

---

**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

---

**FORM 10-Q**

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

For the quarterly period ended September 30, 2003

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

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

Commission File Number 000-21091

---

**FIRST AVENUE NETWORKS, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction  
of incorporation or organization)

**52-1869023**  
(I.R.S. Employer  
Identification No.)

**230 Court Square, Suite 202, Charlottesville, VA 22902**  
(Address of principal executive offices)

**(434) 220-4988**  
(Registrant's telephone number, including area code)

---

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes  No .

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by the court: Yes  No .

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Securities Exchange Act of 1934): Yes  No .

Indicate the number of shares outstanding of each of the registrant's classes of common stock as of the latest practicable date: Pursuant to its plan of reorganization, the registrant has 20,000,000 shares of its common stock outstanding as of October 10, 2003. As of such date, 18,512,064 shares have been distributed pursuant to the plan of reorganization.

---

---

[Table of Contents](#)

**FIRST AVENUE NETWORKS, INC.**

**INDEX**

	<b>Page</b>
PART I. FINANCIAL INFORMATION	
Item 1. <a href="#">Financial Statements</a>	3
Item 2. <a href="#">Management's Discussion and Analysis of Financial Condition and Results of Operations</a>	8
Item 3. <a href="#">Quantitative and Qualitative Disclosures about Market Risk</a>	13
Item 4. <a href="#">Controls and Procedures</a>	13
PART II. OTHER INFORMATION	
Item 6. <a href="#">Exhibits and Reports on Form 8-K</a>	14
<a href="#">Signatures</a>	15
<a href="#">Exhibit Index</a>	16

[Table of Contents](#)

**ITEM 1. Financial Statements**

**FIRST AVENUE NETWORKS, INC. AND SUBSIDIARIES**

**Consolidated Balance Sheets**

**(unaudited)**

**(in thousands, except share data)**

	September 30, 2003		December 31, 2002
Current assets:			
Cash and cash equivalents \$	4,066	\$	5,300
Accounts receivable, net	39		35
Prepaid expenses and other current assets	41		97
Inventory	357		368
Total current assets	4,503		5,800
Property and equipment, net	18		25
FCC licenses	21,600		21,600
Other assets	4		4
Total assets	\$ 26,125	\$	27,429

<b>Current liabilities:</b>			
Accounts payable	\$	54	\$ 718
Accrued compensation and benefits		192	255
Accrued taxes other than income taxes, current portion		350	350
Other accrued liabilities		307	464
<hr/>			
Total current liabilities		903	1,787
Senior secured notes, net		10,200	8,756
Accrued taxes other than income taxes, less current portion		3,760	3,760
<hr/>			
Total liabilities		14,863	14,303
<hr/>			
<b>Commitments and contingencies (Note 3)</b>			
<b>Stockholders' equity:</b>			
Common stock, \$0.001 par value; 50,000,000 shares authorized, 20,000,000 shares issued and outstanding		20	20
Additional paid-in capital		40,936	40,831
Accumulated deficit		(29,694)	(27,725)
<hr/>			
Total stockholders' equity		11,262	13,126
<hr/>			
Total liabilities and stockholders' equity	\$	26,125	\$ 27,429
<hr/>			

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

[Table of Contents](#)

**FIRST AVENUE NETWORKS, INC. AND SUBSIDIARIES**  
**Consolidated Statements of Operations**  
**(unaudited)**  
**(in thousands, except per share data)**

Three Months Ended  
September 30,

Nine Months Ended  
September 30,

2003	2002	2003	2002
------	------	------	------

Costs	\$	33	\$	72	\$	123	\$
-------	----	----	----	----	----	-----	----

Costs:

Technical and network operations		1		3		3	
Leases and marketing		98		44		198	
General and administrative		349		365		938	
Depreciation and amortization		3		2		7	

Total costs and expenses		451		414		1,146	
--------------------------	--	-----	--	-----	--	-------	--

Provisions		(418)		(342)		(1,023)	
------------	--	-------	--	-------	--	---------	--

Interest expense		(487)		(557)		(1,443)	
Interest income		12		25		38	
Other		23		70		459	

Total interest and other		(452)		(462)		(946)	
--------------------------	--	-------	--	-------	--	-------	--

	\$	(870)	\$	(804)	\$	(1,969)	\$
--	----	-------	----	-------	----	---------	----

Weighted average diluted loss per non share							
Net loss \$		(0.04)		(0.04)		(0.10)	

Weighted average		20,000		20,000		20,000	
------------------	--	--------	--	--------	--	--------	--

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

[Table of Contents](#)

**FIRST AVENUE NETWORKS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Cash Flows**  
**(unaudited)**  
**(in thousands)**

	Nine Months Ended September 30,	
	2003	2002
<b>Cash flows from operating activities:</b>		
Net loss	\$ (1,969)	\$ (2,855)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	7	17
Gain on sale of assets held for resale	—	(153)
Stock-based compensation expense	106	—
Non-cash income	—	(10)
Non-cash interest expense	1,443	1,686
Changes in operating assets and liabilities	(821)	(176)
Net cash used in operating activities	(1,234)	(1,491)
<b>Cash flows from investing activities:</b>		
Proceeds from assets held for sale	—	964
Purchases of property and equipment	—	(21)
Net cash	—	943

	provided by investing activities		
Net decrease in cash and cash equivalents		(1,234)	(548)
Cash and cash equivalents, beginning of period		5,300	5,850
Cash and cash equivalents, end of period	\$	4,066	\$ 5,302
<b>Supplemental Disclosure of Cash Flow Information:</b>			
Non-cash financing and investing activities:			
Issuance of senior secured notes for paid-in-kind interest	\$	830	\$ 790

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

[Table of Contents](#)

**First Avenue Networks, Inc. and Subsidiaries  
Notes to Consolidated Financial Statements**

**Note 1—The Company and Basis of Presentation**

First Avenue Networks, Inc. (collectively with its subsidiaries, the “Company”) owns over 750 wireless telecommunication licenses granted by the Federal Communications Commission (“FCC”) that provide coverage of substantially all of the continental United States with 39 GHz spectrum. This license portfolio represents over 980 million channel pops, calculated as number of channels in a given area multiplied by the population covered by these channels.

The Company was previously known as Advanced Radio Telecom Corp. (“ART”). In February 2002, the shareholders approved amendments to the Certificate of Incorporation to change the Company’s name to First Avenue Networks, Inc. ART, with its subsidiaries, filed a voluntary petition with the United States Bankruptcy Court for the District of Delaware (the “Bankruptcy Court”) for protection under Chapter 11 of Title 11 of the United States Code (the “Bankruptcy Code”) on April 20, 2001 (the “Petition Date”).

On October 31, 2001, the Bankruptcy Court approved the Company’s Plan of Reorganization filed with the Bankruptcy Court on September 27, 2001 (the “Plan”). On December 20, 2001 (the “Effective Date”), the Company met all of the Conditions Precedent to the Effective Date (as defined), the Plan was effective and the Company emerged from proceedings under Chapter 11 of the Bankruptcy Code. For financial reporting purposes, the Company reflected its emergence from bankruptcy as of the close of business on December 31, 2001.

The Company is subject to all of the risks inherent in an early-stage business in the telecommunication industry. These risks include, but are not limited to: limited operating history;

management of a changing business; reliance on other third parties; competitive nature of the industry; development and maintenance of efficient technologies to support the business; employee turnover; and, operating cash requirements. Management expects operating losses and negative cash flows to continue for the foreseeable future. Failure to generate sufficient revenues could have a material adverse effect on the Company's results of operations, financial condition and cash flows. The recoverability of assets is highly dependent on the ability of management to execute its business plan.

*Interim financial statements* – Certain information and footnote disclosures normally included in financial statements have been condensed or omitted pursuant to rules and regulations of the Securities and Exchange Commission. The accompanying interim condensed consolidated financial statements are unaudited. In the opinion of Company management, these financial statements include all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the Company's financial position and results of operations for the interim periods presented. The unaudited condensed consolidated financial statements should be read in conjunction with the Company's 2002 audited consolidated financial statements and notes thereto contained in the Company's 2002 Annual Report on Form 10-K.

*Use of estimates* – Preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements. Actual results could differ from those estimates. The more significant estimates made by management include fair values of assets and liabilities, accrued property and use taxes and realization of deferred tax assets.

*FCC licenses* – FCC licenses are granted for initial ten-year terms with renewal dates ranging from 2006 to 2011. Under the provisions of Statement of Financial Accounting Standards No. 142 "Goodwill and Other Intangible Assets" ("SFAS No. 142"), FCC licenses are deemed to have an indefinite useful life and are not amortized.

*Impairment of long-lived assets* – The Company evaluates its long-lived assets for impairment and continues to evaluate them as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. In cases where undiscounted expected cash flows associated with such assets are less than their carrying value, an impairment provision is recognized in an amount by which the carrying value exceeds the estimated fair value of such assets. Recoverability of the carrying value of FCC licenses is dependent on successful deployment of networks and radio links or sales of such assets to a third party. The Company considers the FCC licenses to have an indefinite useful life under the provisions of SFAS No. 142. The Company performs an annual impairment test on this asset. If events and circumstances indicate the assets might be impaired, the Company will perform such a test on an interim basis. The impairment test compares the fair value of the FCC licenses with the carrying value of the asset. If the fair value is less than the carrying values, an impairment loss will be recorded.

*Net loss per share* – Calculation of loss per share for the three months and nine months ended September 30, 2003 and 2002 excludes the effect of warrants and options to purchase 4.0 million and 1.4 million, respectively, shares of common stock since inclusion in such calculation would have been antidilutive.

---

## [Table of Contents](#)

*Stock options* – The Company applies Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations, including Financial Accounting Standards Board Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation", for its stock-based compensation plan. Accordingly, compensation cost for stock options granted to employees and directors is measured on the date of grant to the extent the current market price of the underlying stock exceeds the exercise price. The Company accounts for equity stock options granted to non-employees at fair value.

In September 2003, the Company canceled 940,000 options to purchase common stock at a strike price of \$3.96 which represented all of its outstanding options. The Company replaced these options with 1,388,717 options to purchase common stock at a strike price of \$0.14. Of these options, 277,743 have immediately vested. These options will be accounted for on a variable basis. The remainder vest on a pro rata basis on December 20, 2003 and annually thereafter through December 20, 2006. As a result of this variable method of accounting, the Company has recorded a non-cash compensation charge of \$106,000 during the three months ended September 30, 2003.

The following table summarizes relevant information as to reported results under the Company's intrinsic value method of accounting for stock awards, with supplemental information as if the fair value recognition provisions of SFAS No. 123, "Accounting for Stock Based Compensation," (SFAS 123) as amended by SFAS 148, "Accounting for Stock-Based Compensation – Transition and Disclosure," (SFAS 148) had been applied (in thousands, except per share data):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2003	2002	2003	2002
Loss, as reported	\$ (870)	\$ (804)	\$ (1,969)	\$ (2,000)
Stock based compensation expense included				
Reported loss	106	—	106	—
Stock based compensation expense determined under fair value method for all awards	(53)	—	(53)	—
Loss, as adjusted for fair value method for all stock based awards	\$ (817)	\$ (804)	\$ (1,916)	\$ (2,000)
and diluted earnings per share, as reported	\$ (0.04)	\$ (0.04)	\$ (0.10)	\$ (0.10)

---

## **Note 2—Related Party Transactions**

Holders of approximately 59% of the Company's common stock own approximately 93% of the outstanding senior notes and Class A Warrants. Representatives from two entities holding approximately 45% of the Company's common stock serve on the Company's Board of Directors.

## **Note 3—Commitments and Contingencies**

*Contingencies* – The Company is subject to certain claims and assessments and makes routine filings with the FCC and state regulatory authorities. Management believes that resolution of any such claims or matters arising from such filings, if any, will not have a material adverse impact on the Company's consolidated financial position or results of operations.

## **[Table of Contents](#)**

### **ITEM 2. *MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS***

***Cautionary Statement***—This report includes “forward-looking” information, as that term is defined in the Private Securities Litigation Reform Act of 1995 or by the Securities and Exchange Commission in its rules, regulations and releases, regarding, among other things, our financial and business prospects, the deployment of our services, capital requirements and financing prospects. The Company cautions investors that any such statements are based on currently available operational, financial and competitive information, and are subject to various risks and uncertainties. Actual future results and trends may differ materially depending on a variety of factors. Those factors include, among others, those matters disclosed as Risk Factors at the end of the business section of the Company's most recently filed Annual Report on Form 10-K.

#### ***Overview***

The Company holds over 750 licenses granted by the Federal Communications Commission (“FCC”) and provides wireless, high-speed, point-to-point telecommunications services to 13 customer links. The Company engineered these telecommunication links, purchased and installed radios and tested the links for proper operation and reliability. Its customers incorporate these fixed wireless transmission links into their telecommunication networks and utilize wireless links to provide a primary telecommunication link or, in other cases, redundancy, back up or diversity to other telecommunication services.

The Company's recoverability of its investment in FCC licenses is dependent on its successful execution of its business plan.

The Company's strategy is to utilize its FCC licenses to provide telecommunications services in a capital efficient manner. In the short-term, the Company will seek to identify, contact and serve existing telecommunications carriers in a manner that does not require significant sales and marketing, operating and capital expenditures. Its long-term objective is to develop its business plan in response to carrier, business and other end-user customer demands for wireless, high-speed services.

From its inception in 1993 through the first quarter of 2001, the Company acquired airwave capacity, or spectrum rights, through FCC auctions and purchase transactions, raised capital through public and private offerings of securities, acquired equipment and roof rights, and developed operating and support systems and networks. In 1998, it began to sell a variety of Internet services to end-users in Seattle, WA,

Portland, OR, and Phoenix, AZ. In late 1999, the Company's strategy evolved to providing high-speed transmission services, including Internet access to businesses. During 2000, it launched these services in ten markets. In the first quarter of 2001, the Company was unable to secure additional funding sources to continue to finance operations and service debt.

### ***Reorganization***

The Company sought reorganization under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware ("Court") on April 20, 2001 (the "Petition Date"). It terminated nearly all of its employees, terminated operation of its networks and eliminated customer support. A Joint Plan of Reorganization ("Plan") was developed and was approved by the Court on October 31, 2001. On December 20, 2001 ("Effective Date"), the Plan was effective and the Company emerged from the proceedings under Chapter 11 of the United States Bankruptcy Code pursuant to the terms of the Plan.

Under the Plan, the Company issued 20 million shares of new post-Chapter 11 common stock ("New Common Stock") to unsecured creditors and holders of Series A Preferred Stock ("Old Preferred Stock"). Each holder of an unsecured claim received its pro rata share of 19 million shares of New Common Stock. Each holder of Old Preferred Stock received its pro rata share of 1 million shares of New Common Stock. Holders of pre-chapter 11 common stock ("Old Common Stock") and holders of any other equity interest received no distributions under the Plan. All Old Common Stock, Old Preferred Stock and all other equity interests such as employee stock options and warrants were cancelled on the Effective Date. As of October 10, 2003, the Company has distributed 18,512,064 shares to unsecured creditors and holders of Old Preferred Stock. The remaining 1,487,703 shares will be distributed in November 2003. (See *Liquidity and Capital Resources* for further discussion.)

Prior to the Company's reorganization, it incurred significant operating costs and interest expense. While pursuing its short-term strategy, the Company expects significantly less costs in these areas. The Company also expects its general and administrative and sales and marketing costs to be less than those incurred prior to its reorganization.

### ***Results of Operations***

#### ***Nine months ended September 30, 2003 compared to nine months ended September 30, 2002***

Revenues for the nine months ended September 30, 2003 decreased 44% to \$123,000 from \$221,000 for the nine months ended September 30, 2002 as a result of the number of dedicated wireless links decreasing from 21 at September 30, 2002 to 13 at September 30, 2003.

### **Table of Contents**

Technical and network operations costs and expenses are comprised primarily of roof-top rent and backhaul. Technical and network operations costs and expenses decreased to \$3,000 for the nine months ended September 30, 2003, compared to \$28,000 for the nine months ended September 30, 2002. This decrease resulted from the decrease in the number of facilities rented to provide service to 13 dedicated links. Technical and network operations costs and expenses were 2% and 13% of revenues for the nine months ended September 30, 2003 and 2002, respectively.

Sales and marketing costs and expenses are comprised primarily of compensation and related costs. These costs increased 25% to \$198,000 for the nine months ended September 30, 2003, compared to \$159,000 for the nine months ended September 30, 2002. This increase was due to increased public relation expenses and a non-cash stock-based compensation charge not incurred in the nine months ended September 30, 2002. Sales and marketing costs and expenses were 161% and 72% of revenues for the nine months ended September 30, 2003 and 2002, respectively.

General and administrative costs and expenses decreased 39% to \$938,000 for the nine months ended September 30, 2003 from \$1.5 million for the nine months ended September 30, 2002. This decrease resulted from the absence of expenses in the nine months ended September 30, 2003 that were incurred during the nine months ended September 30, 2002 to finalize the bankruptcy process. During the nine months ended September 30, 2002, the Company employed three of the predecessor company's employees to finalize bankruptcy matters. Additionally, the Company incurred significant legal fees as a result of finalizing the bankruptcy process. General and administrative costs and expenses for the nine months ended September 30, 2003 primarily consist of compensation, occupancy expenses, professional fees and insurance. General and administrative costs and expenses were 763% and 696% of revenues for the nine months ended September 30, 2003 and 2002, respectively.

Depreciation and amortization expense of \$7,000 for the nine months ended September 30, 2003 decreased 59% from \$17,000 for the nine months ended September 30, 2002. This decrease was due to the closure of the predecessor's Kent, WA facility and sale of assets in the nine months ended September 30, 2002. Depreciation and amortization expense was 6% and 8% of revenues for the nine months ended September 30, 2003 and 2002, respectively.

Interest and other expenses decreased to \$946,000 for the nine months ended September 30, 2003 from \$1.3 million for the nine months ended September 30, 2002. This change primarily is attributable to (i) a \$243,000 decrease in interest expense as a result of the Company ceasing in 2003 to record interest on pre-petition amounts due to various state and local governments for use and personal property taxes reported as other non-current liabilities and (ii) \$377,000 in other income recorded during the nine months ended September 30, 2003 as a result of settling disputed bankruptcy claims for amounts less than the recorded liability.

During the nine months ended September 30, 2003, the Company increased its deferred tax valuation allowance to equal the increase in its deferred tax asset based upon management's determination that the recognition criteria for realization had not been met.

#### ***Three months ended September 30, 2003 compared to three months ended September 30, 2002***

Revenues for the three months ended September 30, 2003, decreased 54% to \$33,000 from \$72,000 for the three months ended September 30, 2002 as a result of the number of dedicated wireless links decreasing from 21 at September 30, 2002 to 13 at September 30, 2003.

Technical and network operations costs and expenses are comprised primarily of roof-top rent and backhaul. Technical and network operations costs and expenses decreased 67% to \$1,000 for the three months ended September 30, 2003, compared to \$3,000 for the three months ended September 30, 2002. This reduction resulted from the decrease in the number of facilities rented to provide service to 13 dedicated links. Technical and network operations costs and expenses were 3% and 4% of revenues for the three months ended September 30, 2003 and 2002, respectively.

Sales and marketing costs and expenses are comprised primarily of compensation and related costs. These costs increased 123% to \$98,000 for the three months ended September 30, 2003, compared to \$44,000 for the three months ended September 30, 2002. This increase was due to increased public relation expenses and a non-cash stock-based compensation charge recorded during the three months ended September 30, 2003 not incurred in the three months ended September 30, 2002. Sales and marketing costs and expenses were 297% and 61% of revenues for the three months ended September 30, 2003 and 2002, respectively.

General and administrative costs and expenses decreased 4% to \$349,000 for the three months ended September 30, 2003 from \$365,000 for the three months ended September 30, 2002. This decrease resulted from the absence of expenses incurred in the three months ended September 30, 2002 to liquidate the Company's international subsidiaries offset by a non-cash stock-based compensation charge recorded during the three months ended September 30, 2003 not incurred in the three months ended September 30, 2002. General and administrative costs and expenses for the three months ended September 30, 2003 primarily consist of compensation, occupancy expenses, professional fees and insurance. General and

administrative costs and expenses were 1058% and 507% of revenues for the three months ended September 30, 2003 and 2002, respectively.

## Table of Contents

Depreciation and amortization expense for the three months ended September 30, 2003 increased to \$3,000 from \$2,000 for the three months ended September 30, 2002. Depreciation and amortization expense was 9% and 3% of revenues for the three months ended September 30, 2003 and 2002, respectively.

Interest and other expenses decreased to \$452,000 for the three months ended September 30, 2003 from \$462,000 for the three months ended September 30, 2002. This change is attributable to (i) a \$70,000 decrease in interest expense as a result of the Company ceasing in 2003 to record interest on pre-petition amounts due to various state and local governments for use and personal property taxes reported as other non-current liabilities and (ii) a \$47,000 decrease in other income. Other income for the three months ended September 30, 2002 included amounts realized by the Company for disposing of assets held for sale.

During the three month period ended September 30, 2003, the Company increased its deferred tax valuation allowance the increase in its equal its deferred tax asset based upon management's determination that the recognition criteria for realization had not been met.

### *Liquidity and Capital Resources*

On April 20, 2001, the Company filed a voluntary petition with the Court for protection under Chapter 11 of the Bankruptcy Code. As a result of the Chapter 11 filing, the Company was prohibited from paying, and creditors were prohibited from attempting to collect, claims or debts arising prior to the Petition Date. On October 31, 2001, the Court approved the Plan. On December 20, 2001, after the Company met all of the Conditions Precedent to the Effective Date (as defined), the Plan was effective and the Company emerged from proceedings under Chapter 11 of the Bankruptcy Code. On the Effective Date of the Plan, the Company:

- Filed an Amended and Restated Certificate of Incorporation;
- Cancelled Old Common Stock, Old Preferred Stock and agreements to issue or purchase any additional equity interests;
- Issued 19 million shares of New Common Stock to settle all unsecured creditor claims;
- Issued 1 million shares of New Common Stock to holders of Old Preferred Stock;
- In return for \$11.0 million in cash,
  - Issued \$11.0 million of five-year Senior Secured Notes that bear paid in-kind interest at 9% and are secured by substantially all of the Company's assets; and,
  - Issued 4 million fully-vested, five-year New Class A Warrants with an exercise price of \$0.01 to holders of Senior Secured Notes; and,
- Paid the holder of the \$11.3 million secured vendor financing claim \$6.0 million in cash in full satisfaction of the debt.

In February 2002, the Company verified approximately 90% of the holders of unsecured claims and 100% of the holders of Old Preferred Stock and distributed stock certificates of New Common Stock. The Company has completed the verification of the remaining holders of unsecured claims and will make the final distribution of stock certificates of New Common Stock in November 2003. The Company will not make any additional distributions to holders of Old Preferred Stock.

The Company distributed 17,512,064 and 1,000,000 shares of New Common Stock to holders of unsecured claims and holders of Old Preferred Stock, respectively, in February 2002. The Company will distribute 1,487,703 New Common Shares in November 2003 to settle the remaining unsecured claims. The remaining 1,487,703 shares will be distributed to the New Common Stock holders who previously received the stock in settlement of unsecured claims on a pro rata basis relative to their current holdings.

During the nine months ended September 30, 2003, operating activities used cash of approximately \$1.2 million as compared to \$1.5 million during the nine months ended September 30, 2002. Cash used by operating activities during the nine months ended September 30, 2003 and 2002 resulted primarily from the Company's net loss reduced by non-cash interest expense and depreciation and amortization.

During the nine months ended September 30, 2002, investing activities provided cash of \$943,000 primarily due to proceeds of \$964,000, net of selling costs, from the sale of its network and other equipment.

## **Table of Contents**

Senior Secured Notes are due on December 20, 2006 and are collateralized by all assets of the Company. They bear interest at the rate of 9% per annum that is payable quarterly through the issuance of additional Senior Secured Notes at the Company's option. Only if an event of default has occurred and is continuing is interest mandatorily payable in cash. During the nine months ended September 30, 2003, the Company issued \$830,000 of additional Senior Secured Notes for interest. The Senior Note and Class A Warrant Purchase Agreement contains covenants which limit the Company's ability to incur additional debt, pay dividends or make other distributions, incur liens, merge or sell assets and enter into certain transactions with related parties.

The Company recorded the issuance of the Senior Secured Notes net of the estimated fair value of the New Class A Warrants at the issuance date. Amortization of debt discount of \$613,000 has been determined utilizing the effective interest rate method and is a component of interest expense for the nine months ended September 30, 2003.

The Company had cash and cash equivalents of \$4.1 million at September 30, 2003. Since its inception, the Company has incurred losses from operations and expects to continue to incur losses in the foreseeable future. The Company has altered its business plan to minimize expenditures and the amount of future capital required. At September 30, 2003, it had three employees and non-cancelable financial commitments of less than \$22,000 due in 2003.

The Company believes that the cash balance at September 30, 2003 is sufficient to cover its operations and capital requirements through and including 2004.

## **Critical Accounting Matters and Significant Estimates**

The preparation of consolidated financial statements requires management to make judgments based upon estimates and assumptions that are inherently uncertain. Such judgments affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. Management continuously evaluates its estimates and assumptions, including those related to long-lived assets, inventories, income taxes, contingencies and litigation, and the carrying values of assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

A summary of our most critical accounting policies and significant estimates used in the preparation of our consolidated financial statements is as follows:

- Given the nature of the Company's 39 GHz spectrum, significant judgment is required in making an assessment as to whether the recorded carrying value of these assets exceeds the estimated fair market value. At September 30, 2003, the Company's FCC licenses had an estimated fair value of \$21.6 million. During 2002, the Company recorded a loss of \$24.8 million for the impairment of these FCC licenses as a result of its annual impairment evaluation under SFAS No. 142. In performing its impairment evaluation, the Company identified a number of factors that are considered to be indicative of the value of its FCC licenses, including (i) the decline in its public equity value; (ii) private purchases or restructurings for companies holding similar licenses; and, (iii) the decline in the public equity value of companies providing similar services or holding FCC licenses. Each of the factors was then quantified and weighted in deriving the estimated fair value. No additional impairment of the FCC license value occurred during the nine months ended September 30, 2003.

Several key assumptions were included in the valuation model: (i) the value of the FCC licenses directly correlates with the public trading value of the Company's stock and that of other public companies in the telecommunication industry; (ii) certain private purchases of similar licenses are reflective of the fair value of the underlying assets; (iii) the relative weights assigned to each factor represents the level of the factor's relevancy to the estimation of the fair value of the FCC licenses; and, (iv) the model captures relevant information impacting the fair value of these licenses. Any change in the above assumptions could lead to a different result. The Company will continue to evaluate the fair value of its FCC licenses for impairment as events or changes in circumstances indicate that the carrying value of these assets may not be fully recoverable.

The Company faces various contingencies including the renewal of its FCC licenses in 2006 to 2011 and changing FCC regulations. The loss of some or all of the FCC licenses or the imposition of FCC usage restrictions could adversely affect the Company's future business prospects and operations and result in an impairment to the carrying value of these intangible assets.

- The Company holds inventory, primarily radios, for demonstration and installation purposes and has written it down to estimated net realizable value. If actual market conditions are less favorable than those projected by management, additional write-downs may be required.

---

## [Table of Contents](#)

- On the Effective Date the Company issued \$11.0 million of New Senior Notes, with 4 million New Class A Warrants. The Company recorded the issuance of New Senior Notes and New Class A Warrants by allocating proceeds of \$11.0 million to New Senior Notes and New Class A Warrants based on their estimated relative fair values at the issuance date, resulting in \$4.1 million assigned to New Class A Warrants and \$6.9 million to New Senior Notes. The fair value of warrants was determined using the Black-Scholes option pricing model with key assumptions related to the risk free rate of return, volatility and Company stock price on the issuance date. The value ascribed to the New Class A Warrants was recorded as debt discount and an increase in additional paid-in capital of the Company. Annual amortization of debt discount is determined utilizing the effective interest rate method and is included as a component of interest expense. New Senior Notes are reported as of the balance sheet date at their face value less unamortized debt discount.
- The Company has recorded a full valuation allowance to reduce its deferred tax assets to the amount that is more likely than not to be realized. In the event the Company were to determine that it would be able to realize the deferred tax assets in the future in excess of the net recorded amount, an adjustment to the deferred tax valuation allowance would increase income in the period such determination is made.
- At September 30, 2003, other accrued taxes included accrued property tax and use tax liabilities of

approximately \$2.5 million and \$1.3 million, respectively, which were incurred prior to reorganization. Such liabilities are expected to be released as the Company reaches settlement with the respective tax jurisdictions or at such time that a basis exists for the reversal of this liability. While management believes the amounts represent reasonable estimates of the amounts potentially owed by the Company, the amounts ultimately paid to the respective jurisdictions could differ from the accrued amounts.

- In connection with its emergence from bankruptcy, the Company reflected terms of the Plan in its consolidated financial statements by adopting the fresh start accounting provisions of SOP 90-7 on December 31, 2001. Fresh start accounting creates a new reporting entity and the recorded amounts of assets and liabilities are adjusted to reflect their estimated fair values. In adopting fresh start accounting, the Company utilized the reorganization value or fair value of the entity. The reorganization value of a company is the amount of value available and to become available for the satisfaction of post-petition liabilities and allowed claims, as negotiated between the debtor-in-possession and the creditors and holders of equity interests. A committee of unsecured creditors together with the Company determined a reorganization value of approximately \$53.7 million which was deemed fair value of the assets of the reorganized business, with FCC licenses comprising 86% of the reorganization value. The Company's recoverability of its investment in FCC licenses is dependent upon its successful execution of its business plan.
- The Company is subject to all of the risks inherent in an early-stage business in the telecommunication industry. These risks include, but are not limited to: limited operating history; management of a changing business; reliance on other third parties; competitive nature of the industry; development and maintenance of efficient technologies to support the business; employee turnover; and, operating cash requirements. Management expects operating losses and negative cash flows to continue for the near term. Failure to generate sufficient revenues could have a material adverse effect on the Company's results of operations, financial condition and cash flows. The recoverability of these assets is highly dependent on the ability of management to execute on its business plan.

## [Table of Contents](#)

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company's existing long-term debt has a fixed interest rate; however, future borrowings may bear interest at variable rates and, accordingly, the Company's exposure to market risk for changes in interest rates may change in the future.

At September 30, 2003, the Company had cash and cash equivalents of \$4.1 million that were held in bank accounts and in certificates of deposits with an average interest rate of 0.95% and have an original maturity of less than three months. The Company's investment policy provides that funds in excess of current operating needs may be invested in cash equivalents, marketable securities issued by the U.S. Government, its agencies and commercial paper of domestic corporations. Its policy prohibits investing in instruments with maturities that exceed 35 days. The Company's investment priorities are to minimize short-term risk and preserve capital. The Company has had no holdings of derivative financial or commodity instruments in the past and has no current plans to do so in the future. The Company has not conducted business in foreign currencies in the past and has no current plans to do so in the future.

The Company's long-term debt has a face value of \$12.9 million and bears interest at a fixed rate of 9%. The debt is due in full in 2006.

### **ITEM 4. CONTROLS AND PROCEDURES**

Based on an evaluation of the Company's disclosure controls and procedures as of the end of the three months ended September 30, 2003, each of the chief executive officer and the chief financial officer of the Company have concluded that the Company's disclosure controls and procedures are effective in connection with the Company's filing of this quarterly report on Form 10-Q for the period ended September 30, 2003.

There were no significant changes in the Company's internal controls or in any other factors which could significantly affect those controls, subsequent to the date of the most recent evaluation of the Company's internal controls by the Company, including any corrective actions with regard to any significant deficiencies or material weaknesses.

13

---

## [Table of Contents](#)

### PART II — OTHER INFORMATION

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

(a) Exhibits:

31.1 Certification of Dean M. Johnson under Section 302 of the Sarbanes-Oxley Act.

31.2 Certification of Sandra Thomas Watson under Section 302 of the Sarbanes-Oxley Act.

32.1 Certification of Dean M. Johnson under Section 906 of the Sarbanes-Oxley Act.

32.2 Certification of Sandra Thomas Watson under Section 906 of the Sarbanes-Oxley Act.

(b) Reports on Form 8-K:

The Company did not file a Form 8-K during the quarter ended September 30, 2003.

14

---

## [Table of Contents](#)

### SIGNATURES

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

FIRST AVENUE NETWORKS, INC.

October 31, 2003  
Date

By: /s/ DEAN M. JOHNSON

---

Dean M. Johnson  
President, Chief Executive Officer and  
Director

**Pursuant to the requirements of the securities and exchange act of 1934, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated:**

Signature

Title

Date

---

/s/ DEAN M. JOHNSON	President, Chief Executive Officer and Director	October 31, 2003
<hr/>		
Dean M. Johnson		
/s/ SANDRA THOMAS WATSON	Chief Financial Officer Principal Financial and Accounting Officer	October 31, 2003
<hr/>		
Sandra Thomas Watson		

15

---

[Table of Contents](#)

**EXHIBIT INDEX**

<b>Exhibit No.</b>	<b>Title</b>
<hr/>	<hr/>
31.1	Certification of Dean M. Johnson under Section 302 of the Sarbanes-Oxley Act.
31.2	Certification of Sandra Thomas Watson under Section 302 of the Sarbanes-Oxley Act.
32.1	Certification of Dean M. Johnson under Section 906 of the Sarbanes-Oxley Act.
32.2	Certification of Sandra Thomas Watson under Section 906 of the Sarbanes-Oxley Act.

16