ELEC COMMUNICATIONS CORP
Form 10-Q
April 20, 2007

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

**FORM 10-Q**

(Mark One)

[ X ] QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended February 28, 2007.

OR

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the transition period from ________________ to ________________.

Commission file number 0-4465

eLEC Communications Corp.
(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| New York<br>(State or Other Jurisdiction<br>of Incorporation or Organization) | 13-2511270<br>(I.R.S. Employer<br>Identification No.) |
| 75 South Broadway, Suite 302, White Plains, New York<br>(Address of Principal Executive Offices) | 10601<br>(Zip Code) |
| Registrant s Telephone Number, Including Area Code | 914-682-0214 |

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes_ X_ No___.

Indicate 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___ Accelerated Filer___ Non-Accelerated Filer _X_.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes____ No_X_

The number of outstanding shares of the Registrant s Common Stock as of April 16, 2007 was 22,459,282.

PART 1. FINANCIAL INFORMATION

**Item 1.** **Financial Statements**

eLEC Communications Corp. and Subsidiaries
Condensed Consolidated Balance Sheet

| | Feb. 28, 2007 | Nov. 30, 2006 |
|---|---|---|
| | (Unaudited) | (See Note 1) |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | $ 311,353 | $1,337,525 |
| Accounts receivable, net | 627,143 | 630,197 |
| Prepaid expenses and other current assets | 66,764 | 154,749 |
| Deferred finance costs, net | 864,644 | 1,012,941 |
| Total current assets | 1,869,904 | 3,135,412 |
| Property, plant and equipment, net | 899,478 | 903,281 |
| Other assets | 167,383 | 149,525 |
| Total assets | $2,936,765 | $4,188,218 |
| Liabilities and stockholders equity deficiency | | |
| Current liabilities: | | |
| Current portion of long-term debt and capital lease obligations | $3,353,464 | $3,347,707 |
| Warrant liability | 2,211,404 | 1,251,182 |
| Accounts payable and accrued expenses | 2,626,043 | 2,897,495 |
| Taxes payable | 548,014 | 559,617 |
| Deferred Revenue | 151,900 | 166,100 |
| Total current liabilities | 8,890,825 | 8,222,101 |
| Long-term debt and capital lease obligations, less current maturities | 202,405 | 214,907 |
| Total liabilities | 9,093,230 | 8,437,008 |
| Stockholders equity deficiency: | | |
| Preferred stock $.10 par value, 1,000,000 shares authorized, none issued and outstanding | - | - |
| Common stock $.10 par value, 50,000,000 shares authorized, 22,459,282 and 22,434,282 shares issued and outstanding in 2007 and 2006 | 2,245,928 | 2,243,428 |
| Capital in excess of par value | 27,163,323 | 27,071,584 |
| Deficit | (35,555,158) | (33,554,700) |
| Accumulated other comprehensive loss, unrealized loss on securities | (10,558) | (9,102) |

| | | |
|---|---|---|
| Total stockholders equity deficiency | (6,156,465) | (4,248,790) |
| Total liabilities and stockholders equity deficiency | $2,936,765 | $4,188,218 |

See notes to the condensed consolidated financial statements.

eLEC Communications Corp. and Subsidiaries
Condensed Consolidated Statements of Operations and Comprehensive Loss
(Unaudited)

| | For the Three Months Ended | |
|---|---|---|
| | Feb. 28, 2007 | Feb. 28, 2006 |
| Revenues | $1,741,123 | $2,496,854 |
| Costs and expenses: | | |
| Costs of services | 1,202,749 | 1,419,837 |
| Selling, general and administrative | 1,139,909 | 1,246,680 |
| Provision for bad debts | 49,386 | 117,676 |
| Depreciation and amortization | 173,539 | 86,625 |
| Total costs and expenses | 2,565,583 | 2,870,818 |
| Loss from operations | (824,460) | (373,964) |
| Other income (expense): | | |
| Interest expense | (226,546) | (281,385) |
| Change in warrant valuation | (960,222) | (22,257) |
| Other income | 10,770 | 14,127 |
| Total other income (expense) | (1,175,998) | (289,515) |
| Net loss | (2,000,458) | (663,479) |
| Other comprehensive loss - unrealized loss on marketable securities | (1,456) | (915) |
| Comprehensive loss | ($2,001,914) | ($664,394) |
| Basic loss per share | ($0.09) | ($0.04) |
| Weighted average number of common shares outstanding Basic | 22,435,949 | 16,839,282 |

See notes to the condensed consolidated financial statements.

eLEC Communications Corp. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(Unaudited)

| | For the Three Months Ended | |
|---|---|---|
| | Feb. 28, 2007 | Feb. 28, 2006 |
| Net cash used in operating activities: | ($963,831) | ($836,555) |
| Cash flows used in investing activities, purchase of property and equipment | (51,500) | (122,899) |
| Cash flows from financing activities: | | |
| Repayment of short-term debt | - | (328,324) |
| Repayment of long-term debt | (10,841) | (3,230) |
| Proceeds from notes | - | 1,753,500 |
| Net cash (used in) provided by financing activities | (10,841) | 1,421,946 |
| Increase (decrease) in cash and cash equivalents | (1,026,172) | 462,492 |
| Cash and cash equivalents at beginning of period | 1,337,525 | 205,998 |
| Cash and cash equivalents at the end of period | $311,353 | $668,490 |

See notes to the condensed consolidated financial statements.

**eLEC COMMUNICATIONS CORP.**

**Notes To Condensed Consolidated Financial Statements (Unaudited)**

Note 1-Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and in accordance with the rules and regulations of the Securities and Exchange Commission for Form 10-Q. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month period ended February 28, 2007 are not necessarily indicative of the results that may be expected for the year ended November 30, 2007. For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended November 30, 2006.

Note 2-Major Customers

During the three-month periods ended February 28, 2007 and 2006, no one customer accounted for more than 10% of revenue.

Note 3-Loss Per Common Share

Basic loss per common share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period.

Approximately 11,033,000 and 13,807,000 shares of common stock issuable upon the exercise of our outstanding stock options or warrants or, in the three month period ending February 28, 2006, the conversion of our outstanding convertible debt, were excluded from the calculation of loss per share for the three months ended February 28, 2007 and 2006, respectively, because the effect would be anti-dilutive.

Note 4-Risks and Uncertainties

We provide our wireline services by leasing a portion of the network owned by other larger telecommunications carriers, namely Verizon Services Corp. and Qwest Communications International, Inc., which are commonly referred to as Incumbent Local Exchange Carriers ( ILECs ). We have multi-state commercial service agreements with the ILECs that are subject to termination for material breach, including non-payment, upon written notice and our failure to cure. These agreements allow us to offer wireline telecommunications services to consumers throughout the ILECs territories without us having to incur network equipment expenditures. Although we continue to build an Internet Protocol ( IP ) telephony network, and our long-term plans are dependent upon the success of out IP telephony operations, the majority of our revenues are currently derived from the resale of ILEC services. In light of the foregoing, it is possible that the loss of our relationship with the ILECs would have a severe near-term impact on our ability to conduct our business and on our ability to sell our wireline services operation, for which we have a signed agreement to sell to a third party. Our long-term plans, however, are

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dependent upon the success of our IP operations. Future results of operations involve a number of risks and uncertainties. Factors that could affect future operating results and cash flows and cause actual results to vary materially from historical results include, but are not limited to:

- The availability of additional funds to successfully pursue our business plan;
- The acceptance of IP telephony by mainstream consumers;
- Our ability to market our services to current and new customers and generate customer demand for our products and services in the geographical areas in which we operate;
- Our ability to comply with provisions of our financing agreements;
- The impact of changes the Federal Communications Commission or State Public Service Commissions may make to existing telecommunication laws and regulations, including laws dealing with Internet telephony;
- The highly competitive nature of our industry;
- Our ability to retain key personnel;
- Our ability to maintain adequate customer care and manage our churn rate;
- The cooperation of incumbent carriers and industry service partners that have signed agreements with us;
- Our ability to maintain, attract and integrate internal management, technical information and management information systems;
- The availability and maintenance of suitable vendor relationships, in a timely manner, at reasonable cost;
- Our ability to manage rapid growth while maintaining adequate controls and procedures;
- Failure or interruption in our network and information systems;
- Our inability to adapt to technological change;
- The perceived infringement of our technology on another entity s patents;
- Our inability to manage customer attrition and bad debt expense;
- Failure or bankruptcy of other telecommunications companies upon whom we rely for

services and revenues;
- Our lack of capital or borrowing capacity, and inability to generate cash flow;
- The decrease in telecommunications prices to consumers; and
- General economic conditions.

Note 5-Stock-Based Compensation Plans

We issue stock options to our employees and outside directors pursuant to stockholder-approved and non-approved stock option programs. In December 2004, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 123R, Share-Based Payment . SFAS 123R is a revision of SFAS 123, and supersedes APB 25. Among other items, SFAS 123R eliminates the use of APB 25 and the intrinsic value method of accounting, and requires companies to recognize in their financial statements the cost of employee services received in exchange for awards of equity instruments, based on the grant date fair value of those awards. SFAS 123R permits companies to adopt its requirements using either a modified prospective method, or a modified retrospective method. Under the modified prospective method, compensation cost is recognized in the financial statements beginning with the effective date, based on the requirements of SFAS 123R for all share-based payments granted after that date, and based on the requirements of SFAS 123 for all unvested awards granted prior to the effective date of SFAS 123R. Under the modified retrospective method, the requirements are the same as under the modified prospective method, but this method also permits entities to restate financial statements of previous periods based on proforma disclosures made in accordance with SFAS 123. Beginning in fiscal 2006, we account for stock-based compensation in accordance with the provisions of SFAS 123R and have elected the modified prospective method and have not restated prior financial statements. For the three months ended February 28, 2007 and 2006, we recorded approximately $45,000 and $52,000, respectively, in employee stock-based compensation expense, which is included in our selling, general and administrative expenses. As of February 28, 2007, there was approximately $183,000 of unrecognized stock-compensation expense for previously granted unvested options that will be recognized over a three-year period.

Note 6-Accounts Payable and Accrued Expenses

At February 28, 2007, we are disputing payments on invoices from Verizon amounting to approximately $537,000 because we believe Verizon overcharged us for certain calls made by our customers. Although we are not currently required to pay the disputed amount, Verizon initially rejected our claims. We have escalated many of our claims and hired a firm that specializes in telecom disputes to analyze past call records, resubmit and pursue the claims. This firm has escalated many of the claims and estimated that at a minimum $125,000 of the various claims will be honored. Consequently, we have recorded $412,000 of the disputed charges as a liability and have not recorded the $125,000 amount.

Note 7-Defined Benefit Plan

We sponsor a defined benefit plan covering one active employee and a number of former employees. Our funding policy with respect to the defined benefit plan is to contribute annually not less than the minimum required by applicable law and regulation to cover the normal cost and to fund supplemental costs, if any, from the date each supplemental cost was incurred.

Contributions are intended to provide not only for benefits attributable to service to date, but also for those expected in the future.

For each of the three-month periods ended February 28, 2007 and 2006, we recorded pension expense of $24,000. In the first fiscal period of 2007, we contributed $10,000 while in the first fiscal period 2006 we contributed $52,500 to our defined benefit plan. We expect to contribute approximately $50,000 to our defined benefit plan in fiscal 2007. The current investment strategy for the defined benefit plan is to invest in conservative debt and equity securities. The expected long-term rate of return on plan assets is 8%.

We also sponsor a 401(k) profit sharing plan for the benefit of all eligible employees, as defined. The plan provides for the employees to make voluntary contributions not to exceed the statutory limitation provided by the Internal Revenue Code. We may make discretionary contributions. There were no discretionary contributions made for the three months ended February 28, 2007 or 2006.

Note 8 Principal Financing Arrangements

We have completed three financings with our principal lender and each financing requires a certain amount of monthly principal payments. We have negotiated with our principal lender a principal deferral of nine months until August 1, 2007 for one of our notes and a deferral until June 1, 2007 on another note that we anticipate paying off if we close on the definitive purchase agreement we signed on December 14, 2006 to sell our CLEC subsidiaries. In consideration for the principal deferral, on April 16, 2007 we issued to our lender a seven-year warrant to purchase 1,200,000 shares of our common stock at a price of $0.25. We are in default with our lender for not filing this Report on a timely basis, and we anticipate that we will not be able to make the principal payments due on June 1, 2007 unless we are successful in the selling of our CLEC subsidiaries before then. Because of the default on such debt, the debt can be called immediately, and we have classified it as a current liability on our balance sheet and the related debt finance costs are shown as a current asset.

Note 9-Income Taxes

At November 30, 2005, we had net operating loss carryforwards for Federal income tax purposes of approximately $25,400,000 expiring in the years 2008 through 2026. There is an annual limitation of approximately $187,000 on the utilization of approximately $2,400,000 of such net operating loss carryforwards under the provisions of Internal Revenue Code Section 382. We did not provide for a tax benefit, since it is more likely than not that any such benefit would not be realized.

Note 10 - Sale of Subsidiaries

On December 14, 2006, we entered into two separate definitive purchase agreements ( Agreements ) to sell our two wholly-owned subsidiaries that function as competitive local exchange carriers ( CLECs ) to Cyber Digital, Inc. ( Purchaser ), a publicly-traded shell company. The planned sales are subject to the receipt of required regulatory approvals, and the Purchaser has reported that the approvals have been issued and the written orders will be forthcoming during the first week of May 2007.

In accordance with an amendment to the Agreements, if the closing of the transaction has not occurred by May 12, 2007, the Purchaser or we may terminate the Agreements with no penalty to the terminating party, so long as such delay in closing the transaction is not the result of willful and material breach by the terminating party of any of its obligations under the Agreement. Since the Purchaser is a shell company with no significant tangible assets that requires financing in order to complete this purchase, we are precluded from presenting these subsidiaries as discontinued operations for the quarter ended February 28, 2007. The consummation of this transaction will require the approval of our principal lender.

Note 11 - Business Segment Information

The Company has two reportable business segments: Wireline Telecommunications Services and IP Telecommunications Services. The operating results of these business segments are distinguishable and are regularly reviewed by the Company s chief operating decision maker.

The Wireline Telecommunication Services business segment resells telephone services that run on a wireline network provided by Verizon and Qwest. The IP Telecommunications business segment provides a range of voice telephony service that run over the Internet.

| | Wireline Telecommunication Services | IP Telecommunication Services | Corporate | Total |
|---|---|---|---|---|
| Quarter ended February 28, 2007 | | | | |
| Revenues | $1,552,233 | $188,890 | - | $1,741,123 |
| Operating income (loss) | 131,516 | (614,831) | (341,145) | (824,460) |
| Depreciation and amortization | 3,120 | 51,402 | 119,017 | 173,539 |
| Other income and (expense) | - | (8,422) | (1,167,576) | (1,175,998) |
| Total assets at February 28, 2007 | 838,228 | 1,077,259 | 1,021,278 | 2,936,765 |
| Quarter ended February 28, 2006 | | | | |
| Revenues | $2,471,993 | $24,861 | - | $2,496,854 |
| Operating income (loss) | 334,744 | (435,096) | (273,612) | (373,964) |
| Depreciation and amortization | 2,011 | 29,657 | 54,957 | 86,625 |
| Other income and (expense) | 817 | (2,282) | (288,050) | (289,515) |
| Total assets at February 28, 2006 | 1,392,624 | 842,504 | 843,500 | 3,078,628 |

**Item 2. Management s Analysis and Discussion of Financial Condition and Results of Operations**

*The statements contained in this Report that are not historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to our financial condition, results of operations and business, which can be identified by the use of forward-looking terminology, such as estimates, projects, plans, believes, expects, anticipates, intends, or the negative thereof or other variations thereon, or by discussions of strategy that involve risks and uncertainties. Management wishes to caution the reader of the forward-looking statements that such statements, which are* *contained in this Report, reflect our current beliefs with respect to future events and involve known and unknown risks, uncertainties and other factors, including, but not limited to, economic, competitive, regulatory, technological, key employee, and general business factors affecting our operations, markets, growth, services, products, licenses and other factors discussed in our other filings with the Securities and Exchange Commission, and that these statements are only estimates or predictions. No assurances can be given regarding the achievement of future results, as actual results may differ materially as a result of risks facing us, and actual events may differ from the assumptions underlying the statements that have been made regarding anticipated events. Factors that may cause our actual results, performance or achievements, or industry results, to differ materially from those contemplated by such forward-looking statements include, without limitation those factors set forth under Note 4 Risks and Uncertainties.*

*These forward-looking statements are subject to numerous assumptions, risks and uncertainties that may cause our actual results to be materially different from any future results expressed or implied by us in those statements. These risk factors should be considered in connection with any subsequent written or oral forward-looking statements that we or persons acting on our behalf may issue. All written and oral forward looking statements made in connection with this Report that are attributable to us or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. Given these uncertainties, we caution investors not to unduly rely on our forward-looking statements. We do not undertake any obligation to review or confirm analysts expectations or estimates or to release publicly any revisions to any forward-looking statements to reflect events or circumstances after the date of this Report or to reflect the occurrence of unanticipated events. Further, the information about*

*our intentions contained in this Report is a statement of our intention as of the date of this Report and is based upon, among other things, the existing regulatory environment, industry conditions, market conditions and prices, the economy in general and our assumptions as of such date. We may change our intentions, at any time and without notice, based upon any changes in such factors, in our assumptions or otherwise.*

**Overview**

We are a provider of local, long distance and international voice telephone services. We provide these services over wirelines, using leased facilities of other carriers, and over broadband services, using our own IP telephony product. IP telephony is the real time transmission of voice communications in the form of digitized packets of information over the Internet or a private network, which is analogous to the way in which e-mail and other data is transmitted. We use proprietary softswitch technology that runs on Cisco and Dell hardware to provide broadband telephone services to other service providers, such as cable operators, Internet service providers, WiFi and fixed wireless broadband providers, data integrators, value-added resellers and satellite broadband providers. Our technology enables these carriers to quickly and inexpensively offer premiere broadband telephone services, complete with order flow management for efficient provisioning, billing and support services and user interfaces that are easily customized to reflect the carrier s unique brand.

The worldwide rollout of broadband voice services has allowed consumers and businesses to communicate at dramatically reduced costs in comparison to traditional telephony networks. Traditionally, telephone service companies have built networks based on circuit switching technology, which creates and maintains a dedicated path for individual telephone calls until the call is terminated. While circuit-switched networks have provided reliable voice communications services for more than 100 years, transmission capacity is not efficiently utilized in a circuit-switched system. Under circuit-switching technology, when a person makes a telephone call, a circuit is created and remains dedicated for the entire duration of that call, rendering the circuit unavailable for the transmission of any other calls. Because of the high cost and inefficiencies of a circuit-switched network, we have never owned a circuit-switched network. Instead, we have leased circuit-switched network elements from other carriers in order to provide wireline services to customers.

Data networks, such as IP networks, utilize packet switching technology that divides signals into packets and simultaneously routes them over different channels to a final destination where they are reassembled into the original order in which they were transmitted. No dedicated circuits are required and a fixed amount of bandwidth is not needed for the duration of each call. The more efficient use of network capacity results in the ability to transmit significantly higher amounts of traffic over a packet-switched network than a circuit-switched network. Packet-switching technology enables service providers to converge traditional voice and data networks in an efficient manner by carrying voice, fax, video and data traffic over the same network. IP networks are therefore less expensive for carriers to operate, and these cost savings can be passed on to the consumer in the form of lower costs for local, long distance and international long distance telephone services.

We have created our own Linux-based IP platform and have transitioned into a facilities-based broadband service provider to take advantage of the network cost savings that are inherent in an IP network. We have signed a contract to sell our leased lines telephone business

to another company, so that we can focus our resources and our energies on our broadband voice product. In addition to the cost savings we obtain from the efficient use of network capacity, we believe our network equipment costs are lower than most other carriers as our network and technology require significantly less capital expenditures than a traditional Class 5 telecom switch in a circuit-switched network, and less equipment costs than our broadband voice competitors that utilize a packet-switched network. Our proprietary softswitch provides more than 20 of the Class 5 call features, voice mail and enhanced call handling on our own Session Initiation Protocol ( SIP ) server suite. We control all of the features we offer to broadband voice customers, because instead of a relying on a software vendor, we write the code for any new features that we desire to offer our customers. We have no software licensing fees and our other variable network costs are expected to drop as we increase our network traffic and as we attract more pure IP telephony users with traffic that does not incur the cost of originating or terminating on a circuit- switched network.

Our SIP servers are part of a cluster of servers, which we refer to as a server farm, in which each server performs different network tasks, including back-up and redundant services. We believe the server farm structure can be easily and cost-effectively scaled as our broadband voice business grows. In addition, servers within our server farm can be assigned different tasks as demand on the network dictates. If an individual server ceases to function, our server farm is designed in a manner that subscribers should not have a call interrupted. We support origination and termination using both the G.711 and G.729 voice codecs. Codecs are the algorithms that enable us to carry analog voice traffic over digital lines. There are several codecs that vary in complexity, bandwidth required and voice quality. We primarily use G.711 and G.729 codecs. G.711 is a standard to represent 8 bit compressed pulse code modulation samples for signals of voice frequency. It creates a 64 kilobit per second bitstream, and we find that approximately 90% of the current IP telephony traffic in the United States uses G.711. We frequently process G.711 traffic because some of our wholesale customers do not have the ability to handle G.729. We prefer the G.729 codec, which allows us to utilize the Internet in more cost effective ways. It allows for compressing more calls in limited bandwidth, reducing the call to 8 kilobits per second. For all of our retail customers and our more sophisticated wholesale accounts, we use G.729 to save cost and enhance the quality of the call.

***Plan of Operation***

Our objective is to build a profitable telephone company on a stable and scalable platform with minimal network costs. We want to be known for our high quality of service, robust features and ability to deliver any new product to a wholesale customer or a web store without delay. We believe that to achieve our objective we need to have cradle to grave automation of our back-office web and billing systems. We have written our software for maximum automation, flexibility and changeability.

We know from experience in provisioning complex telecom orders that back-office automation is a key factor in keeping overhead costs low. Technology continues to work for 24 hours a day and we believe that the fewer people a company has in the back office, the more efficiently it can run, which should drive down the cost per order.

Furthermore, our strategy is to grow rapidly by leveraging the capital, customer base and marketing strength of our wholesale customers. Many of our targeted wholesale customers and some of our existing wholesale customers have ample capital to market a private-labeled broadband voice product to their existing customer base or to new customers. We believe our strength is our technology-based platform. By providing our technology to cable companies, CLECs, ISPs, WiFi and fixed-wireless broadband providers, data integrators, value-added resellers, and satellite broadband providers and any other entity that desires to offer a broadband telephony product, we believe we will require significantly less cash resources than other providers will require to attract a similar number of subscribers.

By taking a wholesale approach, our goal is to obtain and manage 500 customers that have an average customer base of 1,000 end-users. We believe we will be more successful and more profitable taking this approach to reaching 500,000 end-users than we would be if we tried to attract and manage 500,000 individual end-users by ourselves.

Three Months Ended February 28, 2007 vs. Three Months Ended February 28, 2006

Our revenue for the three-month period ended February 28, 2007 decreased by approximately $756,000, or approximately 30%, to approximately $1,741,000 as compared to approximately $2,497,000 reported for the three-month period ended February 28, 2006. The reduction in revenues was directly related to the decrease in the customer base or number of local access lines served by our two CLECs, New Rochelle Telephone Corp. and Telecarrier Services Inc. In lieu of telemarketing new CLEC customers, over the past year we used our financial resources to further build and enhance our IP telephony operations. Consequently, while our CLEC sales declined in the first quarter of fiscal 2007 as compared to the comparative quarter of fiscal 2006, our IP telephony revenue increased by approximately $164,000 period over period.

from $25,000 in the first quarter of fiscal 2006 to $189,000 in the first quarter of fiscal 2007. We anticipate that our CLECs will be divested to a third-party purchaser during the second quarter of fiscal 2007 and that future revenues will be derived from IP telephony only.

The roll-out of our broadband voice product has taken significantly longer than we anticipated. We believe a key reason for the delay was the extensive effort required for us to become a customized wholesale service provider. Because of the intense competition on the retail level and the high marketing costs that broadband voice providers have incurred to acquire a subscriber, we decided that we should not compete in the retail arena. Our goal is to obtain 500 customers that will private label and resell our broadband voice services to their customer base. We target cable operators that already are providing broadband Internet services, Internet service providers, WiFi and fixed wireless broadband providers, data integrators, value-added resellers, and satellite broadband providers. We anticipate that our wholesale customers will be able to obtain an average of at least 1,000 broadband voice end-users. We believe our approach, in which we are seeking at least 500 customers that we will manage, and a total of at least 500,000 end users, which our customers will manage, will provide us with the quickest and least expensive way to leverage our technology. Under our approach, we will avoid the expensive customer acquisition costs that other broadband voice carriers are experiencing as they try to find a broadband end-user to try their product. Instead of incurring these costs our self, our customer, which should be able to incur a reduced marketing expense because it has an imbedded customer base already buying broadband service, will incur them. We believe we can empower small and medium-sized broadband providers with the ability to take customers away from the traditional telephone companies.

Our IP telephony facilities have significant unused capacity and we have begun to attract other types of customers to utilize our facilities. For example, we are actively pursuing both buyers and sellers of international cell phone termination minutes. We have sales personnel who

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have previously worked in these markets, and by targeting cell phone termination we are able to realize a higher per minute billing rate and profit, than we would realize on a wireline.

Our gross profit for the three-month period ended February 28, 2007 decreased by approximately $539,000 to approximately $538,000 from approximately $1,077,000 reported in the three-month period ended February 28, 2006. During the same fiscal periods, our gross profit percentage decreased to 30.9% from 43.1%. The decrease in our gross profit resulted primarily from the decrease in the size of our customer base in first quarter of fiscal 2007 relative to the first quarter of fiscal 2006. The decrease in our gross profit percentage during the 2007 period resulted from the higher cost of services that we are now incurring under our wholesale services agreement with Verizon and the higher IP network costs we are now incurring due to the low utilization rate of our IP facilities. While it is difficult for us to predict the gross margins we will achieve on our IP lines because we are offering a variety of wholesale products and our gross margin will be impacted by the product mix, based on current pricing, we anticipate that when we have a sufficient quantity of subscribers, mature wholesale accounts will generate a gross margin of approximately 25% to 40%.

Selling, general and administrative expenses decreased by approximately $107,000, or approximately 9%, to approximately $1,140,000 for the three-month period ended February 28, 2007 from approximately $1,247,000 reported in the same prior year fiscal period. Our salary cost decreased by approximately $115,000 in the first quarter of 2007 over the same period last year.

Our bad debt expense decreased by approximately $69,000, or approximately 58%, to approximately $49,000 for the three months ended February 28, 2006 from approximately $118,000 reported in the prior fiscal period. This decrease was related to the reduction in the number of customers we had during the 2007 period and the fact that the remaining customers represent a mature base that has consistently paid their bills.

Depreciation and amortization expense increased by approximately $87,000 for the three months ended February 28, 2007 to approximately $174,000 as compared to approximately $87,000 for the same period in fiscal 2006. Approximately $66,000 of the increase was for deferred financing costs related to our financing agreements and approximately $21,000 related to our VoIP platform.

Interest expense decreased by approximately $55,000 to approximately $227,000 for the three months ended February 28, 2007 as compared to approximately $281,000 for the three months period ended February 28, 2006. The decrease is due to lower effective borrowing rates in the 2007 quarter and the reversal of an accrual for default interest of approximately $42,000 that our lender has notified us that we will not have to pay. The cash payment portion of the $227,000 in interest expense amounted to approximately $129,000. The remaining balance represented the accretion of a debt discount using the effective interest method over the term of the related debt.

Other income decreased by approximately $3,000, to approximately $11,000 for the three months ended February 28, 2007 as compared to approximately $14,000 for the three months ended February 28, 2006. The decrease resulted from a reduction in commission income.

Warrant expense for the three months ended February 28, 2007, amounted to approximately $960,000 due to the significant increase in the market value of our common stock

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between the period of November 30, 2006 to February 28, 2007, as compared to the expense of approximately $22,000 for the same period in fiscal 2006.

Liquidity and Capital Resources

At February 28, 2007, we had cash and cash equivalents of approximately $311,000 and negative working capital of approximately $7,021,000.

Net cash used in operating activities aggregated approximately $964,000 and $837,000 in the three-month periods ended February 28, 2007 and 2006, respectively. The principal use of cash in fiscal 2007 was the loss for the period of approximately $2,000,000 which was partially offset by a non-cash mark to market warrant adjustment of $960,000. The principal use of cash in fiscal 2006 was the loss for the period of $664,000.

Net cash used in investing activities in the three-month periods ended February 28, 2007 and 2006 aggregated approximately $52,000 and $123,000, respectively, resulting primarily from expenditures related to our VoIP initiative.

Net cash (used in) provided by financing activities aggregated approximately ($11,000) and $1,422,000 in the three-month periods ended February 28, 2007 and 2006, respectively. In fiscal 2007, net cash used in financing activities was the repayment of long-term lease obligations. In fiscal 2006, net cash provided by financing activities resulted from the proceeds of long-term notes of approximately $1,753,500, which was partially offset by the repayment of short-term debt of approximately $328,000.

For the three months ended February 28, 2007, we had approximately $52,000 in capital expenditures primarily related to our IP telephony business. We expect to make equipment purchases of approximately $50,000 to $100,000 in the second fiscal quarter of 2007. We expect that other capital expenditures over the next 12 months will relate primarily to a continued roll-out of VoIP services and will only be required to support a growing customer base of IP telephony subscribers.

Subsequent to February 28, 2007, we have negotiated with our primary lender a principal deferral of nine months for one of our notes and a deferral until June 1, 2007 on another note that we anticipate paying off if we close on the definitive purchase agreement we signed on December 14, 2006 to sell our CLEC subsidiaries. In consideration for the principal deferral, on April 16, 2007 we issued to our lender a seven-year warrant to purchase 1,200,000 shares of our common stock at a price of $0.25. We are in default with our lender for not filing this Report on a timely basis, and we anticipate that we will not be able to make the principal payments due on June 1, 2007 unless we are successful in selling of our CLEC subsidiaries before then. Because of the default on such debt, the debt can be called immediately, and we have classified it as a current liability on our balance sheet and the related debt finance costs are shown as a current asset. If our lender accelerates such debt, we will not be able to satisfy such indebtedness in full, which inability would adversely affect our ability to continue operating as a going concern.

The report of our independent registered public accounting firm on our 2006 financial statements indicates there is substantial doubt about our ability to continue as a going concern. Our operating losses have been funded through the sale of non-operating assets, the issuance of equity securities and borrowings. We believe our current cash resources will not be sufficient to finance our operations. Accordingly, we have engaged a placement agent to raise us up to $1.5 million in equity to support our operating losses. There can be no assurance that such financing will be sufficient to get us to a break-even level, or that the agent will be able to raise the full amount. Our failure to generate sufficient revenues and raise additional capital will have an adverse impact on our ability to achieve our longer-term business objectives, and would adversely affect our ability to continue operating as a going concern.

**Item 3. Quantitative and Qualitative Disclosure About Market Risk**

Our outstanding debt is primarily under three borrowing arrangements with one lender and such borrowings are at the rate of 2% over the prime rate. We currently do not use interest rate derivative instruments to manage our exposure to interest rate changes. As a result of conversion features, warrant issuances and lender discounts, the effective rate of interest has been calculated at rates of approximately 38% on our February 2005 financing, 47% on our November 2005 financing, and 185% on the $650,000 portion of our May 2006 financing.

**Item 4. Controls and Procedures**

(a) *Disclosure Controls and Procedures*. Our management, with the participation of our chief executive officer/chief financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the

Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this Report. Based on such evaluation, our chief executive officer/chief financial officer has concluded that, as of the end of such period, for the reasons set forth below, our disclosure controls and procedures were not effective. We are presently taking the necessary steps to improve the effectiveness of such disclosure controls and procedures.

(b) *Internal Control Over Financial Reporting*. There have not been any changes in our internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the first quarter of 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. In connection with our year-end November 30, 2006 audit, our management became aware of an inadequately designed accounting system as it pertains to our VoX subsidiary. As reported in fiscal 2006 and 2005, we also have a lack of staffing within our accounting department, both in terms of the small number of employees performing our financial and accounting functions and their lack of experience to account for complex financial transactions. Management believes the lack of qualified personnel, in the aggregate, and the inadequately designed accounting system, are both a material weakness in our internal control over financial reporting. We have updated and enhanced our internal reporting at VoX and we will continue to evaluate the number of accounting employees we utilize, the need to engage outside consultants with technical and accounting-related expertise to assist us in accounting for complex financial transactions and the hiring of additional accounting staff with complex financing experience.

We also are evaluating our internal controls systems so that when we are required to do so, our management will be able to report on, and our independent auditors to attest to, our internal controls, as required by Section 404 of the Sarbanes-Oxley Act of 2002. We will be performing the system and process evaluation and testing (and any necessary remediation) required in an effort to comply with the management certification and auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act. In connection with our year-end November 30, 2006 and 2005 audits, we identified the following control deficiencies and issues

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with our internal controls over financial reporting that we believe amount in the aggregate to a significant deficiency in our internal controls over financial reporting:

Due to the voluminous nature of state and local telecom taxes and the small quantity of taxes payable to certain municipalities, we do not remit all our telecom taxes in a timely manner. Certain taxes that we should be remitting on a monthly basis, we remit quarterly or semi-annually because many of the checks and returns that we are processing are for insignificant amounts. We are aware of other telephone companies that follow this process. We continue to monitor the responses, if any, we receive from the tax authorities regarding late filings and we intend to remit such taxes in a timely manner in the future.

Due to the complex nature and changing regulations regarding telecom taxes, we do not always calculate and remit the appropriate amount of taxes due. We are challenging taxes that one state claims are owed to it. At least some of the taxes are due because of the improper calculation of taxes that should have been billed to and collected from our wireline telephone customers in one particular state.

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**eLEC COMMUNICATIONS CORP.**

**PART II-OTHER INFORMATION**

**Item 6.** **Exhibits**

| Exhibit Number | Description |
|---|---|
| 31.1 | Certification of our Chief Executive Officer and Chief Financial Officer, Paul H. Riss, Pursuant to 18 U.S.C. 1350 (Section 302 of the Sarbanes-Oxley Act of 2002) |
| 32.1 | Certification of our Chief Executive Officer and Chief Financial Officer, Paul H. Riss, Pursuant to 18 U.S.C. 1350 (Section 906 of the Sarbanes-Oxley Act of 2002) |

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

eLEC Communications Corp.

Date: April 20, 2007

By: /s/ Paul H. Riss
Paul H. Riss
Chief Executive Officer
(Principal Financial and
Accounting Officer)

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EXHIBIT INDEX

| Exhibit Number | Description |
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**EXHIBIT 31.1**

CERTIFICATION

Pursuant to 18 U.S.C. 1350
(Section 302 of the Sarbanes-Oxley Act of 2002)

I, Paul H. Riss, Chief Executive Officer and Chief Financial Officer of eLEC Communications Corp., certify that:

1. I have reviewed this quarterly report on Form 10-Q of eLEC Communications Corp.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and I have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the registrant s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the registrant s internal control over financial reporting that occurred during the registrant s most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant s internal control over financial reporting; and

5. I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant s auditors and the audit committee of the registrant s board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant s ability to record, process, summarize and report financial information; and

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(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant s internal control over financial reporting.

Date: April 20, 2007

/s/ Paul H. Riss
Paul H. Riss
Chief Executive Officer and Chief Financial Officer

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**EXHIBIT 32.1**

**CERTIFICATION**
Pursuant to 18 U.S.C. 1350
(Section 906 of the Sarbanes-Oxley Act of 2002)

In connection with the Quarterly Report on Form 10-Q of eLEC Communications Corp. (the "Company") for the quarter ended February 28, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Paul H. Riss, as Chief Executive Officer and Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

Date: April 20, 2007 By: /s/ Paul H. Riss
Paul H. Riss
Chief Executive Officer and Chief Financial Officer

This certification accompanies each Report pursuant to § 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of §18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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