

HORNE INTERNATIONAL, INC.  
Form 10-Q  
November 08, 2011

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended: September 25, 2011

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

Horne International, Inc.

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

90-0182158  
(I.R.S. Employer  
Identification No.)

3975 University Drive, Suite 100,  
Fairfax, Virginia  
(Address of principal executive offices)

22030  
(Zip Code)

Registrant's telephone number, including area code: 703-641-1100

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, and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large Accelerated filer  Accelerated Filer  Non-Accelerated Filer  Small Reporting Company

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 September 25, 2011, there were 44,506,054 shares of the issuer's common stock, par value \$0.0001 per share, outstanding.

---

HORNE INTERNATIONAL, INC.

TABLE OF CONTENTS

PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets (Unaudited) as of September 25, 2011 and December 26, 2010	2
--	---

Consolidated Statements of Operations (Unaudited) for the three and nine months ended September 25, 2011 and September 26, 2010	3
---	---

Consolidated Statement of Stockholders' Deficit (Unaudited) for the nine months ended September 25, 2011	4
--	---

Consolidated Statements of Cash Flows (Unaudited) for the nine months ended September 25, 2011 and September 26, 2010	5
---	---

Notes to (Unaudited) Consolidated Financial Statements	6
--	---

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	12
---	----

Item 3. Quantitative and Qualitative Disclosures about Market Risk	15
--	----

Item 4. Controls and Procedures	16
---------------------------------	----

PART II - OTHER INFORMATION

Item 1. Legal Proceedings	17
---------------------------	----

Item 1A. Risk Factors	17
-----------------------	----

Item 6. Exhibits	18
------------------	----

HORNE INTERNATIONAL, INC.  
Consolidated Balance Sheets (Unaudited)  
(Dollars shown in 000's except share amounts)

## PART I - FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

	September 25, 2011	December 26, 2010
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 182	\$ 62
Receivables, net	1,073	507
Prepaid expenses and other current assets	38	38
Total current assets	1,293	607
Property and equipment, net	40	67
Other assets	19	59
<b>TOTAL ASSETS</b>	<b>\$ 1,352</b>	<b>\$ 733</b>
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>		
Current liabilities:		
Accounts payable	\$ 1,031	\$ 163
Line of credit	-	140
Accrued expenses	369	554
Deferred revenues	57	60
Current portion of debt	476	505
Current liabilities of discontinued operations	13	215
Total current liabilities	1,946	1,637
Long-term liabilities:		
Non-current portion of debt	6	14
<b>TOTAL LIABILITIES</b>	<b>1,952</b>	<b>1,651</b>
Commitments and contingencies (Note 9)	-	-
Stockholders' deficit		
Preferred stock, \$0.0001 par value; 20,000,000 shares authorized, none issued	-	-
Common stock, \$0.0001 par value; 80,000,000 shares authorized, 44,506,045 and 42,977,893 issued and outstanding	4	4
Additional paid-in capital	79,731	79,571
Accumulated deficit	(80,335 )	(80,493 )
Total stockholders' deficit	(600 )	(918 )
<b>TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT</b>	<b>\$ 1,352</b>	<b>\$ 733</b>

See accompanying notes to (unaudited) consolidated financial statements.



HORNE INTERNATIONAL, INC.  
Consolidated Statements of Operations (Unaudited)  
(Dollars shown in 000's except share and per share amounts)

	Three months ended		Nine months ended	
	September 25, 2011	September 26, 2010	September 25, 2011	September 26, 2010
Revenues	\$1,469	\$ 769	\$3,812	\$ 2,612
Cost of revenues	1,339	569	3,373	1,941
Gross profit	130	200	439	671
Operating expenses	433	292	1,303	1,462
Net operating loss	(303 )	(92 )	(864 )	(791 )
Non-operating expense, net	(15 )	(55 )	(63 )	(107 )
Loss before income taxes	(318 )	(147 )	(927 )	(898 )
Income tax benefit (expense)	-	-	1	(2 )
Loss from continuing operations	(318 )	(147 )	(926 )	(900 )
Income (loss) from discontinued operations	3	2	1,084	(55 )
Net (Loss) Income	\$(315 )	\$ (145 )	\$158	\$ (955 )
Weighted average common shares outstanding:				
Basic and diluted	44,319,895	42,703,325	43,538,190	42,692,716
Basic and diluted income (loss) per share				
Loss from continuing operations	(0.01 )	(0.00 )	(0.02 )	(0.02 )
Income (loss) from discontinued operations	0.00	0.00	0.02	(0.00 )
Total basic and diluted income (loss) per share	\$(0.01 )	\$ (0.00 )	\$0.00	\$ (0.02 )

See accompanying notes to (unaudited) consolidated financial statements.

**HORNE INTERNATIONAL, INC.**  
**Consolidated Statement of Stockholders' Deficit (Unaudited)**  
**For the Nine Months Ended September 25, 2011**  
 (Dollars shown in 000's except share amounts)

	Common Stock			Accumulated	
	Shares	Amount	APIC	Deficit	Total
Balance as of December 26, 2010	42,977,893	\$4	\$79,571	\$ (80,493 )	\$(918 )
Net income				158	158
Stock option expense			38		38
Restricted stock issued	1,528,152		122		122
Balance as of September 25, 2011	44,506,045	\$4	\$79,731	\$ (80,335 )	\$(600 )

See accompanying notes to the (unaudited) consolidated financial statements.

HORNE INTERNATIONAL, INC.  
Consolidated Statements of Cash Flows (Unaudited)  
For the Nine Months Ended September 25, 2011 and September 26, 2010  
(Dollars shown in 000's except share amounts)

## Statement of Cash Flows

	Nine Months Ended	
	September 25, 2011	September 26, 2010
<b>Cash flows from operating activities:</b>		
<b>Continuing Operations</b>		
Net loss from continuing operations	\$(926 )	\$ (900 )
Adjustments to reconcile net loss to net cash flows		
<b>Cash used in operating activities</b>		
Stock-based compensation	38	519
Issuance of common stocks	122	10
Depreciation and Amortization	28	24
Gain on disposal of equipment	-	2
Change in balance sheet items		
Receivables, net	(566 )	557
Prepaid expenses	-	(5 )
Accounts payable	869	(224 )
Accrued expenses	(185 )	(58 )
Deferred revenue	(3 )	3
Other liabilities	-	30
Other assets	40	(3 )
Net cash used in continuing operations	(583 )	(45 )
<b>Discontinued Operations</b>		
Net income (loss) from discontinued operations	1,084	(55 )
Cash used in discontinued operations	(202 )	-
Net cash provided by (used in) discontinued operations	882	(55 )
Net cash provided by (used in) operations	299	(100 )
<b>Cash flows from investing activities:</b>		
Purchase of property and equipment	(2 )	(30 )
Net cash used in investing activities	(2 )	(30 )
<b>Cash flows from financing activities:</b>		
Cash repayments on capital lease	(7 )	-
Net (repayments) borrowings on lines of credit	(140 )	117
Proceeds from related party debt	310	-
Payments on related party debt	(340 )	-
Net cash (used in) provided by financing activities	(177 )	117
Net increase(decrease) in cash and cash equivalents	120	(13 )
Cash and cash equivalents at beginning of period	62	15
Cash and cash equivalents at end of period	\$182	\$ 2



Supplemental disclosure of cash flow information:

Cash paid for interest	\$62	\$ 42
Cash paid for taxes	\$1	\$ 2

See accompanying notes to the (unaudited) consolidated financial statements.

HORNE INTERNATIONAL, INC.  
Notes to Consolidated Financial Statements (Unaudited)

1. ORGANIZATION AND NATURE OF BUSINESS AND UNCERTAINTY

Horne International, Inc. (the “Company” or “we”, “us”, “our” or similar terms), headquartered in Fairfax, Virginia, is an engineering services company focused on provision of integrated, systems approach based solutions to the energy and environmental sectors. The Company’s solutions are sustainable, agile, and provide immediate as well as long term results. The Company’s service and product offerings encompass engineering, environment, and energy. We provide products and services to both commercial customers and to the United States Government.

Discontinued operations include the results of our Spectrum subsidiary that were closed in June 2008.

The Company’s independent registered public accountants stated in their report on the consolidated financial statements of the Company for the year ended December 26, 2010, that the Company has had recurring operating losses that raise substantial doubt about its ability to continue as a going concern. For the nine months ended September 25, 2011, the Company incurred a loss from continuing operations of approximately \$926,000 and had a stockholders’ deficit of approximately \$600,000 as of that date. The Company recognized \$1,084,000 income from discontinued operations for the nine months ended September 25, 2011. The consolidated financial statements do not include any adjustments related to the recovery and classification of recorded assets, or the amounts and classification of liabilities that might be necessary in the event the Company cannot continue as a going concern.

The Company is dependent upon available cash and operating cash flow to meet its capital needs. The Company is considering all strategic options to improve its liquidity and provide it with working capital to fund its continuing business operations which include equity offerings, assets sales or debt financing as alternatives to improve its cash requirements.

In December 2009, the Company entered into a two-year receivable noncancellable financing agreement with Wells Fargo Bank National Association under which the Company was able to factor certain eligible accounts receivable. The Company replaced this agreement with a new factoring agreement with United Capital Funding at the end of the first quarter of 2011. The new agreement with United Capital funding allows the Company to factor eligible accounts receivable up to \$500,000.

During 2008, the Company entered into a loan agreement with Darryl K. Horne, the Company’s President and Chairman. The loan permitted the Company to borrow up to \$525,000 at 8 percent interest. The company has repaid \$220,000 during the nine months ending September 25, 2011. As of September 25, 2011, the outstanding balance is \$275,000.

On March 22, 2010, the Company entered into a strategic partnership with Intelligent Decisions, Inc. (“Intelligent”), an information technology services company headquartered in Ashburn, Virginia, servicing both commercial and government customers. The agreement between the parties provides for a cash line of credit to the Company in the amount of \$250,000 for business/projects jointly developed by Intelligent and the Company. This line of credit will be secured by the Company’s eligible Accounts Receivable as decided by Intelligent in its sole discretion. No cash will be advanced by Intelligent until Intelligent receives a perfected security interest (i.e., first lien on the orders to be advanced under this cash line of credit). As of September 25, 2011, the outstanding balance is zero.

In March 2011, the Company entered into a receivables financing agreement with Evan Auld-Susott, the company’s Chief Executive Officer, as agent of the Susott Family Limited Partnership. Under the terms of the agreement, Mr. Auld-Susott agreed to finance specific accounts receivable under a line of credit for up to \$500,000 at an interest rate

of 13 percent. The Company has taken draws of \$310,000 and repaid \$120,000 during the nine months ending September 25, 2011. As of September 25, 2011, the outstanding balance is \$190,000. The loan is not convertible into any Company securities.

On January 21, 2011, the Company received notification that the United States Court of Federal Claims had published its ruling on damages in the matter of Spectrum Sciences and Software, Inc. vs. The United States, Case Number 04-1366C, the Munitions Assembly Conveyor (MAC) Lawsuit. The Court awarded Spectrum Sciences and Software, Inc., a subsidiary of Horne International, Inc. damages in the amount of One Million Two Hundred Thousand Dollars (\$1,200,000) plus legal costs. The Company recognized \$1,084,000 in net income from discontinued operations for the nine months ended September 25, 2011 which reflected an award of \$1,211,754 plus an Equal Access to Justice Act estimate of \$340,000 less the cost of litigation of \$470,754.

HORNE INTERNATIONAL, INC.  
Notes to Consolidated Financial Statements (Unaudited)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Basis of Presentation

The consolidated financial statements of Horne International, Inc. include accounts of the Company and its wholly-owned subsidiaries. Intercompany transactions and balances are eliminated in consolidation.

The accompanying unaudited consolidated financial statements for the nine-month periods ended September 25, 2011, and September 26, 2010 have been prepared in accordance with accounting principles generally accepted in the United States of America 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 of the information and disclosures required by generally accepted accounting principles 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 three and nine month periods ended September 25, 2011 are not necessarily indicative of the results that may be expected for the year. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and related footnotes included in the Company's Annual Report on Form 10-K for the year ended December 26, 2010.

Revenue Recognition

The Company's two principal methods of revenue recognition are monthly fixed price contracts in which revenue is recognized ratably over the contract period and time and materials contracts in which revenue is recognized as costs are incurred.

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 basis 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.

The Company currently has a net operating loss carry forward of approximately \$55 million at September 25, 2011. The Company has not recorded any related federal tax benefit in the accompanying consolidated financial statements, due to the possibility that the net operating loss carry forward may not be utilized, for various reasons, including the potential that the Company might not have sufficient profits to use the carry forward or the carry forward may be limited as a result of changes in the Company's equity ownership. The Company adopted Accounting Standards Codification topic 740, subtopic 10 on January 1, 2007, which requires financial statement benefits to be recognized for positions taken for tax return purposes when it is more-likely-than-not that the position will be sustained. There has been no change in our financial position and results of operation due to the adoption of this standard.



HORNE INTERNATIONAL, INC.  
Notes to Consolidated Financial Statements (Unaudited)

### Income (Loss) Per Share

Basic income (loss) per share is calculated by dividing net loss by the weighted-average number of common shares outstanding during the reporting period. Diluted income (loss) per share is computed in a manner consistent with that of basic loss per share 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 of 7,654,660 and 10,468,333 were not included in the computation of diluted income (loss) per share for the nine months ended September 25, 2011, and September 26, 2010, respectively, as the inclusion of these common stock equivalents would have been anti-dilutive.

### Stock-based Compensation

The fair values of stock option awards are determined using the Black-Sholes option pricing model. The compensation expense is recognized on a straight-line basis over the vesting period. The Company, beginning in 2006, has included a vesting period for most options granted. See Note 7 for a detailed discussion of the Company's stock option plan. The Company accounts for stock incentive plans by measurement and recognition of compensation expense for all share-based awards on estimated fair values, net of estimated and actual forfeitures, on a straight line basis over the period during which the employee is required to provide services in exchange for the award.

### Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

### Fair Value of Financial Instruments

The carrying amount of cash and cash equivalents, receivables, accounts payable and accrued expenses approximates fair value because of the short-term nature of those instruments. The carrying amount and fair market value of the Company's short-term investments are the same since short-term investments are recorded at fair value. Debt is recorded at the cash settlement value of the underlying notes and is not revalued.

### Use of Estimates

The 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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Accordingly, results could differ from those estimates and assumptions.

### Recent Accounting Pronouncements

ASU 2010-06, "Improving Disclosure about Fair Value Measurements," was issued January 2010 and requires additional disclosures regarding fair value measurements, amends disclosures about post-retirement benefit plan assets and provides clarification regarding the level of disaggregation of fair value disclosures by investment class. The ASU is effective for interim and annual reporting periods beginning after December 15, 2009, except for certain Level 3 activity disclosure requirements that were effective for reporting periods beginning after December 15, 2010.

Adoption of ASU 2010-06 had no material impact on our consolidated financial statements.

In May 2011, the FASB issued a new accounting standard on fair value measurements that clarifies the application of existing guidance and disclosure requirements, changes certain fair value measurement principles and requires additional disclosures about fair value measurements. The standard is effective for interim and annual periods beginning after December 15, 2011. Early adoption is not permitted. We do not expect this adoption to have a material impact on our financial statements.

In June 2011, the FASB issued a new accounting standard on the presentation of comprehensive income. The new standard requires the presentation of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The new standard also requires presentation of adjustments for items that are reclassified from other comprehensive income to net income in the statement where the components of net income and the components of other comprehensive income are presented. The standard is effective for fiscal years, and interim periods within these years, beginning after December 15, 2011. Early adoption is permitted. The adoption of this standard will have no material impact on our financial statements.

HORNE INTERNATIONAL, INC.  
Notes to Consolidated Financial Statements (Unaudited)

From time to time, new accounting pronouncements are issued by FASB or other standards setting bodies that are adopted by the Company as of the specified effective date. Unless otherwise discussed, the Company believes the impact of recently issued standards that are not yet effective will not have a material impact on its consolidated financial position, results of operations and cash flows upon adoption.

### 3. RECEIVABLES (000's)

Receivables primarily comprise of amounts due to the Company for work performed on contracts directly related to commercial and government customers. The Company has a nominal bad debt reserve as most of our contracts are with governmental entities.

Unbilled receivables represent recoverable costs and estimated earnings consisting principally of contract revenues that have been recognized for accounting purposes but are not yet billable to the customer based upon the respective contract terms.

	September 25, December 26, 2011                      2010	
<b>Accounts Receivable</b>		
Billed AR	\$ 1,000	\$ 420
Unbilled AR	64	77
Holdbacks	11	11
Bad Debt Reserve	(1 )	(1 )
Total Accounts Receivable, Net	\$ 1,074	\$ 507

### 4. PROPERTY AND EQUIPMENT (000's)

	September 25, December 26, 2011                      2010	
<b>Property and Equipment</b>		
Buildings and Improvements	\$ 5	\$ 5
Furniture and Fixtures	11	11
Office Equipment	304	303
Total	\$ 320	\$ 319
Accumulated Depreciation	(280 )	(252 )
Property and Equipment, net	\$ 40	\$ 67

### 5. RELATED PARTY BORROWINGS

The Company's borrowings consist of related party receivable financing and unsecured notes of approximately \$465,000 as of September 25, 2011 and \$495,000 as of December 26, 2010.

#### Darryl Horne Notes

During 2008, the Company entered into a loan agreement with Darryl K. Horne, the Company's President. The agreement permitted the Company to borrow up to \$525,000 at an 8 percent interest rate. The interest is payable quarterly beginning in July 1, 2008, with principal payable upon demand. The note is unsecured and is not convertible



into any Company securities. The Company has repaid \$220,000 during the nine months ending September 25, 2011. As of September 25, 2011, the outstanding balance is \$275,000 and accrued interest is zero.

**Evan Auld-Susott Notes**

In March 2011, the Company entered into a receivables financing agreement with Evan Auld-Susott, the Company's Chief Executive Officer, as agent of the Susott Family Limited Partnership. Under the terms of the agreement, Mr. Auld-Susott agreed to finance specific accounts receivable under a line of credit for up to \$500,000 at an interest rate of 13 percent. The Company has taken draws of \$310,000 and repaid \$120,000 during the period ending September 25, 2011. The outstanding balance and accrued interest is \$190,000 and zero, respectively, as of September 25, 2011. The loan is not convertible into any Company securities.

HORNE INTERNATIONAL, INC.  
Notes to Consolidated Financial Statements (Unaudited)

## 6. LINES OF CREDIT

In March 2011, the Company terminated its financing agreement with Wells Fargo Bank National Association under which the Company was able to factor certain eligible accounts receivable. The Company replaced this agreement with a new factoring agreement with United Capital Funding Corporation at the end of the first quarter of 2011. The agreement with United Capital funding allows the Company to factor eligible accounts receivable up to \$500,000. As of September 25, 2011 and December 26, 2010, the outstanding amount under this factoring arrangement is zero and \$140,000 respectively.

## 7. STOCK OPTION PLAN

On March 22, 2010, the Company entered into a strategic partnership with Intelligent Decisions, Inc. (“Intelligent”). Intelligent is an information technology services company headquartered in Ashburn, Virginia, servicing both commercial and government customers. The agreement between the parties provides for Intelligent to provide business support services to the Company. In return for business support services, the Company awarded to Intelligent 8,333,333 options to purchase common stock and will award up to 12,500,000 additional restricted stock units. During 2010, Company awarded Intelligent 290,569 restricted stock units in exchange for business support services and recorded \$515,884 of stock-based compensation expense related to options. On June 17, 2011, the Stock Option Agreement was amended and the second tranche of 4,166,666 of the original 8,333,333 option shares originally issued to Intelligent were cancelled. During the nine months ended September 25, 2011, the Company awarded 1,523,151 restricted stock units in exchange for business support services and recorded \$0 of stock-based compensation expense related to these options.

The Company has a stock option plan available to eligible employees, non-employee directors, consultants and advisors to acquire proprietary interests in the Company by providing eligible persons an additional incentive to promote the success of the Company as deemed appropriate by senior management. This is accomplished by providing for the granting of Non-Statutory Stock Options to employees, non-employee directors, consultants and advisors. During the first nine months of 2011, the Company granted 300,000 shares of stock options to three members of the Advisory Board and 30,000 shares of stock options to one member of the Board Directors. The Company granted approximately 598,000 shares of stock options to current employees. These stock options vest over time and under certain conditions. During the nine months ended September 25, 2011, the Company recorded approximately \$38,000 of stock based compensation expense related to these options.

The fair values of stock option awards are determined using the Black-Sholes option pricing model. The compensation expense is recognized on a straight-line basis over the vesting period. The Company, beginning in 2006, has included a vesting period for most options granted.

The table below summarizes our stock option activity during the nine months ended September 25, 2011.

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Life (yrs)	Aggregate Intrinsic Value
Options Outstanding 12/26/2010	10,393,333	0.09	4.04	-
Granted	1,452,993	0.20	2.64	-
Exercised	(5,000 )	-	-	-
Cancelled	(4,186,666 )	0.09	-	-
Options Outstanding 9/25/2011	7,654,660	\$ 0.12	3.78	\$ 679,600

Edgar Filing: HORNE INTERNATIONAL, INC. - Form 10-Q

Options Exercisable 9/25/2011	6,226,667	\$ 0.09	4.04	\$ 646,000
-------------------------------	-----------	---------	------	------------

10

---

HORNE INTERNATIONAL, INC.  
Notes to Consolidated Financial Statements (Unaudited)

## 8. DISCONTINUED OPERATIONS

The Company made the strategic decision to close the operations of its Spectrum Sciences and Software, Inc. (SSSI), and Coast Engine & Equipment Co., subsidiaries in early 2008. Accordingly, the operating results of these two entities are included in discontinued operations for all years presented.

The Company recognized \$1,081,000 in net income in the 2nd quarter of 2011 from a judgment in the matter of Spectrum Sciences and Software, Inc. vs. The United States, Case Number 04-1366C. The net income reflects an award of \$1,211,754 plus an Equal Access to Justice Act estimate of \$340,000 less the cost of litigation (\$470,754).

## 9. COMMITMENTS AND CONTINGENCIES

### Operating Leases

The Company leases office space at various locations in the United States. The Company also enters into various other non-cancellable leases for office equipment as necessary.

The table below summarizes our future annual minimum lease payments under non-cancellable agreements with an initial term of greater than one year at inception. (000's)

	2011	2012	2013
Operating Leases	\$ 37	\$ 73	\$ -

### Capital Leases

The Company updated its corporate office phone system in March 2010. The Company entered into a three-year lease agreement with a \$1 buyout option for the phone system with AVAYA Financial Services. This lease requires a monthly payment of \$1,010 plus all applicable taxes.

The table below summarizes our future annual minimum lease payments under this non-cancellable agreement with an initial term of greater than one year at inception. (000's)

	2011	2012	2013
Capital Leases	\$ 3	\$ 12	\$ 3

### Legal Matters

Our outstanding legal proceedings as of December 26, 2010 are described in Note 14 to our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 26, 2010. On January 21, 2011, the Company received notification that the United States Court of Federal Claims had published its ruling on damages in the matter of Spectrum Sciences and Software, Inc. vs. The United States, Case Number 04-1366C, the Munitions Assembly Conveyor (MAC) Lawsuit. The Court awarded Spectrum Sciences and Software, Inc., a subsidiary of Horne International, Inc. damages in the amount of One Million Two Hundred Thousand Dollars (\$1,200,000) plus legal costs. The Company recognized \$1,081,000 in net income from discontinued operation in the second quarter of 2011 which reflected an award of \$1,211,754 plus Equal Access to Justice Act estimate of \$340,000 less the cost of litigation of \$470,754.

SUBSEQUENT EVENTS (Reserved)

11

---

HORNE INTERNATIONAL, INC.

Management's Discussion and Analysis of Financial Condition and Results of Operations

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

The following discussion provides information which management believes is relevant to an assessment and an understanding of the Company's operations and financial condition. This discussion should be read in conjunction with the attached unaudited consolidated financial statements and accompanying notes as well as our annual report on Form 10-K for the fiscal year ended December 26, 2010.

FORWARD-LOOKING STATEMENTS

The matters discussed in this Quarterly Report on Form 10-Q 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 use these 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," contained in our Annual Report of Form 10-K for the fiscal year ended December 26, 2010, as well as any cautionary language in this Form 10-Q, 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 this Form 10-Q. Subsequent events and developments may cause our views to change. While we may elect to update the forward-looking statements at some point in the future, we specifically disclaim any obligation to do so.

DESCRIPTION OF THE COMPANY

The Company provides a variety of services through its wholly-owned subsidiary, Horne Engineering Services, LLC. The Company focuses on providing program engineering, energy solutions, occupational safety and health, environmental sciences, acquisition and procurement, business process engineering, public outreach, and product solutions. Our primary customer in this segment is the U.S. Government, with specific focus within the Departments of Homeland Security, Defense, Transportation and other civilian agencies.

In March 2011, the Company signed a reseller agreement with the IT product and professional services company ThoughtWorks, Inc., a global leader in Lean and Agile products and training. The Company expects this capability to enable it to further its goal of being a total solutions provider to its customers.

The Company was awarded a five-year GSA Schedule 70 contract effective April 15th, 2011. This contract allows the Company to provide federal customers with high-value Lean and Agile software development process solutions.

In May 2011, the Company signed a marketing and reseller agreement with G2 Environmental Technologies, LLC to provide Enerburn®, a diesel fuel combustion catalyst, to government customers.

#### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

In our Form 10-K for the fiscal year ended December 26, 2010, our most critical accounting policies and estimates upon which our financial status depends were identified as those relating to revenue recognition, stock-based compensation, net operating losses and tax credit carryforwards, and impairment of long-lived assets. We reviewed our policies and determined that those policies remain our most critical accounting policies for the three and nine months ended September 25, 2011.

## HORNE INTERNATIONAL, INC.

## Management's Discussion and Analysis of Financial Condition and Results of Operations

## COMPARISON OF THREE MONTHS ENDED SEPTEMBER 25, 2011, AND SEPTEMBER 26, 2010

The following discussion and analysis should be read in conjunction with the unaudited financial statements (and notes thereto) and other financial information of the Company appearing elsewhere in this report.

## Consolidated Overview (000's)

	Three months ended					
	September 25, 2011			September 26, 2010		
Total revenue	\$ 1,469	100.0 %		\$ 769	100.0 %	
Gross profit	130	8.8 %		200	26.0 %	
Operating loss	(303 )	-20.6 %		(92 )	-12.0 %	

Revenue for the quarter ended September 25, 2011, increased by approximately \$700,000, as compared to the quarter ended September 26, 2010. The main driver of revenue increase was new task orders under our Army Corps of Engineers (ACE) contract. Gross profit as a percentage of revenue declined due to the significant amount of low margin revenues. The overall operating loss increased in the third quarter of 2011 compared to the third quarter of 2010 primarily due to the significant amount of low margin revenues.

## COMPARISON OF NINE MONTHS ENDED SEPTEMBER 25, 2011, AND SEPTEMBER 26, 2010

The following discussion and analysis should be read in conjunction with the unaudited financial statements (and notes thereto) and other financial information of the Company appearing elsewhere in this report.

## Consolidated Overview (000's)

	Nine months ended					
	September 25, 2011			September 26, 2010		
Total revenue	\$ 3,812	100.0 %		\$ 2,612	100.0 %	
Gross profit	439	11.1 %		671	25.7 %	
Operating loss	(864 )	-22.7 %		(791 )	-30.3 %	

Revenue for the nine months ended September 25, 2011, increased by approximately \$1,200,000, as compared to the nine months ended September 26, 2010. The main driver of revenue increase was new task orders under our Army Corps of Engineers (ACE) contract. Gross profit as a percentage of revenue declined due to the significant amount of low margin revenues. The overall operating loss increased in the first nine months of 2011 compared to the first nine months of 2010 primarily due to the significant amount of low margin revenues.

## Discontinued Operations

Discontinued operations include the result of Spectrum Sciences & Software, Inc. subsidiary that was closed in June 2008. Net income of \$1,084,000 from discontinued operations was the result of the legal judgment described in note 8 to our unaudited consolidated financial statements contained in this Report.

## Liquidity and Capital Resources



Cash and cash equivalents totaled approximately \$182,000 at September 25, 2011. The Company received a judgment award of \$1,211,754 the Munitions Assembly Conveyor (MAC) Lawsuit in June 2011 and \$340,000 in legal costs in September, 2011. The Company made payments of \$633,135 against the costs of litigation and repaid related parties debt of \$340,000. Our overall cash position has increased by approximately \$133,000 since year-end primarily due to the proceeds from the MAC legal judgment.

During 2008, the Company entered into a loan agreement with Darryl K. Horne, the Company's President. The agreement permitted the Company to borrow up to \$525,000 at 8 percent interest rate. The interest is payable quarterly beginning in July 1, 2008, with principal payable upon demand. The note is unsecured and is not convertible into any Company securities. As of September 25, 2011, the outstanding balance and accrued interest is \$275,000 and zero respectively.

HORNE INTERNATIONAL, INC.

Management's Discussion and Analysis of Financial Condition and Results of Operations

On August 6, 2008, the Company entered into a receivables financing agreement with Mr. Horne. Under the terms of the agreement, Mr. Horne agreed to finance specific accounts receivable under a line of credit for up to \$790,000 at an interest rate of 8.5 percent. As of September 25, 2011 and December 26, 2010, the outstanding balance is \$0 and \$220,000 respectively.

In March 2011, the Company entered into a receivables financing agreement with Evan Auld-Susott, the Company's Chief Executive Officer, as agent of the Susott Family Limited Partnership. Under the terms of the agreement, Mr. Auld-Susott agreed to finance specific accounts receivable under a line of credit for up to \$500,000 at an interest rate of 13 percent. The Company has taken draws of \$310,000 and repaid \$120,000 during the second quarter of 2011. The outstanding balance and accrued interest is \$190,000 and zero respectively as of September 25, 2011. The loan is not convertible into any Company securities.

In March 2011, the Company entered into a financing agreement with United Capital Funding Corporation under which the Company is able to factor certain eligible accounts receivable up to \$500,000. The agreement calls for a fee of .425 percent of the factored amount for each 5 day period that the amount is outstanding. The Company is able to receive 80 percent of any invoices factored to the lender. As of September 25, 2011, there is no balance outstanding under this financing agreement.

On March 22, 2010, the Company entered into a strategic partnership with Intelligent. The partnership provides for the Company to have a cash line of credit in the amount of \$250,000 against business/projects jointly developed by Intelligent and the Company. This line of credit will be secured by the Company's eligible Accounts Receivable on such projects or on the receivables from the Company's full-time equivalent employees arising after the inception of the partnership that are billed against projects as decided by Intelligent in its sole discretion. No cash will be advanced by Intelligent until Intelligent receives a perfected security interest (i.e., first lien on the orders to be advanced under this cash line of credit). As of September 25, 2011, no funds have been advanced to the Company under this line of credit.

As discussed in our 2010 Form 10-K, the Company has substantial liquidity challenges. While we continue to work towards profitability, there is a significant uncertainty that the Company will have sufficient cash flow to sustain its operations.

The Company continues to pursue additional funding sources in the event that funds from operations and financing are not sufficient to provide for our operations. These funding sources would primarily be in the form of bank credit lines. Given our past financial performance, the costs and fees associated with funding sources may be more expensive than the Company has historically paid. The Company can not determine if the funds available from operations will be sufficient for any acquisitions or facility expansions that may be undertaken during the year. Should the Company make any acquisitions or expansions, other sources of financing may be required.

HORNE INTERNATIONAL, INC.

Quantitative and Qualitative Disclosures about Market Risk

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In addition to the risks inherent in our operations, we are exposed to contractual, financial, market, political and economic risks. The following discussion provides additional detail regarding our exposure to interest rates and foreign exchange rates.

Government Contracts

The funding of U.S. government programs is subject to Congressional appropriations. Although multi-year contracts may be authorized in connection with major procurements, Congress generally appropriates funds on a fiscal-year basis, even though a program may continue for many years. Consequently, programs are often only partially funded initially, and additional funds are committed only as Congress makes further appropriations. Provisions in these contracts permit termination, in whole or in part, without prior notice, at the government's convenience or upon contractor default under the contract. Compensation in the event of a termination, if any, is limited to work completed at the time of termination. In the event of termination for convenience, the contractor may receive a certain allowance for profit on the work performed.

Interest Rate Risk

At September 25, 2011, the Company had a revolving credit facility. We have not historically mitigated our exposure to fluctuations in interest rates by entering into interest rate hedge agreements, nor do we have any plans to do so in the immediate future.

Foreign Exchange Risk

We currently do not have any foreign currency risk and accordingly, estimate that an immediate 10 percent change in foreign exchange rates would have no impact on our reported net loss. We do not currently utilize any derivative financial instruments to hedge foreign currency risks.

HORNE INTERNATIONAL, INC.

Controls and Procedures

ITEM 4. CONTROLS AND PROCEDURES

Based on management's evaluation (with the participation of our Chief Executive Officer (CEO) and Chief Financial Officer (CFO)), as of the end of the period covered by this report, our CEO and CFO have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), are effective to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

HORNE INTERNATIONAL, INC.

Other Information

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Our outstanding legal proceedings as of December 26, 2010 are described in Note 14 to our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 26, 2010. On January 21, 2011, the Company received notification that the United States Court of Federal Claims had published its ruling on damages for the Munitions Assembly Conveyor (MAC) Lawsuit. The Court awarded Spectrum Sciences and Software, Inc., a subsidiary of Horne International, Inc. damages in the amount of One Million Two Hundred Thousand Dollars (\$1,200,000) plus legal costs. The Company recognized \$1,081,000 in net income in the 2nd quarter of 2011 which reflected an award of \$1,211,754 plus an Equal Access to Justice Act estimate of \$340,000 less the cost of litigation (\$470,754).

Item 1A. Risk Factors.

We are subject to several risk factors that could have a direct and material impact on the operations of the Company and the market price of our common stock. Those risk factors are disclosed in our 2010 Form 10-K.

## HORNE INTERNATIONAL, INC.

## Exhibits

## ITEM 6. EXHIBITS

Exhibit Number	Description
3.1	Certificate of Incorporation, filed August 28, 1998 (previously filed in registration statement on Form 10-SB File No. 1-31710, filed with the Securities and Exchange Commission on June 10, 2003).
3.2	Certificate of Renewal and Revival, filed March 24, 2003 (previously filed in registration statement on Form 10-SB File No. 1-31710, filed with the Securities and Exchange Commission on June 10, 2003).
3.3	Certificate of Amendment of Certificate of Incorporation, filed April 8, 2003 (previously filed in registration statement on Form 10-SB File No. 1-31710, filed with the Securities and Exchange Commission on June 10, 2003).
3.4	Certificate of Merger filed with the Delaware Secretary of State (previously filed in registration statement on Form 10-SB File No. 1-31710, filed with the Securities and Exchange Commission on June 10, 2003).
3.5	Articles of Merger filed with the Florida Secretary of State (previously filed in registration statement on Form 10-SB File No. 1-31710, filed with the Securities and Exchange Commission on June 10, 2003).
3.6	Amended and Restated Bylaws of Spectrum Sciences & Software Holdings Corp., as amended (previously filed on Form 10-Q, filed with the Securities and Exchange Commission on November 14, 2005).
3.7	Amended and Restated Bylaws of Spectrum Sciences & Software Holdings Corp., as amended (previously filed on Form 8-K, filed with the Securities and Exchange Commission on May 2, 2006).
3.8	Amended Articles of Incorporation of Horne International, Inc. (previously filed on Form 8-K, filed with the Securities and Exchange Commission on September 6, 2006).
4.1	Specimen Certificate of Common Stock (previously filed in registration statement on Form 10-SB File No. 1-31710, filed with the Securities and Exchange Commission on June 10, 2003).
10.1	Employment Agreement, dated as of May 11, 2005, by and between Spectrum Sciences & Software Holdings Corp. and Darryl K. Horne (previously filed on Form 8-K, filed with the Securities and Exchange Commission on March 17, 2005).
10.2	First Amendment to Employment Agreement, dated as of May 23, 2005, by and between Spectrum Sciences & Software Holdings Corp. and Darryl K. Horne (previously filed on Form 8-K, filed with the Securities and Exchange Commission on May 27, 2005).
10.3	2004 Non-Statutory Stock Option Plan, dated March 11, 2004 (previously filed on Form 8-K, filed with the Securities and Exchange Commission on March 12, 2004).
10.4	Amended and Restated Number 1 2004 Non-Statutory Stock Option Plan, dated April 16, 2004 (previously filed on Form S-8, filed with the Securities and Exchange Commission on April 21, 2004).
10.5	Amended and Restated Number 2 2004 Non-Statutory Stock Option Plan, dated November 15, 2004 (previously filed on Form 8-K, filed with the Securities and Exchange Commission on November 19, 2004).
10.6	Stock Option Agreement between Spectrum Sciences & Software Holdings Corp. and Darryl K. Horne, dated May 11, 2005 (previously filed on Form 8-K, filed with the Securities and Exchange



HORNE INTERNATIONAL, INC.

Exhibits

- 10.7 Form of Stock Option Agreement between Spectrum Sciences & Software Holdings Corp. and each of Darryl K. Horne and Michael M. Megless, dated June 8, 2005 (previously filed on Form 8-K, filed with the Securities and Exchange Commission on June 13, 2005).
- 10.8 Receivables financing agreement, dated August 6, 2008 by and between Horne International, Inc. and Darryl K. Horne. (previously filed with the Securities and Exchange Commission on November 6, 2008).
- 10.9 Stock Option Agreement, dated as of March 23, 2010 by and between Horne International, Inc. and Intelligent Decisions, Inc. (previously filed with the Securities and Exchange Commission on May 12, 2010).
- 10.10 Restricted Stock Agreement between Horne International, Inc. and Intelligent Decisions, Inc. (previously filed with the Securities and Exchange Commission on August 10, 2010).
- 10.11 Amendment to Horne International, Inc. Stock Option Plan (previously filed with the Securities and Exchange Commission on August 10, 2010).
- 10.12 Receivables financing agreement, dated March 28, 2011 by and between Horne International, Inc. and Evan Auld-Susott (previously filed with the Securities and Exchange Commission on May 10, 2011).
- 10.13 Receivables financing agreement between Horne International, Inc. and United Capital Funding (previously filed with the Securities and Exchange Commission on May 10, 2011).
- 14.1 Code of Ethics (previously filed on Form 10-KSB, filed with the Securities and Exchange Commission on April 13, 2004).
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 32.1 Certification of Chief Executive Officer & Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).



HORNE INTERNATIONAL, INC.

Exhibits

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, on this 8th day of November 2011.

HORNE INTERNATIONAL, INC.

By: /s/ Evan Auld-Susott  
Evan Auld-Susott  
Chief Executive Officer

By: /s/ Lily L. Xu  
Lily L. Xu  
Chief Financial Officer