

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP

Form 10-Q/A

December 23, 2005

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

**FORM 10-Q/A
Amendment No. 1**

(Mark One)

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

For the quarterly period ended: June 30, 2005

OR

**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: 000-50373

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.

(Exact name of registrant as specified in its charter)

Delaware

90-0182158

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

3130 Fairview Park Drive, Suite 400,
Falls Church, Virginia

22042

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: 703-564-2967

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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). 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

As of December 23, 2005, there were 44,072,200 shares of the issuer's common stock outstanding.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
JUNE 30, 2005 QUARTERLY REPORT ON FORM 10-Q/A
EXPLANATORY NOTE

This Amendment No. 1 on Form 10-Q/A (this Amendment) amends the Quarterly report on Form 10-QSB for the quarter ended June 30, 2005 of Spectrum Sciences & Software Holdings Corp. (the Company) originally filed with the Securities and Exchange Commission on August 22, 2005. This Amendment is being filed to make the following changes to the original filing.

To correct the filing to a Form 10-Q from a 10-QSB as originally filed. This change requires certain additional information be added to our original filing, including December 31, 2004 comparative balance sheets and market risk disclosures.

To revise the foreign currency translation adjustment as a result of the amendment to the consolidated financial statements in the Quarterly Report for the quarter ended March 31, 2005 filed on December 23, 2005.

To revise the footnotes to the consolidated financial statements to summarize previously issued financial data and to include comparative financial data from prior periods.

To update Subsequent Events through the filing date.

To amend the Management's Discussion and Analysis to conform to the segments presented in our current filings and to include historical data for comparison purposes.

To add Part I, Item 3 Quantitative and Qualitative Disclosures about Market Risk.

To revise the Controls and Procedures section.

This Amendment No. 1 does not modify or update disclosures presented in the original Form 10-QSB except as set forth above. Accordingly, the Amendment No. 1 should be read in conjunction with the Company's filings made with the Securities and Exchange Commission subsequent to the original filing date of the Form 10-QSB, including any amendments to those filings.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
JUNE 30, 2005 QUARTERLY REPORT ON FORM 10-Q/A

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SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
JUNE 30, 2005 QUARTERLY REPORT ON FORM 10-Q/A
SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

The matters discussed in our Quarterly Report on Form 10-Q/A may constitute forward-looking statements within the meaning of The Private Securities Litigation Reform Act of 1995. These statements involve known and unknown risks, uncertainties, and other factors that may cause our actual results, activity levels, performance or achievements to be materially different from any future results, activity levels, performance or achievements expressed or implied by such forward-looking statements. In some cases, you can identify these statements by forward-looking words such as could expect estimate may potential will and would or similar words. You should read statements that contain such words carefully because they discuss our future expectations, contain projections of our future results of operations or of our financial position, or state other forward-looking information. We believe it is important to communicate our future expectations to our investors. However, there may be events in the future that we are not able to predict or control accurately. The factors listed in the section captioned Risk Factors , as well as any cautionary language in the Form 10-Q/A, provide examples of risks, uncertainties, and events that may cause our actual results to differ materially from the expectations we describe in our forward-looking statements.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, activity levels, performance or achievements. You should not place undue reliance on these forward-looking statements, which apply only as of the date of the Form 10-Q/A. Subsequent events and future developments may cause our views to change. However, while we may elect to update the forward-looking statements at some point in the future, we specifically disclaim any obligation to do so.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
Consolidated Balance Sheets (Unaudited)

	June 30, 2005	December 31, 2004
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 5,596,126	\$ 5,666,910
Short-term investments	1,910,262	18,795,143
Receivables	15,605,907	2,759,756
Due from Shareholder		705,126
Inventories	538,771	79,010
Prepaid expenses & other current assets	817,493	882,478
Total current assets	24,468,559	28,888,423
Property and equipment, net	7,665,972	2,280,746
Goodwill	15,088,708	
Investments in joint ventures	1,167,032	
Other assets	101,377	43,810
TOTAL ASSETS	\$ 48,491,648	\$ 31,212,979
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 6,098,174	\$ 1,025,030
Line of credit	1,017,764	
Accrued expenses	2,102,666	482,923
Current portion due to related party	118,061	705,126
Deferred revenues	322,848	228,968
Provision for contract losses		148,248
Current portion of long-term debt	379,509	
Total current liabilities	10,039,022	2,590,295
Long-term liabilities:		
Long-term debt, less current portion	2,387,259	
Due to related party, less current portion	67,388	
TOTAL LIABILITIES	\$ 12,493,669	\$ 2,590,295
Commitments and contingencies (Note 11)		
Minority interest	161,881	
Stockholders equity:		

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Preferred stock, \$0.0001 par value; 20,000,000 shares authorized, none issued

Common stock, \$0.0001 par value; 80,000,000 shares authorized, 44,072,200 and 38,969,300 issued and outstanding at June 30, 2005 and December 31, 2004

	4,407	3,897
Additional paid-in capital	79,865,695	69,895,120
Accumulated deficit	(44,079,590)	(41,277,155)
Accumulated other comprehensive income	45,586	822
 Total stockholders' equity	 35,836,098	 28,622,684
 TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	 \$ 48,491,648	 \$ 31,212,979

See accompanying notes to consolidated financial statements.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
Consolidated Statements of Operations and Comprehensive Income (Loss) (Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2005	2004	2005	2004
Revenues	\$ 11,796,428	\$ 3,418,747	\$ 14,339,038	\$ 7,015,325
Cost of revenues	10,121,076	3,054,924	12,269,211	6,329,305
Gross profit	1,675,352	363,823	2,069,827	686,020
Operating expenses	2,961,564	27,053,790	5,254,759	41,005,374
Loss from operations	(1,286,212)	(26,689,967)	(3,184,932)	(40,319,354)
Total non-operating income (expense), net	324,471	8,452	498,576	(4,499)
Loss before provision for income taxes	(961,741)	(26,681,515)	(2,686,356)	(40,323,853)
Income tax benefit	50,485	0	50,485	61,330
Loss before minority interest	(911,256)	(26,681,515)	(2,635,871)	(40,262,523)
Minority interest income(loss)	(146,483)	0	(166,564)	0
Net Loss	\$ (1,057,739)	\$ (26,681,515)	\$ (2,802,435)	\$ (40,262,523)
Weighted average common shares outstanding:				
Basic and diluted	41,774,398	36,795,363	40,388,341	27,505,843
Loss per share:				
Basic and diluted	\$ (0.03)	\$ (0.73)	\$ (0.07)	\$ (1.46)
Net Loss	\$ (1,057,739)	\$ (26,681,515)	\$ (2,802,435)	\$ (40,262,523)
Foreign currency translation adjustments	(22,789)	0	45,586	0
Unrealized gain on available for sale securities	0	13,781	0	13,781

Total comprehensive income(loss)	\$ (1,080,528)	\$ (26,667,734)	\$ (2,756,849)	\$ (40,248,742)
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See accompanying notes to consolidated financial statements.

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SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
Consolidated Statement of Stockholders Equity (Unaudited)

	Common Stock Shares	Amount	APIC	Accumulated Deficit	Accumulated Other Comprehensive Income(Loss)	Total
Balance at January 1, 2005	38,969,300	\$3,897	\$69,895,120	\$(41,277,155)	\$ 822	\$28,622,684
Stock options issued for consulting services			1,399,026			1,399,026
Exercise of stock options	2,900		4,059			4,059
Issuance of common stock for acquisition of Horne Engineering	5,100,000	510	8,567,490			8,568,000
Unrealized loss on investments					(822)	(822)
Foreign currency translation adjustments					45,586	45,586
Net loss				(2,802,435)		(2,802,435)
Balance at June 30, 2005	44,072,200	\$4,407	\$79,865,695	\$(44,079,590)	\$ 45,586	\$35,836,098

2005

Disclosure of reclassification amount:

Reclassification adjustment for losses included in net loss

\$822

See accompanying notes to the consolidated financial statements.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Six Months ended June 30,	
	2005	2004
Cash flows from operating activities		
Net loss	\$ (2,802,435)	\$ (40,262,523)
Adjustments to reconcile net loss to net cash used in operating activities		
Issuance of stock options to related party for consulting services	0	37,258,300
Investor relations expenses paid by a related party	0	2,057,500
Amortization of investment bond premium	0	8,496
Depreciation	304,638	72,083
Issuance of stock options to employees	1,399,026	125,358
Deferred income taxes	0	(28,594)
Minority interest	161,881	0
Loss on disposal of equipment	2,015	0
Realized loss on the sale of bonds	(822)	0
Changes in assets and liabilities		
Receivables	(5,450,599)	(1,170,385)
Accounts payable	3,061,566	(525,982)
Provision for contract losses	(148,248)	0
Other balance sheet changes	626,546	(206,368)
Net cash used in operating activities	(2,846,432)	(2,672,115)
Cash flows from investing activities		
Maturities (purchases) of available for sale investments, net	16,884,881	(22,538,101)
Acquisitions, net of cash received	(12,411,884)	0
Purchase of property and equipment	(2,327,281)	(109,993)
Proceeds from the sale of equipment	7,500	0
Investments in joint ventures	(88,727)	0
Net cash provided by (used in) investing activities	2,064,489	(22,648,094)
Cash flows from financing activities		
Issuance (repayment) of debt, net	1,549,567	(1,061,044)
Net (repayments) borrowings on lines of credit	(1,045,905)	0
Advances from related party	157,852	620,051
Proceeds from the exercise of stock options	4,059	31,113,685
Net cash provided by financing activities	665,573	30,672,692
Foreign exchange translation	45,586	0
Net (decrease) increase in cash and cash equivalents	(70,784)	5,352,483
Cash and cash equivalents at beginning of period	5,666,910	696,959

Cash and cash equivalents at end of period	\$ 5,596,126	\$ 6,049,442
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Non-cash acquisitions of property & equipment totaled \$2,145,755 and \$0 for the periods ended June 30, 2005 and 2004, respectively.

See accompanying notes to the consolidated financial statements.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
Notes to the Consolidated Financial Statements (Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements for the three and six month periods ended June 30, 2005 and 2004 have been prepared in accordance with United States generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission for Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all the information and footnotes required for complete financial statements. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments, consisting only of normal recurring accruals, considered necessary for a fair presentation of the Company's financial position, results of operations, and cash flows as of and for the periods presented.

The results of operations for the interim periods ended June 30, 2005 and 2004 are not necessarily indicative of the results to be expected for the full year. These interim consolidated financial statements should be read in conjunction with the December 31, 2004 consolidated financial statements and related notes included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2004, in addition to the interim financial statements, exhibits and related notes included in the Company's Form 8-Ks filed on February 1, 2005, February 25, 2005, and May 11, 2005, and any amendments thereto.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Nature of Business

Spectrum Sciences & Software Holdings Corp. (the Company), headquartered in Falls Church, Virginia, has five reportable segments: Security Solutions, Industrial and Offshore, Repair and Overhaul, Engineering Consulting, and Procurement Services. Security Solutions includes the design and construction of munitions ground support equipment and containers for the shipping and storage of munitions and software to assist in hazard management and weapons impact analysis. The Security Solutions segment comprises the previously reported segments of management services, manufacturing, and engineering and information technology. Industrial and Offshore operations include the Company's engineering, mechanical contracting and steel fabrication operations in the Province of Newfoundland, Canada. The Company's Repair and Overhaul segment is engaged in providing specialized fabrication and maintenance for ships, lifeboats and maritime navigation systems. The Company's Engineering Consulting segment provides services to the federal government in the areas of energy and the environment, homeland defense and transportation. The Procurement Services segment provides acquisition support services to both government and commercial clients.

The Company acquired M&M Engineering Limited (M&M), Coast Engine and Equipment Co., Inc. (CEECO), and Horne Engineering Services, Inc. (Horne) during the 2005 fiscal year. Details of these acquisitions are included in Note 3.

Income Taxes

The Company accounts for income taxes utilizing the asset and liability method. This approach requires the recognition of deferred tax assets and liabilities for the expected future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enacted date. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.

Notes to the Consolidated Financial Statements (Unaudited)

The Company currently has a net operating loss carry forward of approximately \$9,300,000, which would equate to a deferred tax asset of approximately \$3,000,000 at June 30, 2005. The Company has not recorded this federal tax benefit in the accompanying consolidated financial statements, due to the possibility that the net operating loss carryforward may not be utilized, for various reasons, including the potential that we might not have sufficient profits to use the carryforward or the carryforward may be limited as a result of changes in our equity ownership.

Earnings (Loss) Per Share

The Company reports its earnings (loss) per share in accordance with Financial Accounting Standards Board (FASB) Statement No. 128, Earnings Per Share. Statement No. 128 requires the presentation of basic and diluted loss per share on the face of the statement of operations.

Basic earnings (loss) per share (EPS) is calculated by dividing net income (loss) by the weighted-average number of common shares outstanding during the reporting period. Diluted EPS is computed in a manner consistent with that of basic EPS while giving effect to the impact of common stock equivalents. The Company's common stock equivalents consist of employee, director and consultant stock options to purchase common stock. Common stock equivalents were not included in the computation of diluted earnings (loss) per share for the three and six months ended June 30, 2005 and 2004 as the inclusion of these common stock equivalents would be anti-dilutive as the Company is in a net loss position and including such shares would reduce the net loss per share.

Financial Instruments

The Company considers all highly liquid interest-earning investments with a maturity of three months or less at the date of purchase to be cash equivalents. Short-term investments generally mature between three months and two years from the purchase date. Investments with maturities beyond one year may be classified as short-term based on their highly liquid nature and because such marketable securities represent the investment of cash that is available for current operations. All short-term investments are classified as available for sale and are recorded at market value using the specific identification method; unrealized gains and losses are reflected in Other Comprehensive Income. Investments consist of debt instruments. Debt securities are classified as available for sale and are recorded at market using the specific identification method. Unrealized gains and losses (excluding other-than-temporary impairments) are reflected in Other Comprehensive Income.

Investments are considered to be impaired when a decline in fair value is judged to be other than temporary. The Company employs a systematic methodology that considers available evidence in evaluating potential impairment of its investments. If the cost of an investment exceeds its fair value, the Company evaluates, among other factors, general market conditions, the duration and extent to which the fair value is less than cost, as well as our intent and ability to hold the investment. The Company also considers specific adverse conditions related to the financial health of and business outlook for the investee, including industry and sector performance, changes in technology, operational and financing cash flow factors, and rating agency actions. Once a decline in fair value is determined to be other than temporary, an impairment charge is recorded and a new cost basis for the investment is established.

Foreign Currency Translation

The Company's functional currency is the U.S. dollar, except that the functional currency of M&M is the Canadian dollar. In the accompanying consolidated financial statements, the monetary assets and liabilities of M&M were translated to U.S. dollars using the June 30, 2005 exchange rate of .8142 Canadian dollar to 1.00 U.S. dollar. All monetary consolidated statements of operations items of M&M were translated at the average exchange rate for the six months ended June 30, 2005 of .8086 Canadian dollar to 1.00 U.S. dollar.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
Notes to the Consolidated Financial Statements (Unaudited)

Recent Accounting Pronouncements

In December 2004, the FASB issued Statement of Financial Accounting Standards (SFAS) 123 (revised 2004), Share-Based Payment (SFAS 123R). SFAS 123R requires measurement of all employee stock-based compensation awards using a fair-value method and the recording of such expense in the consolidated financial statements. In addition, the adoption of SFAS 123R requires additional accounting related to the income tax effects and disclosure regarding the cash flow effects resulting from share-based payment arrangements. We selected the Black-Scholes option-pricing model as the most appropriate fair-value method for our awards and will recognize compensation cost on a straight-line basis over our awards vesting periods, if any. We adopted SFAS 123R in the first quarter of 2004. The expected adoption of the following recent accounting pronouncements in the first quarter of 2006 is not expected to have a material impact on our results of operations and financial condition:

SFAS No. 151, Inventory Costs An Amendment of ARB No. 43, Chapter 4

SFAS No. 153, Exchanges of Nonmonetary Assets An Amendment of APB Opinion No. 29.

EITF Issue No. 05-06, Determining the Amortization Period for Leasehold Improvements

In May 2005, the FASB issued SFAS 154, Accounting Changes and Error Corrections (SFAS 154), which replaces Accounting Principles Board Opinions No. 20 Accounting Changes and SFAS 3, Reporting Accounting Changes in Interim Financial Statements An Amendment of APB Opinion No. 28. SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. It establishes retrospective application, or the earliest practicable date, as the required method for reporting a change in accounting principle and restatement with respect to the reporting of a correction of an error. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

3. ACQUISITIONS

M&M Engineering Limited

On February 1, 2005, the Company acquired M&M for \$6,768,202 in cash; a combination of the purchase of 100% of the common stock of M&M and an issuance of 1,000 preferred shares to the Company. The purchase price for the common stock of M&M was \$5,958,802 in cash. Pursuant to the Purchase Agreement, M&M redeemed 1,000 of its preferred shares held by EnerNorth Industries Inc. for \$809,400 immediately prior to closing the acquisition and issued the same number of preferred shares to the Company for \$809,400. The total cost of the acquisition includes approximately \$297,000 of acquisition related expenses for a total cost of \$7,065,202. The primary purpose of this acquisition was to diversify the Company's corporate customer base beyond U.S. federal government contracting and to capitalize on the growth potential in the natural resource sector to include: the offshore oil and gas industries, the hydroelectric sector, mining and the pulp and paper industries in Newfoundland and Labrador.

Coast Engine and Equipment

On February 25, 2005, the Company acquired CEECO with an initial cash payment of \$300,000 plus an earn-out over the next three years. Under the terms of the Purchase Agreement, the Company will pay to the former Shareholders of CEECO a total purchase price of up to \$900,000 over a three-year period. The purchase price is payable in cash and common stock of the Company and is subject to certain adjustments, including, without limitation, adjustments based on CEECO's earnings during such three-year period. In addition to the \$300,000 cash payment for CEECO, there were approximately \$30,000 of acquisition related expenses. Pursuant to a security agreement executed in connection with the Purchase Agreement, the former Shareholders of CEECO will retain a security interest in all of the assets of CEECO until the total purchase price has been paid. The Company has a three-year employment contract with Louis T. Rogers, former owner of CEECO. The CEECO acquisition allows the Company to exploit other non-government customer bases in the south-central Florida region. It also provides the opportunity to pursue business opportunities within the U.S. Coast Guard and U.S. Navy by increasing the Company's presence in that market.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.

Notes to the Consolidated Financial Statements (Unaudited)

As of June 30, 2005, CEECO has met the purchase price EBITDA (earnings before interest, tax, depreciation and amortization), as defined in the agreement, goals for the first year. While these results must be verified through year-end audit, one-quarter of the first year price of \$200,000, or \$50,000 has been accrued. This includes \$50,000 accrued in this fiscal quarter to properly account for this expense.

Horne Engineering, Inc.

On May 11, 2005, the Company acquired all of the issued and outstanding capital stock of Horne Engineering, Inc. (Horne), from its shareholders, Darryl K. Horne, Charlene M. Horne and Michael M. Megless (the Horne Shareholders), pursuant to an Agreement and Plan of Merger (the Merger Agreement). Pursuant to the Merger Agreement, Horne was merged with and into Horne Acquisition LLC, a wholly owned subsidiary of the Company. The purchase price for the capital stock of Horne was \$4.5 million in cash and 6.1 million unregistered shares of the Company's common stock (the Shares). Additional shares of common stock could subsequently become issuable by the Company to the Horne Shareholders to the extent that the average closing price of the Company's common stock on NASD OTC Bulletin Board, or other public securities market, for the trading days during the two month period ending on May 11, 2007 is less than \$3.25 per share, subject to Horne (on a stand alone basis) meeting or exceeding 2005 gross revenues of \$75 million with EBITDA (as defined in the merger agreement) of \$3.25 million (the 2005 EBITDA) and EBITDA of not less than \$3.25 million in 2006. Pursuant to an Amendment and Waiver Agreement entered into among the parties to the Merger Agreement on May 11, 2005 (the Amendment), the Company held back 4.0 million of the Shares payable to the former Horne Shareholders under the Merger Agreement (the Hold Back Shares), with the disposition of those shares subject to two conditions. First, the Amendment requires the Company to release 3.0 million of the Hold Back Shares to the former Horne Shareholders promptly upon receiving certain third party consents relating to certain of Horne's contracts, which are specified in the Amendment. Second, if Horne's 2005 EBITDA is less than \$3.25 million (the EBITDA Shortfall), the Company will be entitled to recover any remaining Hold Back Shares limited such that the value of the recovered Hold Back Shares, based on the closing price of the Company's common stock on May 11, 2005, does not exceed three times the EBITDA Shortfall. As of November 11, 2005, the Company has received the required consents described above and intends to promptly issue three million of the Holdback shares to Horne's former shareholders. See also subsequent events described in Note 13.

In connection with the Merger Agreement, the Company and the Horne Shareholders entered into a Registration Rights Agreement, dated May 11, 2005 (the Rights Agreement), pursuant to which the Company agreed to prepare and file a registration statement pursuant to Rule 415 under the Securities Act of 1933, as amended (the Securities Act), covering the resale from time to time of all of the shares of the Company's common stock issued to the Shareholders pursuant to the Merger Agreement.

Upon the closing of the Merger Agreement, Messrs. Horne and Megless were appointed to the Company's Board of Directors. In connection with the Merger Agreement, Messrs. Horne and Megless executed Employment Agreements with the Company, dated as of May 11, 2005 (the Employment Agreements), pursuant to which such individuals were appointed Chief Executive Officer (CEO), and Chief Financial Officer (CFO), respectively. Pursuant to a Stock Option Agreement executed in connection with the Merger Agreement, Mr. Horne received an option to purchase 1.0 million shares of the Company's common stock at an exercise price of \$1.65 per share, subject to Horne meeting the revenue and EBITDA targets for 2005 as described above. The Company also reserved 2.0 million shares of the Company's common stock for the issuance of stock options to be granted to the employees of Horne at the discretion of Mr. Horne.

Each acquisition described above was accounted for under the purchase method of accounting; accordingly, the purchase price has been allocated to reflect the fair value of assets and liabilities acquired at the date of acquisition. For the six-month period ended June 30, 2005, the results of operations reported for the Company includes a full six months of operations for Spectrum Sciences & Software, Inc. (SSSI), a wholly owned subsidiary of the Company, five months of operations for M&M (February 1, 2005 through June 30, 2005), four months of operations for CEECO (March 1, 2005 through June 30, 2005), and two months of operations for Horne (May 1, 2005 through June 30, 2005), respectively. For the three month and six month periods ended June 30, 2004, the results of operations

represent only those of SSSI.

SPECTRUM SCIENCES & SOFTWARE HOLDINGS CORP.
Notes to the Consolidated Financial Statements (Unaudited)

Pro Forma Results

The results of these acquisitions, had they been consummated at the beginning of each period shown, are included in the pro forma information below. The historical revenues and earnings of M&M, CEECO, and Horne for the periods ended June 30, 2005 and 2004 have been combined with the revenues and earnings of Spectrum Sciences & Software Holdings Corp. for the three and six months ended June 30, 2005 and 2004, respectively. This pro forma information does not necessarily reflect the results of operations that would have occurred had the acquisitions taken place at the beginning of each of the three and six month periods represented and is not necessarily indicative of results that may be obtained in the future.

	Three months ended June 30,		Six months ended June 30,	
	2005	2004	2005	2004
Revenue	\$ 13,307,675	\$ 14,576,726	\$ 37,641,826	\$ 22,888,868
Net loss	(1,046,875)	(26,302,478)	(2,778,843)	(39,691,478)