METRO ONE TELECOMMUNICATIONS INC
Form 10-Q
November 14, 2006

United States
Securities and Exchange Commission

Washington, D.C. 20549

Form 10-Q

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

For the Quarterly Period Ended September 30, 2006

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

Commission File Number 0-27024

METRO ONE TELECOMMUNICATIONS, INC.

(Exact name of registrant as specified in its charter)

OREGON	**93-0995165**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

11200 Murray Scholls Place, Beaverton, Oregon 97007

(Address of principal executive offices) (zip code)

(503) 643-9500

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant has (1) 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 Noo

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. (Check one):

Large accelerated filer o Accelerated filer o Non-accelerated filer x

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

Number of shares of common stock outstanding as of November 10, 2006: 6,233,326 shares, no par value per share.

METRO ONE TELECOMMUNICATIONS, INC.

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Metro One Telecommunications, Inc.
Condensed Consolidated Statements of Operations (Unaudited)

(In thousands, except per share data)	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Revenues	$ 5,205	$ 19,211	$ 25,553	$ 57,739
Costs and expenses:				
Direct operating	3,789	15,390	15,319	47,353
Selling, general and administrative	4,465	11,255	16,813	36,579
Depreciation and amortization	686	1,528	3,040	4,734
Restructuring charges	453	2,745	6,230	4,020
	9,393	30,918	41,402	92,686
Loss from operations	(4,188)	(11,707)	(15,849)	(34,947)
Other income, net	187	235	599	804
Loss before income taxes	(4,001)	(11,472)	(15,250)	(34,143)
Income tax expense		423	50	343
Net loss	$ (4,001)	$ (11,895)	$ (15,300)	$ (34,486)
Net loss per common share:				
Basic	$ (.64)	$ (1.90)	$ (2.45)	$ (5.50)
Diluted	$ (.64)	$ (1.90)	$ (2.45)	$ (5.50)
Weighted average shares outstanding:				
Basic	6,233	6,254	6,233	6,268
Diluted	6,233	6,254	6,233	6,268

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

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Metro One Telecommunications, Inc.
Condensed Consolidated Balance Sheets (Unaudited)

(In thousands)	September 30, 2006	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	$ 12,833	$ 17,769
Restricted cash	5,716	6,860
Accounts receivable, net	2,837	11,982
Prepaid costs and other current assets	1,438	1,759
Total current assets	22,824	38,370
Furniture, fixtures and equipment, net	3,662	7,963
Intangible assets	4,857	5,382
Other assets	134	302
Total assets	$ 31,477	$ 52,017
Liabilities and Shareholders Equity		
Current liabilities:		
Accounts payable	$ 539	$ 534
Accrued liabilities	1,548	2,637
Accrued payroll and related costs	4,361	8,553
Total current liabilities	6,448	11,724
Other long-term liabilities	569	626
Total liabilities	7,017	12,350
Commitments and contingencies		
Shareholders equity:		
Preferred stock, no par value; 2,500 shares authorized, no shares issued or outstanding		
Common stock, no par value; 12,500 shares authorized, 6,233 shares and 6,237 issued and outstanding at September 30, 2006 and December 31, 2005, respectively	120,029	119,937
Accumulated deficit	(95,569)	(80,270)
Total shareholders equity	24,460	39,667
Total liabilities and shareholders equity	$ 31,477	$ 52,017

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

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Metro One Telecommunications, Inc.
Condensed Consolidated Statements of Cash Flows (Unaudited)

(In thousands)	Nine Months Ended September 30, 2006	2005
Cash flows from operating activities:		
Net loss	$ (15,300)	$ (34,486)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	3,040	4,734
Loss on disposal of fixed assets, net	1,117	160
Deferred charges, net	56	382
Stock-based compensation expense	92	
Changes in assets and liabilities:		
Accounts receivable	9,146	4,395
Prepaid costs and other assets	575	774
Accounts payable and other liabilities	(5,390)	(679)
Net cash used in operating activities	(6,664)	(24,720)
Cash flows from investing activities:		
Decrease (increase) in cash restricted to secure letter of credit	1,144	(1,960)
Purchases of short-term securities		(36,805)
Sales of short-term securities		62,180
Capital expenditures	(233)	(1,682)
Proceeds from sale of assets	817	69
Net cash provided by investing activities	1,728	21,802
Cash flows from financing activities:		
Common stock repurchased		(121)
Proceeds from employee stock purchases		103
Net cash used in financing activities		(18)
Net decrease in cash and cash equivalents	(4,936)	(2,936)
Cash and cash equivalents, beginning of period	17,769	24,093
Cash and cash equivalents, end of period	$ 12,833	21,157
Supplemental disclosure of cash flow information:		
Cash (paid) refunded for income taxes, net	$ (109)	$ 2,973

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

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Metro One Telecommunications, Inc.
Notes to Condensed Consolidated Financial Statements (Unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements have been prepared by Metro One Telecommunications, Inc. in conformity with accounting principles generally accepted in the United States of America for interim financial information. Accordingly, certain financial information and footnotes have been omitted or condensed. In the opinion of management, the condensed financial statements include all adjustments necessary for a fair presentation of the results for the interim periods. These condensed consolidated financial statements and notes thereto should be read in conjunction with our audited financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2005. The results of operations for the interim periods shown in this report are not necessarily indicative of results for future interim periods or the entire fiscal year.

The condensed consolidated financial statements include the accounts of Metro One Telecommunications, Inc. and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

On July 6, 2006, we effected a one-for-four reverse split of our common stock. All share and per share data presented in the accompanying financial statements and notes thereto have been restated for the reverse stock split.

Advertising

Costs of advertising are expensed as incurred. Advertising expense was not significant in the third quarter and first nine months of 2006 and was approximately $900,000 and $2.7 million in the third quarter and first nine months of 2005, respectively. Prior to 2006, advertising expense was primarily related to marketing and promotion of our Infone service, which was discontinued in the fourth quarter of 2005. Advertising expenses are included in selling, general and administrative expenses in the condensed consolidated statements of operations.

Cash, Cash Equivalents, and Restricted Cash

Cash and cash equivalents include cash deposits in banks and highly liquid investments with maturity dates of three months or less at the date of acquisition. Restricted cash consists of cash restricted to secure a letter of credit related to our workers compensation program and is invested in a bank certificate of deposit.

Stock-Based Compensation

Effective January 1, 2006, we adopted the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123R, Share-Based Payment, under which compensation expense is recognized in the condensed consolidated statement of operations for the fair value of employee stock-based compensation. We elected the modified-prospective transition method as permitted by SFAS No. 123R and accordingly, prior periods have not been restated to reflect the effect of SFAS No. 123R. The modified-prospective transition method requires that stock-based compensation expense recognized in the Condensed Consolidated Statement of Operations include (1) quarterly amortization of all stock-based compensation granted prior to, but not vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123 and (2) quarterly amortization of all stock-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123R. In addition, pursuant to SFAS No. 123R, we estimate forfeitures when calculating stock-based compensation expense, rather than accounting for forfeitures as incurred, which was our previous method. Compensation expense is recognized over the requisite service (vesting) period using the straight-line attribution method.

As a result of adopting SFAS 123R, net loss for the three and nine months ended September 30, 2006 was $92,000, lower than if we had continued to account for stock-based compensation under APB Opinion No. 25, as we did in the comparable periods in 2005. The effect of recording stock-based compensation on basic and diluted earnings per share for the three and nine month periods ended September 30, 2006 was a per share increase in our net loss of $0.01. Costs related to stock-based compensation are recorded in selling, general, and administrative expenses in the statement of operations.

Prior to the January 1, 2006 adoption of SFAS No. 123R we accounted for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Accordingly, under APB Opinion No. 25, no compensation expense was recognized because the exercise price of our employee stock options was equal to the market price of the underlying stock on the date of grant. We applied the disclosure provisions of SFAS No. 123, Accounting for Stock Based Compensation, as amended by SFAS No. 148, Accounting for Stock Based Compensation Transition and Disclosure, as if the fair value method had been applied in measuring compensation expense.

The following table illustrates the effect on net income and earnings per share for the three and nine month periods ended September 30, 2005 if we had applied the fair value recognition provisions of SFAS No. 123 to our stock-based compensation:

	Three months ended September 30, 2005	**Nine months ended**
(in thousands, except per share amounts)		
Net loss, as reported	$ (9,247)	$ (22,591)
Stock-based compensation expense	(39)	(2,006)
Net loss, pro forma	$ (9,286)	$ (24,597)
Basic net loss per share, as reported	$ (1.48)	$ (3.61)
Basic net loss per share, pro forma	$ (1.48)	$ (3.93)
Diluted net loss per share, as reported	$ (1.48)	$ (3.61)
Diluted net loss per share, pro forma	$ (1.48)	$ (3.93)

Options to purchase our common stock are granted at prices equal to or greater than the fair market value on the date of grant. Options granted to directors generally vest immediately while options granted to employees generally vest and become exercisable quarterly over a four year period. All options generally expire ten years from the date of the grant.

We estimate the fair value of stock options using the Black-Scholes option pricing model. Key input assumptions used to estimate the fair value of stock options include the exercise price of the award, the expected option term, the expected volatility of our stock over the option s expected term, and the risk-free interest rate over the option s expected term and the Company s expected annual dividend yield. The expected option term represents the estimated time until exercise and is based on our historical experience with similar awards, taking into consideration contractual terms, vesting schedules and expected employee behavior. The expected stock price volatility is based on the historical volatility of our stock over the most recent period equal to the expected term of the option, adjusted for activity that is not expected to occur in the future. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected term of the option. We have not yet paid a dividend, and thus the dividend yield is 0.0%. Prospectively, the assumptions will be evaluated and revised as necessary to reflect changes in market conditions and our experience. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by people who receive equity awards.

In March 2005, our Board of Directors accelerated vesting on all of the then outstanding stock options, of which all had fair market values that were less than the exercise prices at that time. In determining to accelerate the vesting of these options, the Board considered the effect on our reported stock option expense in future periods, the comparability of our statements of operations in prior and subsequent periods, and the potential benefit to the Company and our shareholders in retaining the services of affected officers and employees. The pro forma expense included in the stock-based compensation expense noted above associated with the accelerated vesting was approximately $1,592,000.

Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109. FIN 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for our fiscal year beginning January 1, 2007. We are evaluating the impact that the adoption of FIN 48 will have on our consolidated financial position and results of operations.

In September 2006, the FASB issued Statement of Financial Accounting Standard (SFAS) No. 157, Fair Value Measurements, which establishes a framework for measuring the fair value of assets and liabilities. This framework is intended to increase consistency in how fair value determinations are made under various existing accounting standards that permit, or in some cases require, estimates of fair market value. SFAS No. 157 also expands financial statement disclosure requirements about a company s use of fair value measurements, including the effect of such measures on earnings. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We do not expect the adoption of this statement to have a material effect on our consolidated financial position or results of operations.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 108 regarding the process of quantifying financial statement misstatements. SAB No. 108 states that registrants should use both a balance sheet approach and an income statement approach when quantifying and evaluating the materiality of a misstatement. The interpretations in SAB No. 108 contain guidance on correcting errors under the dual approach as well as provide transition guidance for correcting errors. This interpretation does not change the requirements within SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB No. 20 and FASB Statement No. 3, for the correction of an error on financial statements. SAB No. 108 is effective for annual financial statements covering the first fiscal year ending after November 15, 2006. We do not expect the adoption of SAB No. 108 to have a material effect on our consolidated financial position or results of operations.

2. Restructuring Charges and Exit Activities

Primarily during the second and third quarters of 2005, as part of our ongoing efforts to cut costs and align expenses with reduced revenues, we closed and consolidated the operations of 12 of our call centers. Most significant costs associated with closing those call centers were accrued and paid in 2005.

In the first nine months of 2006, we have undertaken additional restructuring activities, due primarily to the departure of call volume from Nextel as discussed in Note 5.

In the first nine months of 2006, we closed 13 call centers and significantly reduced the number of call center and administrative employees. As a result of the closure and other restructuring activities, we paid or accrued approximately $342,000 and $2.5 million of termination benefits in the three and nine month periods ended September 30, 2006, respectively. We also recorded approximately ($60,000) and $1.6 million of expenses related to termination of lease obligations of closed facilities in the three and nine month periods ended September 30, 2006, respectively. In addition, we recorded approximately $171,000 and $2.1 million of other costs, primarily legal and advisory services and dismantling costs, in the three and nine month periods ended September 30, 2006, respectively. Included in the costs for the nine months ended September 30, 2006 were losses incurred on disposal, in the second quarter, of certain corporate and call center assets in the amount of $935,000. These assets had a net book value totaling $1,574,000 at the time of disposal, and we received proceeds of $639,000 from the sale.

At September 30, 2006, we had approximately $432,000 of accrued restructuring costs, primarily related to remaining lease obligations of closed facilities and accrued termination benefits related to certain corporate employees.

Costs incurred in our restructuring activities during the third quarter and first nine months of 2006 are shown in the following table.

	Three months ended September 30, 2006	**Nine months ended September 30, 2006**
Major cost type		
One-time termination benefits	$ 342	$ 2,488
Lease termination costs	(60)	1,608
Other	171	2,134
	$ 453	$ 6,230

The following summarizes the provisions, payments, adjustments and liability for costs associated with our cost reduction efforts for the period shown (in thousands):

	One-time termination benefits	**Lease termination costs**	**Other**	**Total**
Balance at January 1, 2006	$	$ 355	$ 143	$ 498
Provisions	1,764	2,514	738	5,016
Payments	(1,764)	(566)	(764)	(3,094)
Balance at March 31, 2006		2,303	117	2,420
Provisions	382	(846)	1,225	761
Payments	(102)	(458)	(269)	(829)
Adjustments and non-cash items			(1,065)	(1,065)
Balance at June 30, 2006	$ 280	$ 999	$ 8	$ 1,287
Provisions	342	(60)	171	453
Payments	(380)	(770)	(63)	(1,213)
Adjustments and non-cash items		(19)	(76)	(95)
Balance at September 30, 2006	$ 242	$ 150	$ 40	$ 432

We may undertake additional restructuring and/or consolidation efforts in the future that would cause us to incur additional restructuring charges.

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3. Net Loss Per Share

Basic net loss per share is based on the weighted average number of common shares outstanding. Diluted net loss per share reflects the potential dilution that could occur if outstanding options to purchase common stock were exercised or converted into common stock. Basic and diluted weighted average shares outstanding were the same for the three and nine month periods ended September 30, 2006 and 2005 because inclusion of the potential dilutive effect of common stock options in the calculation would be anti-dilutive. There were no adjustments to net loss for the calculation of both basic and diluted net loss per share for either period.

Options to purchase 568,000 and 719,000 shares of common stock were outstanding at September 30, 2006 and 2005, respectively, but were not included in the computation of diluted net loss per share for the three and nine months periods ended September 30, 2006 and 2005 because their effect would be anti-dilutive.

4. Commitments and Contingencies

We are party to various legal actions and administrative proceedings arising in the ordinary course of business. We believe the disposition of these matters will not have a material adverse effect on our financial position, results of operations or cash flows.

From time to time, in the normal course of our business, we issue standby letters of credit and bank guarantees. At September 30, 2006, we had one letter of credit outstanding in the amount of $5,716,000 related to our workers compensation program. The letter of credit is secured by a certificate of deposit for the same amount that is recorded as restricted cash. This letter of credit expires in April 2007.

5. Significant Events

Termination of contract

In February 2005, we entered into a Master Services Agreement for Directory Assistance Services (the Services Agreement) with Nextel Operations, Inc., acting on behalf of certain affiliates (collectively Nextel) of Nextel Communications, Inc. The Services Agreement superseded our previous services agreement dated in June 1999. Under the Services Agreement, we agreed to provide directory assistance services to Nextel s customers on a non-exclusive basis, and Nextel could transition call volume away from us on short notice and/or terminate services entirely.

In October 2005, we received notification from Nextel that it would be terminating the Services Agreement effective January 9, 2006. In February 2006, we entered into a Settlement Agreement and Disentanglement Transition Plan (the Plan) with Nextel that resolved certain disputed matters in connection with the termination of the Services Agreement. Under the Plan, we continued to provide services to Nextel callers through March 31, 2006 in return for the payment by Nextel of approximately $5.75 million. Those payments were in addition to $2.5 million previously paid by Nextel in December 2005 in connection with the transition and in addition to the contractual payments by Nextel for normal service provided by us to Nextel callers through the transition period. Calls from Nextel were substantially transitioned away from us by March 31, 2006, and we have received all amounts due from Nextel as of the date of this filing. Including the $5.75 million received in the first quarter of 2006 as part of the settlement payments, Nextel represented approximately 44% of our revenues for the first nine months of 2006. Nextel accounted for approximately 75% and 73% of our revenues in the third quarter and first nine months of 2005, respectively.

Termination of the Services Agreement has had, and will continue to have, a significant adverse impact on our results of operations and cash flows and raises doubt as to whether we can continue to operate as a going concern. We have experienced net losses in each of the quarterly and annual periods since the first quarter of 2003. We expect to meet our cash requirements in the remainder of 2006 and in 2007 using our existing cash and cash equivalents.

Our management has taken steps to significantly reduce the direct cost of delivering our services, reduce our general and administrative overhead and is aggressively pursuing new and additional sources of revenues to support our reduced cost structure and develop and grow our data services business. There can be no assurance that management s plans will be successful. In such event, we may attempt to establish borrowing arrangements or otherwise raise funds in order to maintain adequate liquidity, although we cannot provide assurance that financing or other funding will be available in amounts or on terms acceptable to us. If we are unable to execute our operations according to our plan or obtain additional financing, we may be forced to cease operations.

Nasdaq listing issues

Our common stock listing was transferred from the Nasdaq National Market to the Nasdaq Capital Market (formerly the Nasdaq SmallCap Market) on February 22, 2006. We elected to seek a transfer to the Nasdaq Capital Market because we had been unable to regain compliance with the $1.00 minimum bid price requirement for continued listing on the Nasdaq National Market. By transferring to the Nasdaq Capital Market, we were afforded an extended grace period in which we could satisfy the $1.00 minimum bid price requirement. At our annual meeting of shareholders, we received approval for, and on July 6, 2006 we effected, a one-for-four reverse stock split. In July 2006, we were notified by Nasdaq that we regained compliance with the Nasdaq listing requirements, and this matter is now closed.

Significant new contract

In August 2006, we entered into a Telecom Information Services Agreement (the Agreement) with Jingle Networks, Inc. (Jingle). Under the Agreement, we will be a preferred directory assistance provider for 1-800-FREE411 . In addition to per call charges, the Agreement includes financial commitments from Jingle based on call volume expansion and other financial incentives. The Agreement is for three years and will automatically renew annually for up to two additional years unless either party provides notice of termination at least 60 days prior to the commencement of such renewal period. Under the Agreement, as a preferred directory provider we will be allocated no fewer calls than any other vendor providing similar services. The Agreement provides that our status as a preferred provider may be terminated by Jingle but, in such event, the warrants described below will be terminated.

In connection with the Agreement, we issued to Jingle two warrants to purchase shares of our common stock. The first warrant is for the purchase of up to 623,250 shares of common stock at an exercise price of $2.60 per share. The warrant will not be exercisable unless and until certain revenue and payment thresholds are achieved by Jingle during specified time periods as outlined in the Agreement. The first warrant terminates on June 30, 2009.

The second warrant is for the purchase of up to 870,075 shares of our common stock; provided, however, that shares represented by the sum of the first and second warrants, if exercised, cannot exceed 19.98% of our total shares outstanding after the warrants are exercised. The exercise price for the second warrant will equal 115% of the average closing price per share of the our common stock over the 20 consecutive trading days ending the last trading day prior to July 1, 2007. The second warrant will not be exercisable unless and until certain revenue and payment thresholds are achieved by Jingle during specified time periods as outlined in the Agreement. The second warrant terminates on July 1, 2009.

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

All statements and trend analyses contained in this item and elsewhere in this report on Form 10-Q relative to the future constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements may, but do not necessarily, also include words such as believes, expects, anticipates, plans, estimates, may, will, should, could, con expressions. Forward-looking statements are not guarantees. They involve known and unknown business and economic risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These risks, uncertainties and other factors include the expiration or pricing of customer contracts, the successful execution of our cost reduction efforts and current business strategy, and our ability to generate cash from operations, and other risks, including those discussed in our most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission (the SEC) and those described in our other filings with the SEC, press releases and other communications. Any forward-looking statement in this report reflects our expectations at the time of this report only. We undertake no obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

Overview

We are a provider of Enhanced Directory Assistance® and other information services through operators and electronically. We contract primarily with wireless carriers, Voice over Internet Protocol (VoIP) providers, cable companies, Competitive Local Exchange Carriers (CLEC) and prepaid carriers to provide our services to their subscribers.

In addition to voice-based services, we also provide directory assistance services in electronic format. These services are provided to customers who electronically issue directory assistance queries and use the returned information to complete and correct their own data records. We currently provide electronic directory assistance services in a number of delivery formats to meet customer needs including automated file processing and real-time individual look ups. We contract with a broad range of companies that require electronic directory assistance, including companies in the service, marketing, and financial sectors. Our Data Services business represents an emerging business based on infrastructure originally developed to support our voice-based call center business.

We offer our voice-based services to a carrier s subscribers under a brand name selected by the carrier. The carrier establishes its own fee structure with its subscribers. Subscribers typically pay the carrier s fees ranging from $1.25 to $1.99 plus airtime charges for directory assistance services. We charge carriers directly and, at present, bear no subscriber collection risk. We charge our customers on a per call basis. Competitive pressures have caused our average revenue per call to decrease in the recent past and such pressures will likely continue.

We currently provide our services to several carriers and other customers. The terms of these contracts are generally similar, with variations in the geographic market to be served, the services and features we are to provide the carriers subscribers and the term. None of these contracts precludes us from providing services to others.

We have expanded our customer base to include data services, specialized operator services, such as with Motorola s VIAMOTO application, and directory assistance services to corporations with offices in the United States and Canada.

Competition in the telecommunications industry, and in the directory assistance market in which we participate, has been intense. Carriers are looking to lower their costs of providing directory assistance and other services through, among other ways, outsourcing to low cost domestic or overseas operators and utilizing automation to reduce costs. In response to these and other issues, in May 2003, we launched Infone, a service that provided enhanced directory and personal assistant services directly to consumers. The initial launch of Infone was accompanied by a significant nationwide marketing and promotion campaign. Revenues from Infone were not significant in relation to total revenues since its inception. Because of our inability to attract a significant number of subscribers to this service, it was discontinued in December 2005.

In the recent past, several of our largest customers have transferred their calls away from us for a variety of reasons, primarily in order to obtain lower prices and/or as a result of consolidation in the wireless industry. As a result of the loss of these customers and the associated revenues and operating losses, since the second quarter of 2005 we have taken significant actions to restructure our operations to lower our cost structure. In addition, we have refocused our efforts on the wholesale directory assistance and data services markets to pursue additional revenue sources in the voice-based and electronic delivery-based directory assistance and information services markets.

Significant Events

Termination of contract

In February 2005, we entered into a Master Services Agreement for Directory Assistance Services (the Services Agreement) with Nextel Operations, Inc., acting on behalf of certain affiliates (collectively Nextel) of Nextel Communications, Inc. The Services Agreement superseded our previous services agreement dated in June 1999. Under the Services Agreement, we agreed to provide directory assistance services to Nextel s customers on a non-exclusive basis, and Nextel could transition call volume away from us on short notice and/or terminate services entirely.

In October 2005, we received notification from Nextel that it would be terminating the Services Agreement effective January 9, 2006. In February 2006, we entered into a Settlement Agreement and Disentanglement Transition Plan (the Plan) with Nextel that resolved certain disputed matters in connection with the termination of the Services Agreement. Under the Plan, we continued to provide services to Nextel callers through March 31, 2006 in return for the payment by Nextel of approximately $5.75 million. Those payments were in addition to $2.5 million previously paid by Nextel in December 2005 in connection with the transition and in addition to the contractual payments by Nextel for normal service provided by us to Nextel callers through the transition period. Calls from Nextel were substantially transitioned away from us by March 31, 2006, and we have received all amounts due from Nextel as of the date of this filing. Including the $5.75 million received in the first quarter of 2006 as part of the settlement payments, Nextel represented approximately 44% of our revenues for the first nine months of 2006. Nextel accounted for approximately 75% and 73% of our revenues in the third quarter and first nine months of 2005, respectively.

Termination of the Services Agreement has had, and will continue to have, a significant adverse impact on our results of operations and cash flows and raises doubt as to whether we can continue to operate as a going concern. We have experienced net losses in each of the quarterly and annual periods since the first quarter of 2003. We expect to meet our cash requirements in the remainder of 2006 and 2007 using our existing cash and cash equivalents.

Our management has taken steps to significantly reduce the direct cost of delivering our services, reduce our general and administrative overhead and is aggressively pursuing new and additional sources of revenues to support our reduced cost structure and develop and grow our data services business. There can be no assurance that management s plans will be successful. In such event, we may attempt to establish borrowing arrangements or otherwise raise funds in order to maintain adequate liquidity, although we cannot provide assurance that financing or other funding will be available in amounts or on terms acceptable to us. If we are unable to execute our operations according to our plan or obtain additional financing, we may be forced to cease operations.

Restructuring

As a result of the termination of the Services Agreement, we have consolidated and reduced our operations significantly and may continue to close call centers and reduce the number of employees both in call centers and in corporate and administrative staff now that the transition of calls from Nextel has been completed.

Primarily during the second and third quarters of 2005, as part of our ongoing efforts to cut costs and align expenses with reduced revenues, we closed and consolidated the operations of 12 of our call centers. Most significant costs associated with closing those call centers were accrued and paid in 2005.

In the first nine months of 2006, we have undertaken additional restructuring activities, due primarily to the departure of call volume from Nextel discussed above. In the first nine months of 2006, we closed 13 call centers and significantly reduced the number of call center and administrative employees. As a result of the closure and other restructuring activities, we paid or accrued approximately $342,000 and 2.5 million of termination benefits in the three and nine month periods ended September 30, 2006, respectively. We also recorded approximately ($60,000) and $1.6 million of expenses related

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to termination of lease obligations of closed facilities in the three and nine month periods ended September 30, 2006, respectively. In addition, we recorded approximately $171,000 and $2.1 million of other costs, primarily legal and advisory services and dismantling costs, in the three and nine month periods ended September 30, 2006, respectively. Included in the costs for the nine months ended September 30, 2006 were losses incurred on disposal, in the second quarter, of certain corporate and call center assets in the amount of $935,000. These assets had a net book value totaling $1,574,000 at the time of disposal, and we received proceeds of $639,000 from the sale.

As of September 30, 2006, we continue to operate six call centers from leased facilities. In addition, we utilize four other leased facilities, including our corporate headquarters and other administrative properties.

Nasdaq listing issues

Our common stock listing was transferred from the Nasdaq National Market to the Nasdaq Capital Market (formerly the Nasdaq SmallCap Market) on February 22, 2006. We elected to seek a transfer to the Nasdaq Capital Market because we had been unable to regain compliance with the $1.00 minimum bid price requirement for continued listing on the Nasdaq National Market. By transferring to the Nasdaq Capital Market, we were afforded an extended grace period in which we could satisfy the $1.00 minimum bid price requirement. At our annual meeting of shareholders, we received approval for, and on July 6, 2006 we effected, a one-for-four reverse stock split. In July 2006, we were notified by Nasdaq that we regained compliance with the Nasdaq listing requirements, and this matter is now closed.

Significant new contract

In August 2006, we entered into a Telecom Information Services Agreement (the Agreement) with Jingle Networks, Inc. (Jingle). Under the Agreement, we will be a preferred directory assistance provider for 1-800-FREE411 . In addition to per call charges, the Agreement includes financial commitments from Jingle based on call volume expansion and other financial incentives. The Agreement is for three years and will automatically renew annually for up to two additional years unless either party provides notice of termination at least 60 days prior to the commencement of such renewal period. Under the Agreement, as a preferred directory provider we will be allocated no fewer calls than any other vendor providing similar services. The Agreement provides that our status as a preferred provider may be terminated by Jingle but, in such event, the warrants described below will be terminated.

In connection with the Agreement, we issued to Jingle two warrants to purchase shares of our common stock. The first warrant is for the purchase of up to 623,250 shares of common stock at an exercise price of $2.60 per share. The warrant will not be exercisable unless and until certain revenue and payment thresholds are achieved by Jingle during specified time periods as outlined in the Agreement. The first warrant terminates on June 30, 2009.

The second warrant is for the purchase of up to 870,075 shares of our common stock; provided, however, that shares represented by the sum of the first and second warrants, if exercised, cannot exceed 19.98% of our total shares outstanding after the warrants are exercised. The exercise price for the second warrant will equal 115% of the average closing price per share of the our common stock over the 20 consecutive trading days ending the last trading day prior to July 1, 2007. The second warrant will not be exercisable unless and until certain revenue and payment thresholds are achieved by Jingle during specified time periods as outlined in the Agreement. The second warrant terminates on July 1, 2009.

Results of Operations

This table shows selected items from our statements of operations expressed as a percentage of revenues:

	Three Months Ended September 30, 2006		Three Months Ended September 30, 2005		Nine Months Ended September 30, 2006		Nine Months Ended September 30, 2005	
Revenues	100.0	%	100.0	%	100.0	%	100.0	%
Direct operating costs	72.8		80.1		59.9		82.0	
Selling, general and administrative costs	75.8		58.6		65.8		63.4	
Depreciation and amortization	13.2		8.0		11.9		8.2	
Restructuring charges	8.7		14.3		24.4		7.0	
Loss from operations	(80.5	)	(60.9	)	(62.0	)	(60.5	)
Other income, net	3.6		1.2		2.3		1.4	
Loss before income taxes	(76.9	)	(59.7	)	(59.7	)	(59.1	)
Income tax expense			2.2		0.2		0.6	
Net loss	(76.9	)%	(61.9	)%	(59.9	)%	(59.7	)%

Comparison of third quarter 2006 to third quarter 2005

Revenues decreased 72.9% to $5.2 million from $19.2 million due primarily to a decrease in call volume and a decrease in our average revenue per call. Call volume decreased to approximately 19 million calls from approximately 59 million calls due primarily to lower call volume from Nextel as a result of their early termination of the Services Agreement. Average revenue per call was approximately $0.25 and $0.32 in the third quarter of 2006 and 2005, respectively, reflecting the change in call volume mix and competitive pressures.

Direct operating costs consist of salaries, wages, benefits and payroll taxes relating to call center personnel plus the costs of listings data and content acquisition. These costs decreased 75.4% to $3.8 million from $15.4 million. This decrease was primarily due to lower personnel and data costs associated with servicing lower call volumes. As a percentage of revenues direct operating costs decreased to 72.8% from 80.1% due primarily to increased call processing efficiencies and decreased labor rates in the call centers resulting from our ongoing cost reduction efforts.

Selling, general and administrative costs decreased 60.3% to $4.5 million from $11.3 million. This decrease resulted primarily from reductions in facilities-related costs of approximately $1.8 million, personnel and associated costs of approximately $2.4 million, network and systems-related costs of $800,000, and marketing and promotion costs of approximately $900,000. As a percentage of revenues, selling, general and administrative costs increased to 85.8% from 58.6% primarily due to lower revenues.

Depreciation and amortization expense decreased 55.1% to approximately $700,000 from $1.5 million. The decrease in depreciation and amortization was due primarily to the overall reduction in acquisition of fixed assets in the last several years as operations have been reduced. Depreciation and amortization increased to 13.2% from 8.0% of revenue as a result of lower revenues.

Restructuring charges in the quarter ended September 30, 2006 consisted primarily of one-time termination benefits for employees of approximately $342,000 and dismantling costs related to the closed call centers of approximately $171,000. In addition, during the third quarter of 2006, we settled or otherwise disposed of lease obligations of several closed call centers. As a result of these settlement activities, we incurred actual costs that were $60,000 lower than the amounts we had previously accrued for those lease obligations. Net restructuring costs were $453,000 in the third quarter of 2006. Restructuring charges of approximately $432,000, primarily related to remaining lease obligations of closed facilities and accrued termination benefits related to certain corporate employees, have been accrued but not paid at September 30, 2006.

Other income was $187,000 and $235,000 in the third quarter of 2006 and 2005, respectively, and consisted primarily of interest income earned on cash and cash equivalents.

Because of our operating losses in the third quarter of 2006, we recorded no federal income tax expense. We have a valuation allowance against deferred tax assets associated with operating losses in this and prior quarters and other deferred tax assets because it is deemed more likely than not that these assets will not be realized. Accordingly, no federal income tax benefit has been recorded with respect to these deferred tax assets. Income tax expense in the third quarter of 2005 was approximately $423,000, reflecting a provision for federal income tax expense related to a proposed adjustment by the Internal Revenue Service (IRS) relating to a prior year tax return under audit.

Liquidity and Capital Resources

As of September 30, 2006, we had approximately $18.6 million in cash and cash equivalents and restricted cash (including $5.7 million of restricted cash) compared to approximately $24.6 million (including $6.9 million of restricted cash) at December 31, 2005. Our business has consumed approximately $6.1 million of cash (including $4.9 million of cash and equivalents and $1.2 million of restricted cash) in the first nine months of 2006 primarily from net operating losses. Management s goal is to restructure our operations to achieve positive, sustainable cash flow and earnings and we believe we have made significant progress toward that goal. There can be, however, no assurances that our cash resources will be sufficient to achieve that goal in the near term or ever. Cash and cash equivalents and restricted cash are recorded at cost which approximates their fair market value. We have no outstanding debt.

Working capital was $16.4 million at September 30, 2006, compared to $26.6 million at December 31, 2005. This change was primarily due to net operating losses in the first nine months of 2006.

Cash flow from operations. Net cash used in operations was $6.7 million in the first nine months of 2006 compared to net cash used in operations of $24.7 million in the first nine months of 2005. This difference of approximately $18.0 million resulted primarily from net decreases in cash paid to or on behalf of employees, cash paid to suppliers, and cash paid for advertising. These net decreases in cash outflows were partially offset by a decrease in cash received from customers and an increase in cash paid for restructuring activities. Cash paid to or on behalf of employees decreased by $34.6 million, cash paid to suppliers decreased by $9.5 million, and cash paid for advertising decreased by $2.8 million. Cash received from customers decreased by $28.6 million and cash paid for restructuring increased by $2.4 million.

Cash flow from investing activities. Cash provided by investing activities was $1.7 million in the first nine months of 2006, primarily resulting from receipt of proceeds from the sale of assets and a reduction in cash used to secure a letter of credit related to our workers compensation program partially offset by cash used for capital purchases. Cash provided by investing activities was $21.8 million in the first months of 2005 resulting primarily from short-term investments being converted to cash and used in operations partially offset by capital expenditures for equipment purchased for upgrades of our corporate-wide infrastructure and an increase in cash restricted to secure a letter of credit related to our workers compensation program.

Cash flow from financing activities. Cash flow from financing activities was not significant in the first nine months of 2006 or 2005.

Future capital needs and resources. The primary use of our capital in the near future is expected to be for working capital. Although cash on hand (including restricted cash) and short-term investments at September 30, 2006 was approximately $18.6 million, our operations and future activities, including additional restructuring efforts, will likely reduce available cash.

We are aggressively pursuing new and additional sources of revenue. We are also adjusting our operations and reducing various elements of our operating costs where feasible. We plan to continue to adjust call centers, personnel and network capacities to care for varying business circumstances, including changes in call volumes, pricing and other provisions of current and future customer contracts.

We plan to meet our cash and working capital requirements using existing cash and cash equivalents during the remainder of 2006 and throughout 2007. However: 1) we have experienced net losses during each quarter since the second quarter of 2003; 2) cash and cash equivalents and restricted cash decreased $6.1 million during the first nine months of 2006; 3) we anticipate additional net losses during 2006 and 2007; and 4) future restructuring of our operations may further reduce available financial resources. As a result of these and/or other issues, there can be no assurance that our existing financial resources will be sufficient or that we will be able to raise sufficient funds from other sources to maintain adequate liquidity. Consequently, if we are unable to execute our current operating plans or obtain additional financing, we may be forced to cease operations.

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Critical Accounting Policies

We prepare our financial statements in conformity with accounting principles generally accepted in the United States of America. As such, we are required to make certain estimates, judgments and assumptions that we believe are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. Management believes that of our significant accounting policies (see Note 1 to the financial statements), those governing accounts receivable, the lives and recoverability of the carrying amount of equipment and other long-lived assets, such as existing intangibles, estimates involving the levels of our contingent liabilities for workers compensation and medical self-insurance and estimates of current and deferred taxes owed may involve a higher degree of judgment, estimation and uncertainty.

Accounts receivable. Our wholesale customer base has primarily consisted of large wireless telephone carriers in the United States. As such, we have had minimal risk of uncollectibility, at any point in time, related to outstanding accounts receivable with these customers. We have not experienced significant collection issues or write-offs related to these customers. Since our accounts receivable are concentrated in relatively few of these wholesale customers, a significant change in the liquidity or financial position of any one of them could adversely impact collection of our accounts receivable and therefore have a material adverse effect on our financial position and future operating results. In addition, our emerging data services business is expected to generate receivables from customers that may not be as financially stable as our large carrier customers which may expose us to greater risk of uncollectible receivables than we have experienced in the past.

Long-lived assets and intangibles. We evaluate the remaining life and recoverability of equipment and other assets, including patents and trademarks and internally developed software, whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. At such time, we estimate the future cash flows expected from the use of such assets and their eventual disposition and, if lower than the carrying amounts, adjust the carrying amount of the assets to their estimated fair value. Because of our changing business conditions, including lower wholesale prices and dependence on a relatively small number of customers for a significant portion of our revenues, our estimates of future cash flows to be generated from our operations could change materially, resulting in the need for us to record additional impairment charges. In addition, as a result of our changing business conditions, we expect to adjust personnel, call centers and network capacities. If any of these activities result in certain of our assets no longer being used in operations, we may need to record an additional impairment charge. As a result of the decision by Nextel to terminate its contract with us, as discussed under Significant Events above, we evaluated our fixed assets and intangibles as of December 31, 2005 for impairment in accordance with SFAS No. 144 and SFAS No. 142. Our evaluation determined that the assets were not impaired as of December 31, 2005.

Self-insurance reserves. We have historically self-insured a portion of our workers compensation and employee medical insurance programs. Under those arrangements we typically purchase stop loss coverage at varying levels in order to mitigate our potential future losses. The nature of these liabilities, which may not fully manifest themselves for several years, requires significant judgment. We evaluate pending workers compensation and medical claims periodically to determine the reasonableness of the reserves we have recorded for such claims. Our evaluation includes estimates of potential incurred-but-unreported claims as well as factors that may cause original estimates of such claims to increase over time, such as available claims data and historical trends and experience, as well as future projections of ultimate losses, expenses, premiums and administrative costs. We adjust these reserves if events or changes in circumstances indicate that ultimate payments related to the claims will be more than the recorded reserves. At September 30, 2006, we have reserved approximately $2.5 million and $489,000 related to our workers compensation and medical programs, respectively. While we believe that the amounts reserved for these obligations are sufficient, any significant increase in the number of claims and costs associated with claims made under these plans could have a material adverse effect on our financial position, results of operations or cash flows.

*Income taxe*s. Accounting for income taxes requires us to estimate our income taxes in each jurisdiction in which we operate. Due to differences in the recognition of items included in income for accounting and tax purposes, temporary differences arise which are recorded as deferred tax assets or liabilities. We estimate the likelihood of recovery of these assets, which is dependent on future levels of profitability and enacted tax rates. Should any amounts be determined not to be recoverable, or assumptions change, we would be required to take a charge to establish a valuation allowance against such deferred tax assets, which could have a material effect on our financial position, results of operations or cash flows. At September 30, 2006, a valuation allowance reduced net deferred tax assets to zero.

Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109. FIN 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for our fiscal year beginning January 1, 2007. We are evaluating the impact that the adoption of FIN 48 will have on our consolidated financial position and results of operations.

In September 2006, the FASB issued Statement of Financial Accounting Standard (SFAS) No. 157, Fair Value Measurements, which establishes a framework for measuring the fair value of assets and liabilities. This framework is intended to increase consistency in how fair value determinations are made under various existing accounting standards that permit, or in some cases require, estimates of fair market value. SFAS No. 157 also expands financial statement disclosure requirements about a company s use of fair value measurements, including the effect of such measures on earnings. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We do not expect the adoption of this statement to have a material effect on our consolidated financial position or results of operations.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 108 regarding the process of quantifying financial statement misstatements. SAB No. 108 states that registrants should use both a balance sheet approach and an income statement approach when quantifying and evaluating the materiality of a misstatement. The interpretations in SAB No. 108 contain guidance on correcting errors under the dual approach as well as provide transition guidance for correcting errors. This interpretation does not change the requirements within SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB No. 20 and FASB Statement No. 3, for the correction of an error on financial statements. SAB No. 108 is effective for annual financial statements covering the first fiscal year ending after November 15, 2006. We do not expect the adoption of SAB No. 108 to have a material effect on our consolidated financial position or results of operations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Substantially all of our liquid resources are invested in money market instruments and short-term debt securities, and therefore, the fair market value of these investments is affected by changes in market interest rates. However, these funds were invested in overnight money market instruments or debt securities with short-term effective maturities at September 30, 2006 and were redeemable on a daily or monthly basis. All of the underlying investments in the money market fund had maturities of three months or less. A hypothetical 1% fluctuation in interest rates would not have a material adverse effect on our financial position, results of operations or cash flows.

ITEM 4. CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of our disclosure controls and procedures (as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act)) at the end of the period covered by this quarterly report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report.

There has not been any change in our internal control over financial reporting, that occurred during the fiscal quarter covered by this report, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 6. EXHIBITS

(a) Exhibits

10.1	Telecom Information Services Agreement between Jingle Networks, Inc. and Metro One Telecommunications, Inc. dated July 1, 2006.
10.2	Common Stock Warrant No. 3 to purchase shares of common stock between Jingle Networks, Inc. and Metro One Telecommunications, Inc., dated July 1, 2006.
10.3	Common Stock Warrant No. 4 to purchase shares of common stock between Jingle Networks, Inc. and Metro One Telecommunications, Inc., dated July 1, 2006.
10.4	Registration Rights Agreement between Jingle Networks, Inc. and Metro One Telecommunications, Inc., dated July 1, 2006.
31.1	Certification of Principal Executive Officer pursuant to Securities and Exchange Commission Rule 13a-14(a).
31.2	Certification of Principal Financial Officer pursuant to Securities and Exchange Commission Rule 13a-14(a).
32.1	Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act Of 2002.

Confidential treatment requested as to certain portions of this exhibit.

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.

Date: November 14, 2006

METRO ONE TELECOMMUNICATIONS, INC.

By: /s/ Duane C. Fromhart
Duane C. Fromhart
Senior Vice President
Chief Financial Officer
(Principal Financial and Accounting Officer)

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