

Edgar Filing: SUN NETWORK GROUP INC - Form 10-Q

SUN NETWORK GROUP INC  
Form 10-Q  
August 14, 2003

UNITED STATES  
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 fiscal quarter ended: June 30, 2003  
Commission file number: 33-42498

SUN NETWORK GROUP, INC.  
(Exact name of registrant as specified in its charter)

Florida 65-024624  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

1440 CORAL RIDGE DR., SUITE 140  
CORAL SPRINGS, FLORIDA 33071  
(Address of principal executive offices)  
(Zip code)

(954) 360-4080  
(Registrant's telephone number, including area code)

Indicate by check mark whether 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 X No  
-----

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of August 1, 2003: 28,448,487 shares of common stock, \$.001 par value per share.

SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
FORM 10-Q  
QUARTERLY PERIOD ENDED JUNE 30, 2003  
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### SUN NETWORK GROUP, INC. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

	June 30, 2003	December 31, 2002
	-----	-----
	(Unaudited)	
Assets		
Current assets:		
Cash .....	\$ 5,417	\$ 81,751
Due from joint venture partner, net .....	-	50,000
Deferred debt issuance cost, net .....	-	10,000
Prepays .....	54,000	20,910
	-----	-----
Total current assets .....	59,417	162,661
	-----	-----
Other assets:		
Radio programs, net .....	2,794	10,192
	-----	-----
Total other assets .....	2,794	10,192
	-----	-----
Total assets .....	\$ 62,211	\$ 172,853
	=====	=====
Liabilities and Stockholders' Deficit		
Current liabilities:		
Convertible debentures, net of discount .....	\$ 500,000	\$ 487,226
Accounts payable .....	38,669	16,961

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Accrued interest .....	57,207	28,053
Accrued penalty .....	290,975	31,233
Accrued compensation, related party .....	118,250	58,750
Due to officer .....	5,241	3,242
	-----	-----
Total current liabilities .....	1,010,342	625,465
	-----	-----
Minority interest .....	39,524	43,224
	-----	-----
Stockholders' deficit:		
Preferred stock (\$0.001 par value; 10,000,000 authorized shares; no shares issued and outstanding at June 30, 2003 and December 31, 2002, respectively) .....	-	-
Common stock (\$0.001 par value; 100,000,000 authorized shares; 28,448,487 and 22,448,487 shares issued and outstanding at June 30, 2003 and December 31, 2002, respectively) .....	28,448	22,448
Common stock issuable (5,000,000 shares at December 31, 2002) .....	-	5,000
Additional paid-in capital .....	1,325,541	1,290,041
Accumulated deficit .....	(2,341,644)	(1,813,325)
	-----	-----
Total stockholders' deficit .....	(987,655)	(495,836)
	-----	-----
Total liabilities and stockholders' deficit	\$ 62,211	\$ 172,853
	=====	=====

See accompanying notes to consolidated financial statements.

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SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2003	2002	2003	2002
	-----	-----	-----	-----
REVENUES .....	\$ 32,110	\$ -	\$ 33,229	\$ -
	-----	-----	-----	-----
OPERATING EXPENSES:				
Compensation .....	37,500	40,655	78,486	81,016
Amortization .....	3,699	-	7,398	-
Bad debt .....	1,645	-	3,273	-
Consulting .....	5,324	119,100	13,129	119,100
Debenture penalty .....	230,153	-	259,742	-
Debt issuance cost amortization ..	5,000	-	10,000	-
Impairment loss .....	-	-	20,910	-
Professional fees .....	18,066	12,074	49,509	13,624
Other selling, general and administrative .....	34,134	23,534	59,712	31,661
	-----	-----	-----	-----
Total Operating Expenses .....	335,521	195,363	502,159	245,401

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LOSS FROM OPERATIONS .....	(303,411)	(195,363)	(468,930)	(245,401)
OTHER INCOME (EXPENSES):				
Settlement expense .....	-	-	(36,500)	-
Interest expense .....	(21,347)	(240,570)	(41,928)	(240,570)
Recovery of bad debt .....	4,777	-	12,066	-
Interest income .....	1,645	-	3,273	-
Total Other Expenses .....	(14,925)	(240,570)	(63,089)	(240,570)
LOSS BEFORE MINORITY INTEREST .....	(318,336)	(435,933)	(532,019)	(485,971)
MINORITY INTEREST IN SUBSIDIARY LOSS .	1,850	-	3,700	-
NET LOSS .....	\$ (316,486)	\$ (435,933)	\$ (528,319)	\$ (485,971)
EARNING (LOSS) PER SHARE:				
Net Loss Per Common Share				
- Basic and Diluted .....	\$ (0.01)	\$ (0.02)	\$ (0.02)	\$ (0.02)
Weighted Common Shares Outstanding				
- Basic and Diluted .....	28,448,487	22,045,190	28,249,592	21,860,456

See accompanying note to consolidated financial statements.

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SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

	For the Six Months Ended June 30,	
	2003	2002
Cash flows from operating activities:		
Net loss .....	\$ (528,319)	\$ (485,971)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization expense .....	7,398	-
Bad debt expense .....	3,273	-
Impairment loss .....	20,910	-
Amortization of deferred debt issuance costs .....	10,000	-
Amortization of debt discounts to interest expense	12,774	-
Stock based consulting expense .....	36,500	84,000
Interest expense .....	-	240,570
Allocation of loss to minority interest .....	(3,700)	-
(Increase) decrease in:		

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Interest receivable .....	(3,273)	-
Prepays .....	(54,000)	-
Increase (decrease) in:		
Accounts payable .....	21,708	1,581
Accrued expenses .....	29,154	-
Accrued penalties .....	259,742	-
Accrued compensation, related party .....	59,500	75,000
	-----	-----
Net cash used in operating activities .....	(128,333)	(84,820)
	-----	-----
Cash flows from financing activities:		
Equity proceeds from stockholders .....	-	82,390
Loan proceeds from stockholders .....	-	20,442
Proceeds from convertible debt .....	-	250,000
Deferred debt issuance costs .....	-	(20,000)
Proceed from loan from joint venture partner .....	50,000	-
Proceeds from (payments on) loans from officer .....	1,999	(29,263)
	-----	-----
Net cash provided by financing activities .....	51,999	303,569
	-----	-----
Net (decrease) increase in cash .....	(76,334)	218,749
Cash at beginning of period .....	81,751	5,321
	-----	-----
Cash at end of period .....	\$ 5,417	\$ 224,070
	=====	=====
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest .....	\$ -	\$ -
	=====	=====
Income Taxes .....	\$ -	\$ -
	=====	=====

See accompanying notes to consolidated financial statements.

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SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2003  
(UNAUDITED)

NOTE 1 - BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Organization

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). The accompanying consolidated financial statements for the interim periods are unaudited and reflect all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the consolidated financial position and consolidated operating results for the periods presented.

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These consolidated financial statements should be read in conjunction with the consolidated financial statements of Sun Network Group, Inc. for the year ended December 31, 2002, 2001 and 2000 and notes thereto contained in the Report on Form 10-K for the year ended December 31, 2002 as filed with the SEC. The results of operations for the six months ended June 30, 2003 are not necessarily indicative of the results for the full fiscal year ending December 31, 2003.

Sun Network Group, Inc. was incorporated under the laws of Florida on May 9, 1990 and was inactive for several years.

On September 5, 2002, the Company formed a general partnership with one other partner. The partnership, Radio X Network ("Radio X"), was formed to independently create, produce, distribute, and syndicate radio programs. The Company offers radio programs to radio stations in exchange for advertising time on those stations, which the Company then sells to advertisers. This is known in the media industry as "barter syndication." In return for providing the radio stations with programming content, the Company receives advertising minutes, which the Company then sells to advertisers. The amount of advertising minutes received is based on several factors, including the type and length of the programming and the audience size of the radio station affiliate. In some instances, the Company may also receive a monthly license fee in addition to or in lieu of the commercial inventory and may derive revenues from sponsorship and merchandising. Sun Network Group, Inc. acts as a holding company for Radio X and RadioTV Network, Inc. RadioTV Network Inc. is developing a business to produce and broadcast television versions of top rated radio programs.

### Principles of Consolidation

The consolidated financial statements include the accounts of Sun Network Group, Inc., its wholly owned subsidiary, RadioTV Network, Inc., and its controlled subsidiary Radio X. All significant intercompany accounts and transactions have been eliminated in consolidation.

### Revenue Recognition

The Company accounts for revenues from its Radio TV Network, Inc operations in accordance with the AICPA Accounting Standards Executive Committee Statement of Position No. 00-2, "Accounting by Producers or Distributors of Films" ("SOP 00-2").

The Company produced in the past and may again in the future, episodic television series and generates revenues from the sale of broadcast licenses. The terms of the licensing arrangement may vary significantly from contract to contract and may include fixed fees, variable fees with or without nonrefundable minimum guarantees, or barter arrangements.

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SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
June 30, 2003  
(UNAUDITED)

### NOTE 1 - BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

#### Revenue Recognition (Continued)

The Company recognizes monetary revenues when evidence of a sale or licensing arrangement exists, the license period has begun, delivery of the film to the licensee has occurred or the film is available for immediate and unconditional delivery, the arrangement fee is fixed or determinable, and collection of the

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arrangement fee is reasonably assured. The Company recognizes only the net revenue due to the Company pursuant to the formulas or amounts stipulated in the customer contracts.

The Company recognizes revenues from barter arrangements in accordance with the Accounting Principles Board Opinion No. 29 "Accounting for Non-Monetary Exchanges," ("APB 29") as interpreted by EITF No. 93-11 "Accounting for Barter Transactions Involving Barter Credits." In general, APB 29 and its related interpretation require barter revenue to be recorded at the fair market value of what is received or what is surrendered, whichever is more clearly evident.

The Company recognizes revenues from the sale of radio program advertising in its Radio X Network operations when the fee is determinable and after the commercial advertisements are broadcast. Any amounts received from customers for radio advertisements that have not been broadcast during the period are recorded as deferred revenues until such time as the advertisement is broadcast.

The Company recognizes radio program license fee revenues when evidence of a licensing arrangement exists, the license period has begun, delivery of the program to the licensee has occurred or is available for immediate and unconditional delivery, the arrangement fee is fixed or determinable, and collection of the arrangement fee is reasonably assured.

### NOTE 2 - CONVERTIBLE DEBENTURES AND WARRANTS AND DEFAULT

On June 27, 2002, the Company entered into a Securities Purchase Agreement to Issue and sell 12% convertible debentures, in the aggregate amount of \$750,000, convertible into shares of common stock, of the Company. The Company is permitted to use the proceeds to make one or more loans for a legitimate business purpose, which such loans, in the aggregate, may not exceed \$100,000. As of June 27, 2002, \$250,000 in convertible debentures were issued to various parties. The holders of this debt have the right to convert all or any amount of this debenture into fully paid and non-assessable shares of common stock at the conversion price with the limitation that any debenture holder may not convert any amount of the debentures if after conversion that debenture holder would beneficially hold more than 4.9% of the total outstanding common stock of the Company. However, any debenture holder may waive this limitation provision with 61 days written notice to the Company. The conversion price generally is the lesser of (a) 50% of the market value of the common stock as defined in the debenture or (b) \$0.15. Interest is payable either quarterly or at the conversion date at the option of the holder. The convertible debentures mature on June 27, 2003, and are secured by substantially all present and future assets of the Company. (see default discussion below)

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SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
June 30, 2003  
(UNAUDITED)

### NOTE 2 - CONVERTIBLE DEBENTURES AND WARRANTS (CONTINUED)

In 2002, the Company paid \$20,000 of legal fees related to the debenture issuances and recorded these fees as a deferred debt issuance cost asset to be amortized over the one-year term of the debentures. Amortization of the deferred debt issuance cost included in general and administrative was \$10,000 for the six months ended June 30, 2003.

In connection with the convertible debentures issued, warrants to purchase 250,000 common shares were issued to the holders at an exercise price per share of \$0.15. The warrants are exercisable immediately and through the third

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anniversary of the date of issuance. These warrants were treated as a discount on the convertible debenture and in 2002 were valued at \$9,430 under SFAS No. 123 using the Black-Scholes option-pricing model.

On August 8, 2002, an additional \$250,000 of convertible debentures and warrants to purchase 250,000 common shares were purchased from the Company for \$250,000 with the terms similar to that described above and maturing on August 8, 2003. The warrants were treated as a discount on these convertible debentures and in 2002 were valued at \$14,775 computed using the Black-Scholes option-pricing model.

The discount on the convertible debentures is amortized to interest expense over the term of the debentures starting on July 1, 2002. Amortization included in interest expense for the six months ended June 30, 2003 was \$12,774.

If the registration statement relating to the debentures is not declared effective within 90 days of June 27, 2002 or loses quotation in the NASD OTCBB the Company is obligated to pay a fee to the debenture holders equal to 2% per month on the principal balance outstanding. As of June 30, 2003, the registration statement was not effective and accordingly, the Company has recorded \$59,507 in penalty fee expenses for the six months ended June 30, 2003 resulting in a total accrued penalty related to this penalty of \$90,740 at June 30, 2003.

Under the debenture, the Company incurs a liquidated damages penalty for not having enough authorized shares to allow for the issuance of all dilutive securities based on a formula as stipulated in the Debenture agreement. The penalty rate is computed as 3% of the outstanding debenture balance per month which computes to \$15,000 per month. The accrued penalty through June 30, 2003 amounted to \$116,137. Although the Company authorized the increase of its authorized shares to 200,000,000 in May 2003, this increase was not sufficient to satisfy the required authorized shares pursuant to the Debenture Agreement and therefore the penalty has been accrued through June 30, 2003.

On June 28, 2003 (the "Default Date") the Company defaulted on its maturity date payment on \$250,000 of debentures. A default penalty is computed under the terms of the debenture as \$84,098 and has been charged to operations on the Default Date and included in accrued penalty at June 30, 2003.

The convertible debenture liability is as follows at June 30, 2003:

Convertible debenture	\$ 500,000
Less: unamortized discount on debenture	-
	-----
Convertible debenture, net	\$ 500,000
	=====

Accrued interest at June 30, 2003 was \$57,207.

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SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
 June 30, 2003  
 (UNAUDITED)

NOTE 3 - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

The Financial Accounting Standards Board has recently issued several new accounting pronouncements:

Statement No. 146, "Accounting for Exit or Disposal Activities" ("SFAS 146")



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addresses the recognition, measurement, and reporting of cost that are associated with exit and disposal activities that are currently accounted for pursuant to the guidelines set forth in EITF 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to exit an Activity (including Certain Cost Incurred in a Restructuring)," cost related to terminating a contract that is not a capital lease and one-time benefit arrangements received by employees who are involuntarily terminated - nullifying the guidance under EITF 94-3. Under SFAS 146, the cost associated with an exit or disposal activity is recognized in the periods in which it is incurred rather than at the date the Company committed to the exit plan. This statement is effective for exit or disposal activities initiated after December 31, 2002 with earlier application encouraged. The adoption of SFAS 146 did not have a material impact on the Company's financial position, results of operations or liquidity.

In December 2002, the FASB issued Statement of Financial Accounting Standards No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure. Statement 148 provides alternative methods of transition to Statement 123's fair value method of accounting for stock-based employee compensation. It also amends the disclosure provisions of Statement 123 and APB Opinion No. 28, Interim Financial Reporting, to require disclosure in the summary of significant accounting policies of the effects of an entity's accounting with respect to stock-based employee compensation on reported net income and earnings per share in annual and interim financial statements. Statement 148's amendment of the transition and annual disclosure requirements of Statement's 123 are effective for fiscal years ending after December 15, 2002. Statement 148's amendment of the disclosure requirements of Opinion 28 is effective for interim periods beginning after December 15, 2002. The adoption of the disclosure provisions of Statement 148 as of December 31, 2002 did not have a material impact on the Company's financial condition or results of operations.

In November 2002, the FASB issued FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" (FIN 45). FIN 45 requires that upon issuance of a guarantee, a guarantor must recognize a liability for the fair value of an obligation assumed under a guarantee. FIN 45 also requires additional disclosures by a guarantor in its interim and annual financial statements about the obligations associated with guarantees issued. The recognition provisions of FIN 45 are effective for any guarantees issued or modified after December 31, 2002. The disclosure requirements are effective for financial statements of interim or annual periods ending after December 15, 2002. The adoption of this pronouncement did not have a material effect on the earnings or financial position of the Company.

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SUN NETWORK GROUP, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
June 30, 2003  
(UNAUDITED)

### NOTE 3 - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS (CONTINUED)

In January 2003, the FASB issued Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities." FIN 46 requires that if an entity has a controlling financial interest in a variable interest entity, the assets, liabilities and results of activities of the variable interest entity should be included in the consolidated financial statements of the entity. FIN 46 requires that its provisions are effective immediately for all arrangements entered into after January 31, 2003. The Company does not have any variable interest entities created after January 31, 2003. For those arrangements entered into prior to January 31, 2003, the FIN 46 provisions are required to be adopted at the beginning of the first interim or annual period beginning after June 15, 2003.

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The Company has not identified any variable interest entities to date and will continue to evaluate whether it has variable interest entities that will have a significant impact on its consolidated balance sheet and results of operations.

### NOTE 4 - STOCKHOLDERS' DEFICIT

#### Preferred Stock

On June 5, 2003, the Company's Board of Directors authorized 10,000,000 shares of preferred stock, par value \$0.001. Such preferred stock, or any series thereof, shall have such designations, preferences, participating, optional or other annual rights and qualifications, limitations or restrictions adopted by the Company's Board of Directors.

#### Common Stock

In January 2003, 5,000,000 shares previously issuable were issued.

On February 4, 2003, the Company settled a lawsuit by issuing 1,000,000 common shares and \$6,500 in cash. The shares were valued at the quoted trading price of \$0.03 per share on the settlement date resulting in a total settlement expense of \$36,500.

On June 5, 2003, with the approval of the Company's Board of Directors, the authorized number of common shares, \$0.001 par value, issuable by the Company was increased from 100,000,000 to 200,000,000.

### NOTE 5 - IMPAIRMENT LOSS

The Company received certain capital stock of a private German company in exchange for a prepaid expense of \$20,910 that was recorded at December 31, 2002. As the valuation of the capital stock received could not be supported based on valuation or other objective data, the Company has elected the conservatively impair this asset for accounting purposes. Accordingly, the Company recorded an impairment loss of \$20,910 for the six months ended June 30, 2003.

### NOTE 6 - COMMITMENTS

On February 21, 2003 the Company executed a Production and Studio Facility Agreement (the "Agreement") whereby the Company will pay a vendor to construct a production facility and provide certain initial stipulated production services relating to a television program for which the Company has exclusive rights. Production is to commence no later than October 1, 2003.

The total consideration to be paid by the Company is \$162,000. The Company paid \$54,000 upon execution of the agreement and became committed to pay the next \$54,000 on August 1, 2003. Another \$54,000 will be due when the studio construction is completed. As of the date of this report, the \$54,000 due on August 1, 2003 has not been paid. As contingent consideration, the Company will pay 5% of all "net receipts" as defined in the Agreement

The Company may terminate the agreement after July 1, 2003 and received as a refund any unused portion of the consideration advanced plus \$10,000.

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### NOTE 7 - REPORTABLE SEGMENTS

There were no reportable segments for the six months ended June 30, 2002.

At June 30, 2003, the Company had two reportable segments: Network TV and Network Radio. The Company's reportable segments have been determined in accordance with the Company's internal management structure. The following table sets forth the Company's financial results by operating segments:

June 30, 2003	Network TV	Network Radio	Total
Assets .....	\$ 59,417	\$ 2,794	\$ 62,211
Revenues .....	\$ 30,000	3,229	\$ 33,229
Amortization .....	-	(7,398)	(7,398)
Other operating expenses .....	(479,466)	(15,295)	(494,761)
Interest income .....	3,273	-	3,273
Interest expense .....	(41,928)	-	(41,928)
Settlement expense .....	(36,500)	-	(36,500)
Recovery of bad debt .....	-	12,066	12,066
Minority interest in subsidiary losses .....	-	3,700	3,700
Segment loss .....	\$ (524,621)	\$ (3,698)	\$ (528,319)

### NOTE 8 - GOING CONCERN

As reflected in the accompanying consolidated financial statements, the Company had an accumulated deficit of \$2,341,644 and a working capital deficit of \$950,925 at June 30, 2003, and cash used in operations in for the six months ended June 30, 2003 of \$128,333. In addition, revenues were nominal.

In 2002, the Company received \$500,000 in funding and a commitment for an additional \$250,000 which should be available once the Company's Form SB-2 becomes effective. In addition, management has implemented revenue producing programs in its new subsidiary, Radio X Network, which have started to generate revenues.

Management expects operations to generate negative cash flow at least through December 2003 and the Company does not have existing capital resources or credit lines available that are sufficient to fund operations and capital requirements as presently planned over the next twelve months. The Company's ability to raise capital to fund operations is further constrained because they have already pledged substantially all of their assets and have restrictions on the issuance of the common stock.

The Company expects to generate substantially all revenues in the future from sales of Radio X Network programs. However, the Company's limited financial resources have prevented the Company from aggressively advertising its product to achieve consumer recognition.

The ability of the Company to continue as a going concern is dependent on the Company's ability to further implement its business plan and generate revenues. The consolidated financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern. Management believes that the actions presently being taken to further implement its business plan and generate additional revenues provide the opportunity for the Company to continue as a going concern.

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

#### OVERVIEW

The Company acquired all of the assets of RadioTV Network, Inc ("RTV") on July 16, 2001 in a transaction treated as a recapitalization of RTV. RTV has been developing and operating, for the past few years, a new television network that produced and distributed TV adaptations of top rated radio programs and also produces and distributes radio programs through a partnership with an established radio network.

#### RECENT DEVELOPMENTS

On June 27, 2002 the Company entered into agreement with four (4) institutional investors to provide the Company \$750,000 in capital through a Secured Convertible Debenture Offering ("Debenture"). The Company has filed and withdrawn a SB-2 Registration Statement and, subsequently, a SB-2/A amended Registration Statement and a new SB-2 Registration Statement in connection with the Debenture.

On June 28, 2002 the Company entered into an Option Agreement and Plan of Merger ("Agreement") to acquire all of the assets of Live Media Enterprises, Inc ("Live"), a west coast based independent producer of consumer lifestyle events. On September 3, 2002 the Company elected to terminate the Agreement with Live and will not proceed with the acquisition even on modified terms. In connection with the Agreements the Company has loaned Live the sum of \$56,000. This loan is documented in two Promissory Notes and is collateralized by substantially all of the assets of Live and personally guaranteed by Live's principal shareholder and officer. The Company is presently attempting to collect its debts from Live in the Los Angeles Superior Court.

On September 5, 2002, the Company entered into agreement with Sports Byline USA, L.P. to own and operate a new, national radio network, Radio X. Radio X intends to develop, produce, license, broadcast and distribute radio programs, targeted to young males that will be distributed via traditional terrestrial stations, via satellite and over the Internet. The Company has contributed the sum of \$100,000 to this business plus certain management services. Our partnership interest is 50%, however, we have an overriding voting control over all matters of the partnership. Radio X currently has three radio programs in distribution.

The Company intends to use the net proceeds from the Debenture to develop, operate and expand the businesses of RTV and Radio X and to continue to seek other opportunities for the Company. The Company believes that upon completing the Debenture financing it will have sufficient capital to operate through the end of 2003. The Company will, however, continue to seek additional capital to fund further development, expansion and operation of its businesses. Upon conversion of the Debentures into the Company common stock there will be substantial shareholder dilution.

#### RESULTS OF OPERATIONS

Six months ended June 30, 2003 compared to the six months ended June 30, 2002

#### REVENUES

Revenues for the six months ended June 30, 2003 were \$33,229 as compared to revenues for the six months ended June 30, 2002 of \$0. Of the \$33,229 of revenue, \$30,000 was derived from video production and \$3,229 revenues were derived from the new consolidated subsidiary, Radio X Network during its initial months of operation.

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### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

#### OPERATING EXPENSES

Compensation was \$78,486 for the six months ended June 30, 2003 compared to \$81,016 for the comparable period in 2002. Compensation relates solely to compensation under our employment agreement with our president.

Amortization of radio programs of \$7,398 for the six months ended June 30, 2003 results from amortizing the radio programs intangible assets that resulted from the investment by our subsidiary, RadioTV Network, Inc, in the Radio X Network. The intangible asset is being amortized using the straight-line method over the expected useful life of the program of one year. There was no asset being amortized in the comparable period in 2002 as the investment was made in September 2002.

Consulting expense for the six months ended June 30, 2003 was \$13,129 compared to \$119,100 for the six months ended June 30, 2002.

The Debenture penalty of \$259,742 for the six months ended June 30, 2003 represents the accrued penalty under the provisions of the Convertible Debentures. The penalties relate to the deadlines associated with the Company filing a Registration Statement in connection with the Convertible Debentures and liquidated damages penalty for not having enough authorized shares to allow for the issuance of all dilutive securities based on a formula as stipulated in the Debenture agreement and a default penalty of \$84,098 on the June 28, 2003 maturity of \$250,000 of debentures

For the six months ended June 30, 2003, the Company had an impairment loss of \$20,910 as compared to \$0 for the six months ended June 30, 2002. The impairment relates to certain capital stock received in a German private company in lieu of a refund of a prepaid expense paid to a service provider. Since there was no objective valuation data supporting the value of the capital stock received, the Company elected to impair this asset.

Professional fees for the six months ended June 30, 2003 were \$49,509 compared to \$13,624 for the six months ended June 30, 2002. The increase is primarily related to accounting and legal, audit and registration statement related services regarding our filing a SB-2 and our quarterly and annual reports.

Other selling, general and administrative expenses were \$59,712 for the six months ended June 30, 2003 compared to \$31,661 for the six months ended June 30, 2002. The increase in expenses is primarily due to travel of \$26,498, talent costs in Radio X of \$5,900, insurance of \$5,448, telephone of \$3,832 and other miscellaneous operating expenses.

Interest expense was \$41,928 for the six months ended June 30, 2003 compared to \$240,570 for the six months ended June 30, 2002. Interest expense for the six months ended June 30, 2003 is attributed to the Convertible Debenture offering and includes accrued interest of the Convertible Debentures and amortization of the debt discount. For the six months ended June 30, 2002, \$240,520 of interest expense was recognized relating to an imbedded beneficial conversion feature on the convertible debentures.

On February 4, 2003, the Company settled a lawsuit by issuing 1,000,000 common shares and \$6,500 in cash. The shares were valued at the quoted trading price of \$0.03 per share on the settlement date resulting in a total settlement expense of \$36,500.

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As a result of these factors, we reported a net loss of \$528,319 or \$(.02) per share for the six months ended June 30, 2003 as compared to a net loss of \$485,971 or \$(.02) per share for the six months ended June 30, 2002.

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### LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2003, we had a stockholders' deficit of \$2,341,644. Our operations have been funded by an equity investor in our common stock where we issued 183,088 common shares for \$82,390 cash during 2002 and by the sale of convertible debentures of \$500,000 through June 30, 2003. These funds were used primarily for working capital, capital expenditures, advances to third parties in anticipation of entering into a merger or acquisition agreement and to pay down certain related party loans. The cash balance at June 30, 2003 was \$5,417 and we will have to minimize operations until we receive additional cash flows from our businesses or complete our Debenture financing.

We have no other material commitments for capital expenditures except for the anticipated launch of a RadioTV Network program in 2003. We expect an additional \$250,000 in convertible debenture financing upon effectiveness of our registration statement. We may also receive financing from the exercise of 500,000 outstanding warrants, which would provide maximum funds of \$75,000. Other than several thousand dollars to be generated from our advertising sales from the broadcast of our initial program on the Radio X Network, debenture proceeds and warrant exercise proceeds we have no external sources of liquidity. Although we believe we will have sufficient capital to fund our anticipated operations through fiscal 2003, we are not currently generating meaningful revenues and, unless we raise additional capital, we may not be able to continue operating beyond fiscal 2003.

Net cash used in operations during the six months ended June 30, 2003 was \$128,333 and was substantially attributable to net loss of \$528,318 offset primarily by non-cash stock based expenses of \$36,500, impairment loss of \$20,910, non-cash debt discount amortization of \$12,774, amortization of deferred debt issuance costs of \$10,000, net changes in operating assets and liabilities of \$312,831. In the comparable period of 2001 we had net cash used in operations of \$16,289 primarily relating to the net loss of \$50,038 primarily offset by a change in accrued compensation of \$37,500.

Net cash provided by financing activities for the six months ended June 30, 2003 was \$51,999 as compared to net cash provided by financing activities of \$303,569 for the six months ended June 30, 2002. During the six months ended June 30, 2003, we received proceeds from a loan from our joint venture partner of \$50,000 and a loan from an officer of \$1,999. The loan from our joint venture partner came from funds held by that partner and due to our controlled subsidiary, Radio X. In the comparable period of 2002, we received a loan from stockholder of \$20,442, equity proceeds from stockholders of \$82,390, net proceeds from convertible debt of \$230,000 offset by payment on loans to officers of \$29,263.

For the fiscal year ended December 31, 2002, our auditors have issued a going concern opinion in connection with their audit of the Company's financial statements. These conditions raise substantial doubt about our ability to continue as a going concern if sufficient additional funding is not acquired or alternative sources of capital developed to meet our working capital needs.

### CRITICAL ACCOUNTING POLICIES

A summary of significant accounting policies is included in Note 1 to the audited financial statements included in our Annual Report on Form 10-K, as

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amended, for the year ended December 31, 2002 as filed with the United States Securities and Exchange Commission. We believe that the application of these policies on a consistent basis enables us to provide useful and reliable financial information about our operating results and financial condition.

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### ESTIMATES

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

### REVENUE RECOGNITION

We account for film revenues in accordance with the AICPA Accounting Standards Executive Committee Statement of Position No. 00-2, "Accounting by Producers or Distributors of Films" ("SOP 00-2").

We generally produce episodic television series and radio programs and generate revenues from advertising sales and the sale of broadcast licenses. Advertising revenues can vary significantly subject to a program's popularity and distribution and general supply and demand and the terms of the licensing arrangements may vary significantly from contract to contract and may include fixed fees, variable fees with or without nonrefundable minimum guarantees, or barter arrangements.

We recognize monetary revenues when evidence of a sale or licensing arrangement exists, the license period has begun, delivery of the film to the licensee has occurred or the film is available for immediate and unconditional delivery, the arrangement fee is fixed or determinable, and collection of the arrangement fee is reasonably assured. The Company recognizes only the net revenue due to the Company pursuant to the formulas or amounts stipulated in the customer contracts.

We recognize revenues from barter arrangements in accordance with the Accounting Principles Board Opinion No. 29 "Accounting for Non-Monetary Exchanges," ("APB 29") as interpreted by EITF No. 93-11 "Accounting for Barter transactions Involving Barter Credits." In general, APB 29 and its related interpretation require barter revenue to be recorded at the fair market value of what is received or what is surrendered, whichever is more clearly evident. We recognize revenues from the sale of radio program advertising when the fee is determinable and after the commercial advertisements are broadcast. Any amounts received from customers for radio advertisements that have not been broadcast during the period are recorded as deferred revenues until such time as the advertisement is broadcast. We recognize radio program license fee revenues when evidence of a licensing arrangement exists, the license period has begun, delivery of the program to the licensee has occurred or is available for immediate and unconditional delivery, the arrangement fee is fixed or determinable, and collection of the arrangement fee is reasonably assured.

### STOCK BASED COMPENSATION

We account for stock transactions with employees in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees." In accordance with Statement of Financial Accounting Standards No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation," we adopted the pro forma disclosure requirements of SFAS 123. We account for stock issued to non-employees in accordance with SFAS

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123 and related interpretations.

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### ITEM 3. CONTROLS AND PROCEDURES

#### Evaluation of Disclosure Controls and Procedures

Our management, under the supervision and with the participation of our chief executive officer and chief financial officer, conducted an evaluation of our "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934 (the "Exchange Act") Rules 13a-14I) within 90 days of the filing date of this Quarterly Report on Form 10-Q (the "Evaluation Date"). Based on their evaluation, our chief executive officer and chief financial officer have concluded that as of the Evaluation Date, our disclosure controls and procedures are effective to ensure that all material information required to be filed in this Quarterly Report on Form 10-Q has been made known to them in a timely fashion.

#### Changes in Internal Controls

There have been no significant changes (including corrective actions with regard to significant deficiencies or material weaknesses) in our internal controls or in other factors that could significantly affect these controls subsequent to the Evaluation Date set forth above.

### PART II - OTHER INFORMATION

#### Item 1. Legal Proceedings

None

#### Item 2. Changes in Securities and Use of Proceeds

On June 5, 2003, the Company's Board of Directors authorized 10,000,000 shares of preferred stock, par value \$0.001. Such preferred stock, or any series thereof, shall have such designations, preferences, participating, optional or other annual rights and qualifications, limitations or restrictions adopted by the Company's Board of Directors.

In January 2003, 5,000,000 shares previously issuable were issued.

On February 4, 2003, the Company settled a lawsuit by issuing 1,000,000 common shares and \$6,500 in cash. The shares were valued at the quoted trading price of \$0.03 per share on the settlement date resulting in a total settlement expense of \$36,500.

On June 5, 2003, with the approval of the Company's Board of Directors, the authorized number of common shares, \$0.001 par value, issuable by the Company was increased from 100,000,000 to 200,000,000.

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

None

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

##### (a) Exhibits

31.1 Certification of pursuant to Section 302 of the Sarbanes-Oxley



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Act of 2002

32.1 Certification pursuant to Section 906 of the Sarbanes-Oxley  
Act of 2002

Reports on Form 8-K

None

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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.

SUN NETWORK GROUP, INC.

Dated: August 14, 2003

By: /s/ T. Joseph Coleman  
T. Joseph Coleman  
Chief Executive Officer,  
President and Director

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