617,356	\$ 3,141,509
Cost of sales	395,726	330,062	1,069,242	959,928
Gross margin	477,219	828,866	1,548,114	2,181,581
Research and development expenses, including \$17,007 and \$51,398 of non-cash stock based compensation for the three and nine months ended September 30, 2006, respectively.	173,651	120,199	478,057	397,198
Selling, general and administrative expenses, including \$30,649 and \$94,084 of non-cash stock based compensation for the three and nine months ended September 30, 2006, respectively.	603,522	672,851	1,923,111	1,998,213
Depreciation expense	3,820	2,158	11,690	7,070

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Restructuring, and other credits	-	-	(81,000)	-
Total operating expenses	780,993	795,208	2,331,858	2,402,481
(Loss)income from operations	(303,774)	33,658	(783,744)	(220,900)
Other income	396	-	396	15,339
Interest income/(expense) related party	-	(2,595)	(1,696)	(7,306)
Interest income/(expense) (1)	(9,449)	(2,527)	(32,438)	(2,562)
(Loss)income before income taxes	(312,827)	28,536	(817,482)	(215,429)
Income tax expense	50	-	563	822
Net (loss)income	\$ (312,877)	\$ 28,536	\$ (818,045)	\$ (216,251)
Per share data:				
Net income(loss) per share				
Basic	\$ (0.01)	\$ 0.00	\$ (0.03)	\$ (0.01)
Diluted	\$ (0.01)	\$ 0.00	\$ (0.03)	\$ (0.01)
Weighted average number of common shares outstanding				
Basic	32,785,565	27,050,044	30,954,167	25,606,383
Diluted	32,785,565	32,041,785	30,954,167	25,606,383

(1) Includes amortization of deferred financing costs of \$8,833 and \$26,986 for the three and nine months ended September 30, 2006.

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



**ION NETWORKS, INC. AND SUBSIDIARY**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)

	For the Nine Months	For the Nine Months
	Ended September 30,	Ended September 30,
	2006	2005
Cash flows from operating activities		
Net loss	\$ (818,045)	\$ (216,251)
Adjustments to reconcile net loss to net cash used in operating activities:		
Restructuring and other credits	(81,000)	-
Depreciation and amortization	179,582	100,224
Non-cash stock-based compensation	151,556	-
Provision for inventory reserve	(55,290)	(49,296)
Interest on convertible debt related party	1,696	7,306
Amortization of deferred financing costs	26,986	2,083
Changes in operating assets and liabilities:		
Accounts receivable	596,573	(318,038)
Inventories	(17,513)	(31,234)
Prepaid expenses and other current assets	45,825	11,485
Other assets	(85)	-
Accounts payable	(184,726)	(63,635)
Accrued expenses	(29,971)	(37,980)
Accrued payroll and related liabilities	(200,067)	36,443
Deferred income	(9,709)	(47,685)
Sales tax payable	-	(6,060)
Net cash used in operating activities	(394,188)	(612,638)

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Cash flows from investing activities		
Acquisition of property and equipment	(15,566)	(10,686)
Capitalized software expenditures	(383,898)	(458,127)
Net cash used in investing activities	(399,464)	(468,813)
Cash flows from financing activities		
Principal payments on debt and capital leases	(6,805)	(1,725)
Advances from related parties	-	160,500
Repayment of advances from related parties	-	(160,500)
Borrowings from revolving credit facility	465,000	200,000
Repayment of revolving credit facility	(265,000)	-
Deferred financing costs	(2,698)	(25,000)
Proceeds from the sale of common stock	-	671,141
Proceeds from the exercise of warrants, net	468,201	-
Net cash provided by financing activities	658,698	844,416
Net decrease in cash and cash equivalents	(134,954)	(237,035)
Cash and cash equivalents beginning of period	196,342	287,437
Cash and cash equivalents end of period	\$ 61,388	\$ 50,402

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



**ION NETWORKS, INC. AND SUBSIDIARY**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

September 30, 2006

(Unaudited)

**NOTE 1 - CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

ION Networks, Inc ("ION" or the "Company") designs, develops, manufactures and sells security solutions that protect enterprise network administrative interfaces from improper, unauthorized or otherwise undesirable access from external and internal sources. Administrative interfaces are the network access points used by highly trained technical individuals who are charged with the responsibilities of maintaining and supporting the networks and devices employed within the networks such as servers, routers, PBXs and similar network equipment. These technicians may be employees of the enterprise or employed by third parties such as managed service providers, consultants, device vendors or application developers. In all cases, they are considered trusted insiders since in order to perform their jobs, permission to enter and work within the network must be granted. The Company's solution, comprised of centralized management and control software, administrative security appliances and soft tokens, are designed to provide secure, auditable access to all administrative interfaces and monitored security once working within the network. Service Providers, Enterprises and Governmental Agencies utilize the ION solution globally in their voice, data and converged environments, to establish and maintain security policies while providing the support and maintenance required of networks and their devices.

The Company is a Delaware corporation founded in 1999 through the combination of two companies - MicroFrame ("MicroFrame"), a New Jersey Corporation (the predecessor entity to the Company, originally founded in 1982), and SolCom Systems Limited ("SolCom"), a Scottish corporation located in Livingston, Scotland (originally founded in 1994). The Scottish corporation was dissolved in 2003. The Company's principal objective is to address the need for security and network management and monitoring solutions, primarily for the PBX-based telecommunications market, resulting in a significant portion of the Company's revenues being generated from sales to various telecommunications companies.

The condensed consolidated balance sheet as of September 30, 2006, the condensed consolidated statements of operations for the three and nine months ended September 30, 2006 and 2005 and the condensed consolidated statements of cash flows for the nine months ended September 30, 2006 and 2005, have been prepared by the Company without audit. In the opinion of management, all adjustments (which include normal recurring adjustments) necessary to make the Company's financial position, results of operations and cash flows at September 30, 2006 and 2005 not misleading have been made. The results of operations for the three and nine months ended September 30, 2006 and 2005 are not indicative of a full year or any other interim period.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. It is suggested that these financial statements be read in conjunction with the audited financial statements and notes thereto



included in the report on Form 10-KSB for the year ended December 31, 2005, filed with the Securities and Exchange Commission.

At September 30, 2006, the Company had an accumulated deficit of \$44,212,352 and working capital of \$280,361. The Company also realized a net loss of \$818,045 for the nine months ended September 30, 2006. During the nine months ended September 30, 2006 the Company received net proceeds of \$468,201 from the exercise of 3,325,882 warrants. The Company continues to have a delicate cash position. Management believes it is necessary for it to continue to strictly manage expenditures and to increase product revenues. In addition, the Company has historically received proceeds from the sale of its New Jersey Net Operating Losses during the fourth quarter of previous years. While no assurance can be made that the Company will again receive such proceeds, the Company has been approved for this program in 2006 and expects to use the proceeds received under this program for general working capital purposes.

The Company failed to comply with certain financial covenants in the Revolving Credit Facility as of March 31, 2006 and September 30, 2006. This default can result in the Company not being permitted to borrow under the Revolving Credit Facility in the future. The Company's ability to continue operations will be materially adversely affected if it is unable to borrow under the Revolving Credit Facility and it is unable to replace the Revolving Credit Facility with another credit facility having satisfactory financial and other terms. The Company received a waiver on its March 31, 2006 financial covenant default. The waiver included a modification to the Financing agreement whereby the borrower can add back non cash adjustments for stock based compensation for the purpose of calculating the net profit after tax covenant requirement. The Company has not yet received a waiver on its September 30, 2006 financial covenant default, and accordingly, has classified the amounts due as a current liability. However, the Company is currently in the process of seeking a waiver on this default, although there is no assurance that one will be obtained.

## **NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### *Principles of Consolidation*

The accompanying condensed consolidated financial statements include the accounts of ION Networks, Inc. and Subsidiary. All material inter-company balances and transactions have been eliminated in consolidation.

### *Reclassifications*

Certain amounts in the financial statements for the three and nine months ended September 30, 2005 have been reclassified to conform to the presentation of the financial statements for the three and nine months ended September 30, 2006. There was no change in previously reported net loss.

### *Capitalized Software*

The Company capitalizes computer software development costs in accordance with the provisions of Statement of Financial Accounting Standards No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed" ("SFAS No. 86"). SFAS No. 86 requires that the Company capitalize computer software development costs upon the establishment of the technological feasibility of a product, to the extent that such costs are expected to be recovered through future sales of the product. Management is required to use professional judgment in determining whether development costs meet the criteria for immediate expense or capitalization. These costs are amortized to cost of sales by the greater of the amount computed using (i) the ratio that current gross revenues from the sales of software bear to the total of current and anticipated future gross revenues from the sales of that software, or (ii) the straight-line method over the estimated useful life of the product. As a result, the carrying amount of the capitalized software costs may be reduced materially in the near term.

The Company records impairment losses on capitalized software and other long-lived assets used in operations when events and circumstances indicate that the assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amount of those items. The Company's cash flow estimates are based on historical results adjusted to reflect its best estimate of future market and operating conditions. The net carrying value of assets not recoverable is reduced to fair value. While the Company believes that its estimates of future cash flows are reasonable, different assumptions regarding such cash flows could materially affect the Company's estimates.

Amortization expense totaled \$69,916 and \$27,461 for the three months ending September 30, 2006 and 2005, respectively. Amortization expense totaled \$167,892 and \$93,155 for the nine months ending September 30, 2006 and 2005, respectively. Amortization expense is included in Cost of Sales in the Statement of Operations.

### *Net Loss Per Share*

Basic net loss per share is computed by dividing net loss attributable to common shareholders by the weighted average number of common shares outstanding during the period. Diluted net loss per share reflects the potential dilution that could occur if securities or other instruments to issue common stock were exercised or converted into common stock. Potentially dilutive securities of 9,320,688 and 12,785,422 at September 30, 2006 and 2005 are excluded from the computation of diluted net loss per share as their inclusion would be antidilutive.

## Stock-Based Compensation

The Company had stock-based compensation expense in the amount of \$49,615 and \$151,556 for the three and nine months ended September 30, 2006. Prior to January 1, 2006, the Company accounted for stock-based compensation under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25 ( APB 25 ). Accordingly, the Company generally recognized compensation expense only when it granted options with a discounted exercise price. Any resulting compensation expense was recognized ratably over the associated service period, which was generally the option vesting term. Prior to January 1, 2006, the Company provided pro-forma disclosure amounts in accordance with FAS No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure" ("FAS 148"), as if the fair value method defined by FAS No. 123, Accounting for Stock-Based Compensation ( FAS 123 ), had been applied to its stock-based compensation.

Effective January 1, 2006, the Company adopted the fair value recognition provisions of Share Based Payment ( FAS 123R ), using the modified prospective transition method and therefore has not restated prior periods' results. Under this transition method, stock-based compensation expense for the three and nine months ended September 30, 2006 included compensation expense for stock-based compensation awards granted prior to, but not yet fully vested as of January 1, 2006 based on the grant date fair value estimated in accordance with the original provisions of FAS 123. Stock-based compensation expense for all share-based payment awards granted after January 1, 2006 is based on the grant-date fair value estimated in accordance with the provisions of FAS 123R. The Company recognizes these compensation costs over the requisite service period of the award, which is generally the option vesting term.

As a result of adopting FAS 123R, the impact to the Condensed Consolidated Financial Statements for the three and nine months ended September 30, 2006 on net loss was \$49,615 and \$151,556, respectively, greater than if the Company had continued to account for stock-based compensation under APB 25. There is no impact on both basic and diluted net loss per share for the three and nine months ended September 30, 2006. As of September 30, 2006, the unvested options totaled \$195,337 of which \$105,283 is for options granted prior to January 1, 2006 and \$90,054 is for options granted after January 1, 2006.

The fair value of share-based payment awards was estimated using the Black-Scholes option pricing model with the following assumptions and weighted average fair values as follows:

	<b>Nine months ended September 30</b>	
	<b>2006</b>	<b>2005</b>
Risk-free interest rate	4.85%-5.10%	4.00%
Dividend yield	N/A	N/A
Expected volatility	208-224%	69.25-71.20%
Expected life in years	5	5
Expected forfeiture rate (through term)	75.9%	-

The pro forma table below reflects net loss and basic and diluted net loss per share for the three and nine months ended September 30, 2005 had the Company applied the fair value recognition provisions of SFAS 123, as follows:

	Three months ended		Nine months ended	
	September 30, 2005		September 30, 2005	
	(Unaudited)		(Unaudited)	
Net income(loss) as reported	\$	28,536	\$	(216,251)
Deduct: Stock based employee compensation determined under fair value method		(38,981)		(106,148)
Net loss pro forma	\$	(10,445)	\$	(322,399)
 Basic and diluted net loss per share:				
Basic and diluted - as reported	\$	0.00	\$	(0.01)
Basic and diluted - pro forma	\$	0.00	\$	(0.01)

The determination of the fair value of stock-based awards on the date of grant is affected by the Company's stock price as well as assumptions regarding a number of complex and subjective variables. These variables include the price of the underlying stock, the Company's expected stock price volatility over the expected term of the awards, actual and projected employee stock option exercise behaviors, risk-free interest rate and the expected annual dividend yield on the underlying shares.

The Company uses historical information to estimate expected life and forfeitures within the valuation model. The risk-free rate for periods within the expected life of the award is based on the U.S. Treasury yield curve in effect at the time of grant. Expected volatility is based on historical volatility of the price of our common stock over the calculated expected life. The Company does not anticipate paying cash dividends in the future and therefore uses an expected dividend yield of 0.0%.

Developing these assumptions requires significant judgment on the part of the Company and, generally, may involve analyzing available historical data, considering whether historical data is relevant to predicting future behavior, making appropriate adjustments to historical data for future expectations, supplementing or replacing Company-specific historical data with data from other supportable sources and appropriately weighting each of the inputs. These assumptions are evaluated at each grant date. If factors change and the Company employs different assumptions for estimating share-based compensation expense in future periods or if the Company decides to use a different valuation model, the future periods may differ significantly from what the Company has recorded in the current period and could materially affect operating income, net income/(loss) and net income/(loss) per share. Option valuation models require the input of highly subjective assumptions including the expected life of the option. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options. Consequently, there is a significant risk that the Company's estimates of the fair values of stock-based compensation awards on the grant dates may not reflect the actual values realized upon the vesting, exercise, expiration, early termination or forfeiture of those stock-based payments in the future.

If actual results differ significantly from these estimates or different key assumptions were used, there could be a material effect on the Company's financial statements. The future impact of the cost of stock-based compensation on our results of operations, including net income/(loss) and earnings/(loss) per diluted share, will depend on, among other factors, the level of equity awards as well as the market price of the Company's common stock at the time of the award as well as various other assumptions used in valuing such awards. The Company will periodically evaluate these estimates.



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A summary of option activity for the nine months ended September 30, 2006 is as follows:

Options	Shares	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2006	4,889,831	\$0.32	4.15 years	
Granted	2,777,000	\$0.18	4.25 years	
Exercised	-	-	-	
Canceled	(492,150)	\$0.25	4.20 years	
Expired	(85,650)	\$0.90	0 years	
Outstanding at September 30, 2006	7,089,031	\$0.27	3.71 years	\$7,500
Exercisable at September 30, 2006	4,184,714	\$0.21	3.13 years	\$7,500

A summary of the status of the Company's non-vested shares as of September 30, 2006, and changes during the nine months ended September 30, 2006 is presented below:

Non-vested Shares	Shares	Weighted-Average Grant Date Fair Value
Non-vested at January 1, 2006	1,019,081	\$0.60
Granted	2,400,000	\$0.11
Vested	(422,064)	\$0.23
Forfeited	(92,700)	\$0.12
Non-vested at September 30, 2006	2,904,317	\$0.17

The weighted-average grant-date fair value of options granted during the nine months ended September 30, 2006 and 2005 amounted to \$0.18 per share. There have been no exercises of stock options during the nine months ended September 30, 2006.

*Warranty Costs*

The Company estimates its warranty costs based on historical warranty claim experience. Future costs for warranties applicable to sales recognized in the current period are charged to cost of sales. The warranty accrual is reviewed quarterly to reflect the remaining obligation. Adjustments are made when actual warranty claim experience differs from estimates. The warranty accrual included in other current liabilities as of September 30, 2006 is \$10,000.

#### *New Accounting Pronouncements*

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* ( SFAS No. 157 ). This Statement defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements and accordingly, does not require any new fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is in the process of evaluating the potential impact, if any, of the adoption of SFAS No. 157 will have on our results of operations, financial condition and cash flow.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" ("FIN 48"), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in its financial statements, the impact of a tax position, if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective as of the beginning of the Company's 2007 fiscal year, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. The Company is currently evaluating the impact of adopting FIN 48 on its financial statements.

In March 2006, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standard 156 *Accounting for Servicing of Financial Assets* ( SFAS 156 ), which requires all separately recognized servicing assets and servicing liabilities be initially measured at fair value. SFAS 156 permits, but does not require, the subsequent measurement of servicing assets and servicing liabilities at fair value. Adoption is required as of the beginning of the first fiscal year that begins after September 15, 2006. Early adoption is permitted. The adoption of SFAS 156 is not expected to have a material effect on the Company's consolidated financial position, results of operations or cash flows.

In February 2006, the FASB issued Statement of Financial Accounting Standard 155 *Accounting for Certain Hybrid Financial Instruments* ( SFAS 155 ), which eliminates the exemption from applying SFAS 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), to interests in securitized financial assets so that similar instruments are accounted for similarly regardless of the form of the instruments. SFAS 155 also allows the election of fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a remeasurement event. Adoption is effective for all financial





instruments acquired or issued after the beginning of the first fiscal year that begins after September 15, 2006. Early adoption is permitted. The adoption of SFAS 155 is not expected to have a material effect on the Company's consolidated financial position, results of operations or cash flows.

**NOTE 3 - INVENTORIES**

Inventories, net of allowance for obsolescence of \$48,813 at September 30, 2006, consists of the following:

Raw materials	\$	287,908
Finished goods		310,973
	\$	598,881

**NOTE 4 RESTRUCTURING AND OTHER CREDITS**

As of September 30, 2006, the Company has included as part of accounts payable and accrued expenses certain liabilities that may, in the future, result in additional restructuring credits. The Company's accounts payable balance includes invoices for professional services in the amount of \$88,687. Accrued expenses include professional services in the amount of \$118,671. These items arose from alleged services provided to the Company between November 2002 and August 2003. The Company is disputing these amounts with the vendors, however, at the present time, management is unable to estimate the final outcome of these disputes but believes that the final settlement amount should not exceed the total of the above amounts. The Company released \$60,000 of professional services and \$21,000 of shareholder relations related expenses from disputed accruals during the nine months ended September 30, 2006.

**NOTE 5 REVOLVING CREDIT FACILITY**

On September 21, 2005, the Company entered into the asset based Revolving Credit Facility, for \$2.5 million with Bridge Bank, N.A. The Revolving Credit Facility has a two-year term, which upon maturity, requires payment of the outstanding principal and interest balance. The Revolving Credit Facility provides for advances of up to \$2.0 million against 80% of eligible accounts receivables and an additional \$500,000 against inventory capped at 30% of eligible accounts receivables. The annual interest rate is prime plus 1.75% (10.0% at September 30, 2006), with a minimum prime rate of 6.25%. Certain assets of the Company secure the Revolving Credit Facility, and the Company is subject to certain financial and restrictive covenants, as defined in the agreement. As of September 30, 2006, the outstanding balance on the Revolving Credit Facility was \$200,000.

The Company failed to comply with certain financial covenants in the Revolving Credit Facility, as of March 31, 2006 and September 30, 2006. This default can result in the Company not being permitted to borrow under the Revolving Credit Facility in the future. The Company's ability to continue operations will be materially adversely affected if it is unable to borrow under the Revolving Credit Facility and it is unable to replace the Revolving Credit Facility with another credit facility having satisfactory financial and other terms.

The Company received a waiver on its March 31, 2006 financial covenant default. The waiver included a modification to the financing agreement whereby the borrower can add back non cash adjustments for stock based compensation for the purpose of calculating the net profit after tax covenant requirement. The Company has not yet received a waiver on its September 30, 2006 financial covenant default, however, the Company is currently in the process of seeking a waiver on this default, although there is no assurance that one will be obtained. -

## **NOTE 6 STOCKHOLDERS EQUITY**

### *Common Stock*

On August 5, 2004, the Company issued a convertible debenture (the "Debenture") for \$200,000 cash to Stephen M. Deixler, one of the Company's directors. On February 15, 2006, Mr. Deixler converted the Debenture into 2,409,639 shares of common stock. The Debenture would have matured on August 5, 2008 and had an interest rate of five (5%) percent per annum, compounded annually. The principal amount of the Debenture was convertible at any time by the holder into shares of the Company's common stock, \$.001 par value, at a conversion price equal to \$0.083 per share (the "Conversion Price"), for a total of 2,409,639 shares of common stock.

### *Warrants*

In connection with the sale of common stock on February 14, 2002, the Company issued warrants to purchase 1,120,000 shares of common stock with a five year term and an exercise price of \$1.25 per share, subject to certain adjustments, including a weighted-average ratchet adjustment for certain issuances of the Company's equity securities below the warrant exercise price. On April 25, 2006, the Company agreed to reduce the warrant exercise price to \$0.15 per share on the condition that warrant holders simultaneously exercise all warrants. The Company received net proceeds of \$168,000 from the exercise of these 1,120,000 warrants on April 27, 2006.

In connection with the sale of common stock on March 31, 2005, warrants to purchase 2,205,882 shares of common stock, subject to certain adjustments, with a five year term and an exercise price of \$0.23 per share, subject to certain adjustments, including a full ratchet adjustment for certain issuances of the Company's equity securities below the warrant exercise price, were issued. In the event that the closing bid price of the Company's common stock equaled or exceeded \$0.69 per share for a period of 20 consecutive trading days and certain other conditions were met, the Company would redeem the warrants on 30 days prior written notice (during which periods the warrants could exercised) for a redemption price of \$.001 per share of common stock underlying such warrants. On April 25, 2006, the Company agreed to reduce the warrant exercise price to \$0.15 on the condition that warrant holders simultaneously exercise all warrants. The Company received net proceeds of \$330,882 from the exercise of these 2,205,882 warrants on April 27, 2006.

### *Options*

The Company has two option plans in place and adopted in previous years.

In June 1998, the Company adopted its 1998 Stock Option Plan (the "1998 Plan"). The aggregate number of shares of common stock for which options may be granted under the 1998 Plan is 3,000,000. The maximum number of options which may be granted to an employee during any calendar year under the 1998 Plan is 400,000. The term of these non-transferable stock options may not exceed ten years. The exercise price of these stock options may not be less than 100% (110% if the person granted such options owns more than ten percent of the outstanding common stock) of the fair value of one share of common stock on the date of grant.

In November 2000, the Company adopted its 2000 Stock Option Plan (the "2000 Plan"). The aggregate number of shares of common stock for which options may be granted under the 2000 Plan is 3,000,000. The maximum number of options which may be granted to an employee during any calendar year under the 2000 Plan is 400,000. The term of these non-transferable stock options may not exceed ten years. The exercise price of these stock options may not be less than 100% (110% if the person granted such options owns more than ten percent of the outstanding common stock) of the fair value of one share of common stock on the date of grant.

On January 23, 2006, the Company adopted its 2006 Stock Incentive Plan (the "2006 Plan"). The aggregate number of shares of common stock for which options may be granted under the 2006 Plan is 4,000,000. The maximum number of options, which may be granted to an employee during any calendar year under the 2006 Plan, is 500,000. The term of these non-transferable stock options may not exceed ten years. The exercise price of these stock options may not be less than 100% (110% if the person granted such options owns more than ten percent of the outstanding common stock) of the fair value of one share of common stock on the date of grant. On January 23, 2006, the Company granted employees options to purchase an aggregate of 1,335,000 shares of common stock with an exercise price of \$0.18 per share under the 2006 Plan, for a total value of approximately \$57,000, subject to shareholder approval at the Company's next shareholder meeting. On November 8, 2006, at the 2006 Annual Meeting of Stockholders of the Company, the Company's stockholders approved the 2006 Stock Incentive Plan. As of September 30, 2006, these 1,335,000 options were the only options outstanding under the 2006 Plan, and they were not exercisable.

On January 23, 2006, the Company granted employees options to purchase an aggregate of 1,335,000 shares of common stock with an exercise price of \$0.18 per share for a total value of approximately \$57,000 under a previously approved option plan. None of these option grants were exercisable as of September 30, 2006.

On January 23, 2006, the Company granted board members immediately exercisable options to purchase an aggregate of 9,000 shares of common stock, for two board meetings held on January 11, 2006 and January 23, 2006, with an exercise price of \$0.18 for a total value of \$804 under a previously approved option plan. All of these option grants were exercisable as of September 30, 2006.

On February 14, 2006, the Company granted board members immediately exercisable options to purchase an aggregate of 4,500 shares of common stock with an exercise price of \$0.20 for a total value of \$803 under a previously approved option plan. All of these option grants were exercisable as of September 30, 2006.

On March 15, 2006, the Company granted board members immediately exercisable options to purchase an aggregate of 4,500 shares of common stock with an exercise price of \$0.18 for a total value of \$803 under a previously approved option plan. All of these option grants were exercisable as of September 30, 2006.

On May 10, 2006, the Company granted board members immediately exercisable options to purchase an aggregate of 4,500 shares of common stock with an exercise price of \$0.21 for a total value of \$931 under a previously approved option plan. All of these option grants were exercisable as of September 30, 2006.

On June 30, 2006, the Company granted a non-employee director immediately exercisable options to purchase 50,000 shares of common stock with an exercise price of \$0.11 per share for a total value of \$5,428 under a previously approved option plan.

On August 8, 2006, the Company granted board members immediately exercisable options to purchase an aggregate of 4,500 shares of common stock with an exercise price of \$0.12 for a total value of \$934 under a previously approved option plan. All of these option grants were exercisable as of September 30, 2006.



On August 8, 2006, the Company granted an employee options to purchase an aggregate of 30,000 shares of common stock with an exercise price of \$0.12 for a total value of \$3,428 under a previously approved option plan. None of these option grants were exercisable as of September 30, 2006.

#### **NOTE 7 SALES CONCENTRATIONS**

Historically, the Company has been dependent on several large customers each year, but they are not necessarily the same every year. For the three months ended September 30, 2006, the Company's most significant customers (stated as an approximate percentage of revenue) were Qwest 21%, Sprint 20%, Avaya 15%, and, with outstanding accounts receivables of \$109,473, \$0 and \$110,438, respectively, compared to the three months ended September 30, 2005, Avaya 26%, and Verizon 23% were the Company's most significant customers, with outstanding accounts receivables of \$281,632 and \$256,892, respectively. In general, the Company cannot predict with certainty, which large customers will continue to order.

The loss of any of these customers or a significant decline in sales volumes from any of these customers could have a material adverse effect on the Company's financial position, results of operations and cash flows.

#### **NOTE 8 COMMITMENTS**

The Company extended a lease on May 11, 2006 for approximately 7,000 square feet for its principal executive offices at 120 Corporate Blvd., South Plainfield, New Jersey for an additional 5 years. The agreement provides for an escalating base rent of \$4,665 per month effective August 2006 through July 2007, \$4,815 per month effective August 2007 through July 2008, and an additional increase of \$145 every August thereafter through August 2010. The tenant has the option to terminate the Lease effective July 31, 2009 with six months written notice to the Landlord.

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

### Cautionary Statement Under The Private Securities Litigation Reform Act of 1995

A number of statements contained in this report are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties that could cause actual results to differ materially from those expressed or implied in the applicable statements. You can identify forward-looking statements by our use of words such as may, will, should, could, expects, plans, intends, anticipates, believes, potential, or continue or the negative or other variations of these words, or other comparable words or phrases. These statements include, but are not limited to, statements regarding the Company's ability to gain further market recognition and the Company's cost reduction efforts. These risks and uncertainties include, but are not limited to, uncertainty as to the acceptance of the Company's products; risks related to technological factors; potential manufacturing difficulties; uncertainty of product development; uncertainty of obtaining or maintaining adequate financing; dependence on third parties; dependence on key personnel and changes in the Company's sales force and management; the risks associated with the expansion of the Company's sales channels; competition; a limited customer base; risk of system failure, security risks and liability risks; risk of requirements to comply with government regulations; vulnerability to rapid industry change and technological obsolescence; and general economic conditions. Unless otherwise required by applicable law, the Company assumes no obligation to update any such forward-looking statements, or to update the reasons why actual results could differ from those projected in the forward-looking statements.

### OVERVIEW

Historically, a significant portion of our revenues in each quarter and year has been derived from sales to relatively few customers, and we expect this trend to continue. We do not have purchase contracts with any of our customers that obligate them to continue to purchase our products, and they could cease purchasing products from us at any time. A delay in purchase or cancellation by any of our customers could cause quarterly revenues to vary significantly. In addition, during a given quarter, a significant portion of our revenues may be derived from the sale of a relatively small number of systems. Accordingly, a small change in the number of systems we sell may also cause significant changes in our operating results. Because fluctuations in the timing of orders from our customers or in the number of individual systems we sell could cause our revenues to fluctuate significantly in any given quarter or year, we do not believe that period-to-period comparisons of our financial results are necessarily meaningful, and they should not be relied upon as an indication of our future performance.

Prior to January 1, 2006 the Company accounted for stock-based compensation under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25 ( APB 25 ). Accordingly, the Company generally recognized compensation expense only when it granted options with a discounted exercise price. Any resulting compensation expense was recognized ratably over the associated service period, which was generally the option vesting term. Prior to January 1, 2006, the Company provided pro-forma disclosure amounts in accordance with FAS No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure" ("FAS 148"), as if the fair value method defined by FAS No. 123, Accounting for Stock-Based Compensation ( FAS 123 ), had been applied to its stock-based compensation.

Effective January 1, 2006 the Company adopted the fair value recognition provisions of Share Based Payment ( FAS 123R ), using the modified prospective transition method and therefore has not restated prior periods' results. Under this transition method, stock-based compensation expense for the first quarter of fiscal 2006 included compensation expense for stock-based compensation awards granted prior to, but not yet fully vested as of January 1, 2006 based on the grant date fair value estimated in accordance with the original provisions of FAS 123. Stock-based compensation expense for all share-based payment awards granted after January 1, 2006 is based on the grant-date fair



value estimated in accordance with the provisions of FAS 123R. The Company recognizes these compensation costs over the requisite service period of the award, which is generally the option vesting term.

The impact to the Condensed Consolidated Financial Statements for the three and nine months ended September 30, 2006 on net loss was \$49,615 and \$151,556, respectively, greater than if the Company had continued to account for stock-based compensation under APB 25. There is no impact on both basic and diluted net loss per share for the three and nine months ended September 30, 2006. As of September 30, 2006, the unvested options totaled \$195,337 of which \$105,283 is for options granted prior to January 1, 2006 and \$90,054 is for options granted after January 1, 2006.

## **RESULTS OF OPERATIONS**

*For the three months ended September 30, 2006 compared to the same period in 2005:*

Net sales for the three months ended September 30, 2006, were \$872,945 compared to net sales of \$1,158,928 for the same period in 2005, a decrease of \$285,983 or 24.7%. Revenues for the third quarter of 2006 declined compared to the same period last year for hardware and accessories from \$913,318 to \$743,738 or a difference of \$169,580, in addition high margin products such as software, professional services, maintenance and repairs declined by \$99,452 from \$210,594 to \$111,142.

Cost of sales for the three months ended September 30, 2006 \$395,726 was compared to \$330,062 for the same period in 2005. Cost of sales as a percentage of net sales for the three months ended September 30, 2006 increased to 45.3% from 28.5% for the same period in 2005. Gross margins decreased to 54.7% from 71.5% in the quarter ending September 30, 2006 compared to the same period last year. The 16.8% gross margin reduction was the result of three primary factors 1) decline in net sales for higher margin software,

professional services, maintenance and repairs, 2) lower prices for hardware and accessories due to a shift from prior generation hardware products to the new 5600 product line, 3) sharp increase in the charge for capitalized software amortization expenses to \$69,916 during the three months ended September 30, 2006 compared to \$27,461 for the same period in 2005.

Research and development expenses for the three month period ended September 30, 2006 \$173,651 were compared to \$120,199 for the same period in 2005 or an increase of \$53,452. The increase is primarily due to professional services for the three months ended September 30, 2006 of \$62,031 compared to \$24,994, an increase of \$37,037, from the same period in 2005. In addition non-cash stock based compensation was \$17,007 compared to zero in 2005.

Selling, general and administrative expenses ("SG&A") for the three months ended September 30, 2006 were \$603,522 compared to \$672,851 for the same period in 2005, an decrease of \$69,329. The decrease in SG&A expenses was due primarily to decreased payroll related expenses for salaries, benefits and incentive compensation of \$89,079, decreased marketing expenses of \$11,265 offset in part by increased charges for non-cash stock based compensation expenses of \$30,649.

Depreciation expense was \$3,820 for the three months ended September 30, 2006 compared to \$2,158 in the same period in 2005. The increase was due to an increase of depreciable fixed assets in the three months ended September 30, 2006 as compared to the same period in 2005.

Net loss for the three months ended September 30, 2006 amounted to \$312,877 compared to net income of \$28,536 for the same period in 2005. The decrease in net income of \$341,413 was due primarily to the combined impact of lower net sales of \$285,983 and higher cost of goods of \$65,664 resulting in reduced gross margins of \$351,647.

*For the nine months ended September 30, 2006 compared to the same period in 2005:*

Net sales for the nine months ended September 30, 2006, \$2,617,356 were compared to net sales of \$3,141,509 for the same period in 2005, a decrease of \$524,153 or 16.7%. Revenues for the nine months ended September 30, 2006 declined compared to the same period last year for hardware and accessories from \$2,328,434 to \$2,035,643 or a difference of \$292,791, in addition high margin products such as software, professional services, maintenance and repairs declined by \$229,766 from \$818,664 to \$588,898.

Cost of sales for the nine months September 30, 2006 was \$1,069,242 compared to \$959,928 for the same period in 2005. Cost of sales as a percentage of net sales for the nine months ended September 30, 2006 increased to 40.9% from 30.6% for the same period in 2005. The 10.3% reduction in gross margin to 59.1% from 69.4% for the nine

month period ended September 30, 2006 and 2005, respectively, was primarily related to increased amortization expense for capitalized software costs of \$74,737 resulting in approximately a 3.5% gross margin decline, reduced prices of approximately 4.0% and 1.9% negative comparative impact due to reductions in inventory reserve favorable adjustments in the prior year totaling \$46,389 compared to unfavorable inventory reserve adjustments totaling \$10,682.

Research and development expenses for the nine months ended September 30, 2006 was \$478,057 compared to \$397,198 for the same period in 2005 or a increase of \$80,859. The increase is primarily due to professional services for the nine months ended September 30, 2006 of \$114,138 compared to \$68,719, an increase of \$45,419, from the same period in 2005 offset in part by increased capitalized software of \$8,344. In addition non-cash stock based compensation was \$51,398 compared to zero in 2005.

Selling, general and administrative expenses ("SG&A") for the nine months ended September 30, 2006 were \$1,923,111 compared to \$1,998,213 for the same period in 2005, a decrease of \$75,102. The decrease in SG&A expenses was due primarily to decreased payroll related expenses of \$123,587, decreased marketing expenses of \$52,880 and reduced travel related expenses of \$16,206 offset in part by non-cash stock based compensation expenses of \$94,084 and professional services of \$32,822.

Restructuring and other credits for the nine months ended September 30, 2006 amounted to a \$81,000 benefit compared to zero for the same period in 2005. The Company released \$60,000 of professional services and \$21,000 of shareholder relation related expenses, from disputed accruals during the nine months ended September 30, 2006.

Depreciation expense was \$11,690 for the nine months ended September 30, 2006 compared to \$7,070 in the same period in 2005. The increase was due to the acquisition of depreciable assets in the nine months ended September 30, 2006 as compared to the same period in 2005.

Net loss for the nine months ended September 30, 2006 increased to \$818,045 from \$216,251 for the same period in 2005. The increase in net loss of \$601,794 was due primarily to the combined impact of lower net sales of \$524,153 and higher cost of goods of \$109,314 resulting in reduced gross margins of \$633,467. The net improvement of total operating expenses of \$70,623 was offset in part by increased interest and other expenses of \$39,209.

## **FINANCIAL CONDITION AND CAPITAL RESOURCES**

The Company's working capital balance as of September 30, 2006 was \$280,361 compared to \$679,515 at December 31, 2005. The decrease of \$399,154 was due primarily to a smaller reduction in current liabilities of \$305,395 mainly made up of accounts payable of \$199,726, accrued expenses of \$95,971 and payroll related liabilities of \$200,067 offset by an increase in the revolving credit line of \$200,000 than the reduction in current assets of \$704,549 mainly made up of cash and cash equivalents of \$134,954, net accounts receivable of \$596,573 offset by an increase in net inventory of \$72,803.

The Company failed to comply with certain financial covenants in the Revolving Credit Facility, as of March 31, 2006. On June 20, 2006, the Company received a waiver for its financial covenant default for March 31, 2006 and revision to the loan agreement to adjust GAAP earnings/losses for the impact of non-cash stock based compensation items for the purpose of calculating the net profit after tax covenant requirement.

The Company failed to comply with certain financial covenants in the Revolving Credit Facility, as of September 30, 2006. This default can result in the Company not being permitted to borrow under the Revolving Credit Facility in the future. The Company's ability to continue operations will be materially adversely affected if it is unable to borrow under the Revolving Credit Facility and it is unable to replace the Revolving Credit Facility with another credit facility having satisfactory financial and other terms. The Company has not yet received a waiver on its September 30, 2006 financial covenant default. However, the Company is currently in the process of seeking a waiver on this default, although there is no assurance that one will be obtained. As of September 30, 2006, the outstanding balance on the revolving credit facility was \$200,000.

The Company has historically received proceeds from the sale of its New Jersey Net Operating Losses during the fourth quarter of previous years. While no assurance can be made that the Company will again receive such proceeds, the Company has been approved for this program in 2006 and expects to use the proceeds received under this program for general working capital purposes.

On April 27, 2006 the Company received gross proceeds of \$498,882 from the exercise of 3,325,882 warrants.

Net cash used in operating activities during the nine months ended September 30, 2006 was \$394,188 compared to \$612,638 in the same period in 2005, a difference of \$218,450. Improved cash amounts provided by collection of accounts receivable and deferred income of \$914,611 and \$37,976, respectively, and the non-cash stock based compensation of \$151,556, offset by the increased net loss of \$601,794, and reductions to both accounts payable of \$121,091 and accrued payroll and related liabilities of \$236,510.

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Net cash used in investing activities during the nine months ended September 30, 2006 was \$399,464 compared to net cash used during the same period in 2005 of \$468,813. Capitalized software expenditures for the nine months ended September 30, 2006 was \$383,898, a decrease of \$74,229 from \$458,127 for the same period in 2005.

Net cash provided by financing activities during the nine months ended September 30, 2006 was \$658,698 compared to \$844,416 during the nine months ended September 30, 2005. This \$185,718 decrease was due primarily to the Company realizing \$202,940 less in net proceeds from the sale of common stock and exercise of warrants.

### **ITEM 3. CONTROLS AND PROCEDURES**

Prior to the filing of this report, the Company's management carried out an evaluation, under the supervision and with the participation of its Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's controls and procedures were effective as of the end of the period covered by this report to ensure that information required to be disclosed by the Company in the reports filed by it under the Securities and Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and include controls and procedures designed to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer of the Company, as appropriate to allow timely decisions regarding required disclosure.

The Company's chief executive officer and chief financial officer have also concluded that there has been no change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected or is reasonably likely to materially affect the Company's internal control over financial reporting.

**PART II. OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

The Company is not currently involved in any legal proceedings other than routine litigation incidental to the business.

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

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**ITEM 5. OTHER INFORMATION**

None.





**ITEM 6. EXHIBITS**

- 31.1 \* Certification of Chief Executive Officer pursuant to Securities Exchange Act Rule 13a-14(a)
- 31.2 \* Certification of Chief Financial Officer pursuant to Securities Exchange Act Rule 13a-14(a)
- 32 \* Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, of Chief Executive Officer and Chief Financial Officer

\* Filed herewith

**SIGNATURES**

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

Date: November 13, 2006

**ION NETWORKS, INC.**

*/s/ Norman E. Corn*

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*Norman E. Corn, Chief Executive Officer*

*/s/ Patrick E. Delaney*

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*Patrick E. Delaney, Chief Financial Officer*

**Exhibit Index**

- 31.1 \* Certification of Chief Executive Officer pursuant to Securities Exchange Act Rule 13a-14(a)
- 31.2 \* Certification of Chief Financial Officer pursuant to Securities Exchange Act Rule 13a-14(a)
- 32 \* Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002, of Chief Executive Officer and Chief Financial Officer

\* Filed herewith

I, Norman E. Corn, certify that:

1.

I have reviewed this quarterly report on Form 10-QSB of ION Networks, Inc.;

2.

Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3.

Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;

4.

The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

a)

Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared.

b)

Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period

covered by this report based on such evaluation; and

c)

Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and

5.

The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):

a)

All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

b)

Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: November 13, 2006

/s/ Norman E. Corn

Norman E. Corn

Chief Executive Officer



I, Patrick E. Delaney, certify that:

1.

I have reviewed this quarterly report on Form 10-QSB of ION Networks, Inc.;

2

Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3

Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;

4

The small business issuer's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

a)

Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared.



b)

Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c)

Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and

5.

The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):

a)

All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

b)

Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: November 13, 2006

/s/ Patrick E. Delaney

Patrick E. Delaney

Chief Financial Officer



**ION Networks, Inc.**

CERTIFICATION

In connection with the periodic report of ION Networks, Inc. (the Company) on Form 10-QSB for the period ended September 30, 2006 as filed with the Securities and Exchange Commission (the Report), each of the undersigned officers of the Company, hereby certifies as of the date hereof, solely for purposes of Title 18, Chapter 63, Section 1350 of the United States Code, that to the best of their knowledge:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company at the dates and for the periods indicated.

Date: November 13, 2006

By: /s/ Norman E. Corn

Norman E. Corn

Chief Executive Officer

Date: November 13, 2006

By: /s/ Patrick E. Delaney

Patrick E. Delaney

Chief Financial Officer

