

UCN INC  
Form 10-Q/A  
April 01, 2008  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

**FORM 10-Q/A**

(Amendment No. 1)

**Quarterly report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934**  
For the quarterly period ended June 30, 2007

or

**Transition report pursuant to section 13 or 15(d) of the Securities Exchange act of 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No. 1-33762

**UCN, INC.**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**87-0528557**  
(IRS Employer  
Identification No.)

**14870 Pony Express Road, Bluffdale, Utah 84065**  
(Address of principal executive offices and Zip Code)

**(801) 320-3300**  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 28,431,589 shares of common stock as of August 14, 2007.

**Table of Contents****Explanatory Note**

The Audit Committee of the Board of Directors recently received the results of an independent investigation into certain accounting and financial reporting matters. The results of the investigation as well as results of additional reviews and procedures conducted by management were reported to the Board of Directors. As a result, the Board of Directors determined that our previously issued condensed consolidated financial statements filed with our quarterly reports on Form 10-Q for the quarters ended September 30, June 30, and March 31, 2007, and our consolidated financial statements for the year ended December 31, 2006, should no longer be relied upon because of certain accounting errors in the disclosures to the financial statements. Accordingly, we are restating our previously issued financial statements for those periods. The effects of the restatements of the condensed consolidated financial statements are limited to the footnote disclosure of operating segment results and do not affect our Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Operations, Condensed Consolidated Statements of Stockholders' Equity, and Condensed Consolidated Statements of Cash Flows. Restated financial information is presented in this report, as well as in our amended reports on Form 10-Q for the periods ended March 31, 2007 and September 30, 2007. We do not intend to file an amendment to our Form 10-K for the year ended December 31, 2006; rather the restatement of 2006 segment disclosures will be presented in our Form 10-K for the year ended December 31, 2007. For a discussion of the accounting errors and the adjustments made as a result of the restatement, see Note 11 of Notes to Condensed Consolidated Financial Statements included in Part I Item 1 Financial Statements and Part I Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations - Segment Reporting. This Form 10-Q/A does not reflect events that occurred after the August 14, 2007 filing date of the Quarterly Report on Form 10-Q that was originally filed, or modify or update the disclosures presented in the original Form 10-Q, except to reflect the matters described above. Other events occurring after the filing of the original Form 10-Q or other disclosures necessary to reflect subsequent events have been addressed in our reports filed with the Securities and Exchange Commission subsequent to the filing of the original Form 10-Q.

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**Table of Contents****UCN, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)***(in thousands except share data)*

	June 30, 2007	December 31, 2006
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 2,394	\$ 4,559
Restricted cash		10
Accounts and other receivables, net of allowance for uncollectible accounts of \$1,654 and \$1,746, respectively	9,441	8,996
Other current assets	477	594
<b>Total current assets</b>	<b>12,312</b>	<b>14,159</b>
Property and equipment, net	5,386	4,810
Intangible assets, net	8,701	6,373
Goodwill	1,634	
Other assets	530	617
<b>Total assets</b>	<b>\$ 28,563</b>	<b>\$ 25,959</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$ 603	\$ 720
Trade accounts payable	7,137	8,350
Accrued liabilities	2,156	2,024
Accrued commissions	1,277	1,448
Deferred revenue	117	
<b>Total current liabilities</b>	<b>11,290</b>	<b>12,542</b>
Long-term debt and revolving credit note	3,972	6,523
Other long-term liabilities and deferred revenue	55	46
<b>Total liabilities</b>	<b>15,317</b>	<b>19,111</b>
Commitments and contingencies (Notes 3, 7, 9 and 10)		
Stockholders' equity:		
Common stock, \$0.0001 par value; 100,000,000 shares authorized; 28,428,589 and 25,385,031 shares issued and outstanding as of June 30, 2007 and December 31, 2006, respectively	3	3
Additional paid-in capital	59,643	50,071
Warrants and options outstanding	1,330	1,268
Accumulated deficit	(47,730)	(44,494)
<b>Total stockholders' equity</b>	<b>13,246</b>	<b>6,848</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 28,563</b>	<b>\$ 25,959</b>

See notes to condensed consolidated financial statements



**Table of Contents****UCN, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)***(in thousands except per share data)*

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Revenue	\$ 19,975	\$ 20,968	\$ 39,795	\$ 43,590
Operating expenses:				
Costs of revenue (excluding depreciation and amortization shown separately below)	11,128	13,580	22,665	29,063
Selling and promotion	4,102	3,432	7,952	7,050
General and administrative	4,164	3,223	7,862	6,478
Depreciation and amortization	1,495	1,865	3,288	3,744
Research and development	447	352	875	664
Total operating expenses	21,336	22,452	42,642	46,999
Loss from operations	(1,361)	(1,484)	(2,847)	(3,409)
Other income (expense):				
Interest income	3	42	18	82
Interest expense	(202)	(326)	(402)	(584)
Loss on early extinguishment of debt		(364)		(364)
Total other expense	(199)	(648)	(384)	(866)
Loss before income taxes	(1,560)	(2,132)	(3,231)	(4,275)
Income tax expense	2	8	5	8
Net loss	\$ (1,562)	\$ (2,140)	\$ (3,236)	\$ (4,283)
Net loss per common share:				
Basic and diluted	\$ (0.06)	\$ (0.09)	\$ (0.12)	\$ (0.18)
Weighted average common shares outstanding:				
Basic and diluted	28,166	24,053	27,243	23,588

See notes to condensed consolidated financial statements

**Table of Contents****UCN, INC.****CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY (Unaudited)***(in thousands)*

	Common Stock					
	Shares	Amount	Additional	Warrants/	Accumulated	Total
Balance at January 1, 2007	25,385	\$ 3	\$ 50,071	\$ 1,268	\$ (44,494)	\$ 6,848
Exercise of stock options to purchase common shares	235		574			574
Stock-based compensation			599			599
Warrant issued in conjunction with consulting agreement				68		68
Warrants issued to lender for approval of BenchmarkPortal acquisition (Note 3)				83		83
Shares issued due to cashless warrant exercise	37		189	(189)		
Issuance of common shares in conjunction with BenchmarkPortal acquisition (Note 3)	1,536		4,500			4,500
Issuance of common shares in conjunction with ScheduleQ acquisition (Note 3)	109		330			330
Conversion of ComVest convertible term note	1,127		3,380			3,380
Warrants issued in conjunction with investor relations agreement				100		100
Net loss					(3,236)	(3,236)
Balance at June 30, 2007	28,429	\$ 3	\$ 59,643	\$ 1,330	\$ (47,730)	\$ 13,246

See notes to condensed consolidated financial statements

**Table of Contents****UCN, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)***(in thousands)*

	<b>Six months ended June 30,</b>	
	<b>2007</b>	<b>2006</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$ (3,236)	\$ (4,283)
<b>Adjustments to reconcile net loss to net cash used in operating activities:</b>		
Depreciation and amortization	3,288	3,744
Amortization of note financing costs	379	83
Stock-based compensation	599	297
Warrants issued for consulting services	143	
Loss on early extinguishment of debt		364
<b>Changes in operating assets and liabilities (net effects of acquisitions):</b>		
Accounts and other receivables, net	142	944
Other current assets	179	69
Other non-current assets	(259)	33
Trade accounts payable	(1,471)	(2,774)
Accrued liabilities	141	(289)
Accrued commissions	(171)	(89)
Deferred revenue	(246)	
<b>Net cash used in operating activities</b>	<b>(512)</b>	<b>(1,901)</b>
<b>Cash flows from investing activities:</b>		
Decrease in restricted cash	10	641
Acquisition of BenchmarkPortal, Inc.	(500)	
Contingent purchase price payments to BenchmarkPortal stockholders	(166)	
Contingent purchase price payments to ScheduleQ stockholders	(6)	
Direct acquisition costs	(245)	
Purchases of property and equipment	(1,299)	(632)
<b>Net cash provided by (used in) investing activities</b>	<b>(2,206)</b>	<b>9</b>
<b>Cash flows from financing activities:</b>		
Net borrowings and payments under line of credit	500	664
Principal payments on long-term debt	(265)	(3,639)
Principal payments on long-term debt assumed in conjunction with the acquisition of ScheduleQ	(256)	
Proceeds from exercise of options and warrants	574	141
Private placement offering, net of offering costs		4,211
Debt financing costs		(186)
Payments on early extinguishment of debt		(377)
<b>Net cash provided by financing activities</b>	<b>553</b>	<b>814</b>
<b>Net decrease in cash and cash equivalents</b>	<b>(2,165)</b>	<b>(1,078)</b>
Cash and cash equivalents at the beginning of the period	4,559	5,471
<b>Cash and cash equivalents at the end of the period</b>	<b>\$ 2,394</b>	<b>\$ 4,393</b>

(continued)



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See notes to condensed consolidated financial statements

**Table of Contents****UCN, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)***(in thousands)*

	<b>Six months ended June 30,</b>	
	<b>2007</b>	<b>2006</b>
<b>Supplemental cash flow information:</b>		
Cash paid for interest	\$ 307	\$ 423
Cash paid for income taxes	\$ 8	\$ 2
<b>Supplemental schedule of non-cash investing and financing activities:</b>		
Issuance of common stock related to acquisition of BenchmarkPortal Inc. (Note 3)	\$ 4,500	\$
Issuance of long-term debt related to the acquisition of Benchmark Portal	100	
Conversion of convertible term note at \$3.00 per share for 1,126,664 share of common stock (Notes 6 and 8)	3,380	
Issuance of common stock related to ScheduleQ acquisition (Note 3)	330	
Issuance of long-term debt related to the acquisition of ScheduleQ (Note 3)	302	
Assumption of long-term debt issued to the acquisition of ScheduleQ (Note 3)	256	
Cashless warrant exercise (Note 8)	189	
Warrants issued to lender for approval of BenchmarkPortal acquisition (Note 3)	83	
Contingent purchase price payments to BenchmarkPortal stockholders included in accounts payable (Note 4)	56	
Property and equipment included in accounts payable	52	183
Fee charged by lender for approval of BenchmarkPortal acquisition applied to revolving credit facility (Note 3)	40	
Fee charged by lender for modification of certain debt covenants applied to revolving credit facility	35	
Issuance of warrants with debt agreement		542
Property and equipment financed with capital lease obligations		196
		(concluded)

During the first quarter of 2007, UCN completed two acquisitions and acquired all outstanding equity of BenchmarkPortal, Inc. and ScheduleQ, LLC. See Note 3 for a disclosure of assets acquired and liabilities assumed through these acquisitions.

See notes to condensed consolidated financial statements

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**UCN, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**For the three and six months ended June 30, 2007 and 2006**

(unaudited)

**NOTE 1 BASIS OF PRESENTATION**

These unaudited interim financial statements of UCN, Inc. and its subsidiaries (collectively "UCN") have been prepared in accordance with the rules and regulations of the United States Securities and Exchange Commission ("SEC"). Such rules and regulations allow the omission of certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States, so long as the statements are not misleading. In the opinion of management, these financial statements and accompanying notes contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly the financial position and results of operations for the periods shown. These interim financial statements should be read in conjunction with the audited financial statements and notes thereto contained in the Annual Report on Form 10-K for the year ended December 31, 2006, as filed with the SEC on March 28, 2007. The results of operations for the three and six month periods ended June 30, 2007 are not necessarily indicative of the results to be expected for the full year.

UCN experienced net losses of \$3.2 million and \$4.3 million for the six months ended June 30, 2007 and 2006, respectively. Included within the net loss during the year were: 1) \$3.3 million of depreciation and amortization; 2) \$599,000 of non-cash stock-based compensation expense (Note 9) and 3) \$168,000 in non-cash expense related to two consulting agreements that were satisfied through the issuance of warrants.

UCN's working capital surplus of \$1.6 million at December 31, 2006 decreased to \$1.0 million at June 30, 2007. The primary reason for the reduction in working capital was due to a \$2.2 million decrease in cash. This decrease in cash was driven by a \$1.2 million reduction in accounts payable as well as an increase of \$445,000 in accounts receivable due to the normal business timing of cash payments and collections. This decrease in cash was partially offset by an \$117,000 decrease in the current portion of long-term debt due to the conversion of the ComVest \$3.4 million convertible term note. This conversion will save UCN an estimated \$468,000 in cash payments during 2007 and will significantly improve the current ratio in future periods by eliminating the associated current portion of long-term debt.

In addition to the cash amount listed on the condensed consolidated balance sheets, the Company also has access to additional available borrowings under the revolving credit facility. The available borrowings under the revolving credit facility increased \$1.4 million to \$3.6 million at June 30, 2007 compared to \$2.2 million available at December 31, 2006, resulting in total cash and additional availability under the revolving credit facility of \$6.0 million as of June 30, 2007.

The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should UCN be unable to continue as a going concern. UCN's continuation as a going concern is dependent upon the ability to generate sufficient cash flow to meet obligations on a timely basis and ultimately to achieve successful operations.

UCN has taken the following actions:

On June 29, 2007, UCN filed a shelf registration on Form S-3 with the SEC. Under the terms of this shelf registration, UCN may offer from time to time up to \$12 million in common shares. The registration statement became effective on July 13, 2007 and UCN has not sold any shares under the registration statement.

In February 2007, UCN closed two acquisitions (Note 3), which improved the overall inContact product offering suite. With these new products, UCN provides customers the ability to monitor agent effectiveness through its customer survey tools and the ability to efficiently monitor their agent needs. These new service offerings provide UCN additional inContact and service opportunities to potential customers as well as provide up-sale opportunities to existing customers. These acquisitions added an additional \$1.1 million and \$1.6 million of higher-margin inContact revenue during the three and six months ended June 30, 2007, respectively.

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The inContact segment revenue increased to \$6.0 million during the quarter ended June 30, 2007, a 72% increase from the same period in 2006 for a year to date total of \$10.8 million. This increase was a result of the selling and promotion effort the Company has undertaken to bring these products to market. Excluding the \$1.1 million in revenue from the acquisitions, the segment increased 40% compared to the second quarter of 2006. UCN expects to see continued revenue growth in the inContact segment in 2007 (Note 11).

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Management believes these actions will allow UCN to have sufficient cash flows available to meet short-term requirements and to enable UCN to continue as a going concern.

### **NOTE 2 ACCOUNTING PRONOUNCEMENTS**

#### **Adoption of New Accounting Pronouncements**

**Adoption of FIN 48:** In June 2006, the Financial Accounting Standards Board ( FASB ) issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement 109* ( FIN 48 ). FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing a recognition threshold for tax positions taken or expected to be taken in a tax return. FIN 48 requires that entities recognize in their financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. FIN 48 is effective for fiscal years beginning after December 15, 2006. Interest and penalties, if incurred, would be recognized as components of income tax expense. The Company's adoption of FIN 48 on January 1, 2007 had no impact on the Company's condensed consolidated financial statements as the Company does not have any uncertain income tax positions that would require adjustment.

#### **Recent Accounting Pronouncements**

**Fair Value Measurements** In September 2006, the FASB issued Statement of Financial Accounting Standard (SFAS) 157, *Fair Value Measurements*. SFAS 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on assumptions that market participants would use in pricing the asset or liability. The Company is required to adopt SFAS 157 in the first quarter of 2008. The Company does not expect that the implementation of SFAS 157 will have a material effect on the Company's results of operations or financial position.

**Fair Value Option** In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Liabilities – Including an amendment of FASB Statement No. 115*. SFAS 159 permits entities to choose to measure certain financial assets and liabilities at fair value (the fair value option ). Unrealized gains and losses, arising subsequent to adoption, are reported in earnings. The Company is required to adopt SFAS 159 in the first quarter of 2008. The Company does not expect that the implementation SFAS 159 will have a material effect on the Company's results of operations or financial position.

### **NOTE 3 ACQUISITIONS**

#### *BenchmarkPortal, Inc. Acquisition*

On February 9, 2007, UCN closed the acquisition of BenchmarkPortal, Inc. to enhance and expand the services offered under the inContact suite of services. Through the acquisition of 100% of BenchmarkPortal's outstanding stock, UCN acquired a call center survey and analysis business, operated under the name of Echo<sup>TM</sup>. The Echo business includes: 1) a customer base; 2) automated survey and analysis software and related service offerings; and 3) the related sales, marketing and technical staff. As consideration for the agreement, UCN paid the following:

\$500,000 in cash to or for the benefit of the BenchmarkPortal stockholders at closing; and

\$4,500,000 by issuing 1,535,836 shares of its restricted common stock to BenchmarkPortal stockholders.

In addition to the amounts paid at closing, UCN agreed to pay contingent purchase price payments to BenchmarkPortal stock holders in the following amounts:

\$2.0 million of additional contingent purchase price cash payments to BenchmarkPortal stockholders in 36 equal monthly installments of \$55,556, subject to adjustment if monthly recurring revenue during the payout period from customers' accounts acquired in the transaction do not remain at certain levels which are adjusted for estimated attrition; and

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Up to an additional \$7.0 million maximum contingent quarterly earn out to BenchmarkPortal stockholders paid on a variable percentage of recurring revenue from the sale of Echo services during the four-year period after closing in excess of \$900,000 per quarter.

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The following table summarizes the preliminary allocation of estimated fair values of the assets acquired and liabilities assumed at the date of acquisition (in thousands):

Current assets	\$ 623
Property, plant and equipment	255
Intangibles	3,435
Goodwill	1,300
<b>Total assets acquired</b>	<b>5,613</b>
Current liabilities	(203)
Deferred revenue	(363)
Other long-term liabilities	(47)
<b>Total liabilities assumed</b>	<b>(613)</b>
Net assets acquired	\$ 5,000
Cash paid	\$ 500
UCN common stock issued	4,500
<b>Purchase price</b>	<b>\$ 5,000</b>

*ScheduleQ, LLC Acquisition*

On October 19, 2006, UCN entered into a Reseller License Agreement with ScheduleQ, LLC. Under the terms of the license agreement, UCN acquired a limited exclusive right and continuing non-exclusive right to market and distribute ScheduleQ software and services to end-users. ScheduleQ software and services consist primarily of a platform-based workforce management system for call centers, which can operate through the inContact service. At the same time UCN entered into a Purchase Option Agreement with ScheduleQ and the members of that limited liability company. On February 9, 2007, UCN exercised its option to purchase 100% of the outstanding ownership of ScheduleQ, LLC. The acquisition closed on February 15, 2007. To complete the transaction, UCN paid former members of ScheduleQ the following consideration:

\$360,676 in non-interest bearing promissory notes to be paid in 48 equal monthly installments that are secured by the software code and any improvements thereto discounted to \$302,000 using a discount rate of nine percent;

\$330,000 by issuing 108,912 restricted common shares of UCN; and

\$256,324 in notes assumed and paid subsequently to closing.

In addition to the amounts paid at closing, UCN agreed to pay contingent purchase price to ScheduleQ stock holders in the following amounts:

An earn out to be paid over a term of 48 months based on the number of licenses sold by UCN with a minimum aggregate earn out payment of \$100,000 and a maximum of \$982,000.

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The following table summarizes the preliminary allocation of estimated fair values of the assets acquired and liabilities assumed at the date of acquisition (in thousands):

<b>SQ Acquisition</b>	
Property, plant and equipment	\$ 5
Intangibles	817
Goodwill	102
<b>Total assets acquired</b>	<b>924</b>
Accrued direct acquisition costs	(34)
Assumed notes payable	(256)
Note payable issued	(304)
<b>Total liabilities assumed</b>	<b>(594)</b>
Net assets acquired	\$ 330
<b>UCN common stock issued</b>	<b>\$ 330</b>

The Company has accounted for both the BenchmarkPortal and ScheduleQ transactions using the purchase method of accounting and has included the operating results of each business in UCN's condensed consolidated statements of operations since the respective date of each acquisition. Management has allocated the purchase price to the acquired tangible and intangible assets and liabilities based on their respective fair values. In addition, UCN incurred additional direct acquisition costs of \$308,000 for BenchmarkPortal and \$34,000 for ScheduleQ, which increases the amounts allocated to goodwill. The following unaudited pro forma financial information presents operating results as if both acquisitions had occurred at the beginning of the respective periods (in thousands except per share data):

	<b>Three months ended June 30,</b>	
	<b>2007</b>	<b>2006</b>
Net revenue	\$ 19,975	\$ 21,645
Net loss	(1,562)	(2,166)
Basic and diluted net loss per share	\$ (0.06)	\$ (0.09)
	<b>Six months ended June 30,</b>	
	<b>2007</b>	<b>2006</b>
Net revenue	\$ 40,226	\$ 44,916
Net loss	(3,264)	(4,393)
Basic and diluted net loss per share	\$ (0.12)	\$ (0.19)

These pro forma results have been prepared for comparative purposes only and include certain adjustments such as additional amortization expense as a result of intangible assets arising from the acquisition, additional interest expense as a result of issuing the promissory notes, and depreciation on certain items of equipment acquired. The results are not necessarily indicative either of the results of operations that actually would have resulted had the acquisition been in effect at the beginning of the respective years, or of results to be achieved in the future.

**NOTE 4 INTANGIBLE ASSETS**

Intangible assets consisted of the following (in thousands):

**June 30, 2007**

**December 31, 2006**



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	Gross Assets	Accumulated Amortization	Intangible assets, net	Gross Assets	Accumulated Amortization	Intangible assets, net
Customer lists acquired	\$ 16,495	\$ 13,856	\$ 2,639	\$ 15,684	\$ 12,777	\$ 2,907
Technology and patents	10,314	5,653	4,661	7,980	4,540	3,440
Trade name and trade marks	1,213		1,213			
Goodwill	1,634		1,634			
Non-compete agreement	376	188	188	154	128	26
	\$ 30,032	\$ 19,697	\$ 10,335	\$ 23,818	\$ 17,445	\$ 6,373

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In conjunction with the BenchmarkPortal acquisition (Note 3), UCN recorded the following intangibles as of June 30, 2007 (in thousands):

<b>Intangible asset</b>	<b>Estimated Fair Value</b>	<b>Estimated Useful Life</b>	<b>Amortization Method</b>
Technology and patents	\$ 1,634	5	Straight line
Goodwill	1,526	Indefinite	Impairment review
Trade name and trade marks	1,194	Indefinite	Impairment review
Customer lists acquired	736	10	Accelerated
Non-compete agreement	179	3	Straight line
<b>Total</b>	<b>\$ 5,269</b>		

UCN agreed to pay former BenchmarkPortal stockholders monthly installments of \$55,556 in contingent purchase price payments, subject to adjustment if monthly recurring revenue during the payout period from specified customer accounts acquired does not remain at certain levels, which are adjusted for estimated attrition. During the three and six months ended June 30, 2007, BenchmarkPortal stockholders earned a total of \$177,000 and \$226,000, respectively in contingent purchase price payments that have been recorded to goodwill.

In conjunction with the ScheduleQ acquisition (Note 3), UCN recorded the following intangibles as of June 30, 2007 (in thousands):

<b>Intangible asset</b>	<b>Estimated Fair Value</b>	<b>Estimated Useful Life</b>	<b>Amortization Method</b>
Technology and patents	\$ 699	8	Straight line
Goodwill	108	Indefinite	Impairment review
Customer lists acquired	75	5	Accelerated
Non-compete agreement	43	2	Straight line
<b>Total</b>	<b>\$ 925</b>		

UCN agreed to pay former ScheduleQ members monthly installments in contingent purchase price payments based on based on the number of licenses sold. During the six months ended June 30, 2007, former ScheduleQ members earned a total of \$6,000 in contingent purchase price payments that have been recorded to goodwill.

Amortization of intangibles for the fiscal years ended 2007, 2008, 2009, 2010 and 2011 is expected to be \$4.0 million, \$3.2 million, \$0.9 million, \$0.5 million and \$0.5 million respectively.

**NOTE 5 ACCRUED LIABILITIES**

Accrued liabilities consisted of the following (in thousands):

	<b>June 30, 2007</b>	<b>December 31, 2006</b>
Accrued payroll and other compensation	\$ 975	\$ 656
Accrued payphone and carrier charges	848	782
Operating lease obligations assumed as part of prior acquisition	122	250
Accrued professional fees	133	164
Other	78	172

\$ 2,156      \$ 2,024

**Table of Contents****NOTE 6 LONG-TERM DEBT, NOTES PAYABLE AND CAPITAL LEASES**

As of June 30, 2007, UCN is in compliance with all of its financial and non-financial covenants.

Long-term debt, notes payable and capital leases consist of the following (in thousands):

	June 30, 2007	December 31, 2006
Convertible term note to ComVest Capital, LLC of \$4.5 million was converted into 1,126,664 shares of common stock at \$3.00 per share and paid in full in April 2007 (Note 8)	\$	\$ 3,380
Revolving credit note with ComVest Capital, LLC, with maximum availability of \$7.5 million, bearing interest at a fixed 9.0 percent, there are no requirements to repay outstanding principal payments until May 2010	3,838	3,258
Promissory notes payable to former ScheduleQ, LLC shareholders, interest imputed at 9.0 percent, payable monthly, secured by the software code acquired and any improvements thereto. Principal payments due monthly, final principal payment due February 15, 2011 (Note 3)	281	
Capital Leases	809	1,042
	4,928	7,680
Current portion of long-term debt	(68)	(250)
Current portion of capital lease payments	(656)	(636)
Debt discounts on convertible term note and revolving credit note, net of current portion of \$121 and \$166, respectively	(232)	(271)
	\$ 3,972	\$ 6,523

**NOTE 7 RELATED PARTY TRANSACTIONS**

During the three and six months ended June 30, 2007, UCN paid the Chairman of the Board of Directors (Chairman), \$5,000 per month for consulting, marketing, and capital raising activities. Starting in September 2001 and continuing to January 2003, the Chairman provided three carriers with his personal guaranty of payment up to \$800,000. These guarantees have not changed since their inception and UCN has indemnified the Chairman for any losses for which he may become personally liable.

**NOTE 8 CAPITAL TRANSACTIONS**

On June 29, 2007, UCN filed a shelf registration on Form S-3 with the SEC. Under the terms of this shelf registration, UCN may offer from time to time up to \$12 million in common shares. The registration statement became effective on July 13, 2007 and UCN has not sold any shares registered under the registration statement.

On April 18, 2007, ComVest Capital exercised its right to convert the term note to common stock. UCN issued 1,126,664 shares of common stock on conversion of approximately \$3.4 million in principal amount of the convertible term note and paid, in cash, \$15,000 of interest as complete payment and satisfaction of that note. The shares of common stock issued to ComVest Capital were previously registered for resale under a registration statement on Form S-1 filed with the Securities and Exchange Commission.

During the six months ended June 30, 2007, former employees and members of UCN's Board of Directors exercised options to purchase a total of 235,336 shares of common stock and UCN received total proceeds of \$574,000.

In March 2007, a warrant holder converted 164,125 warrants in a cashless exercise into 36,810 shares of UCN common stock.

In conjunction with the ScheduleQ acquisition that was closed in February 2007, UCN issued a total of 108,912 shares of its restricted common stock to ScheduleQ stockholders (Note 3).

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In conjunction with the BenchmarkPortal acquisition that was closed in February 2007, UCN issued a total of 1,535,836 shares of its restricted common stock to BenchmarkPortal stockholders (Note 3).

In conjunction with the BenchmarkPortal acquisition, UCN entered into a consulting agreement with the founder of BenchmarkPortal and issued warrants to purchase a total of 60,000 shares of UCN common stock at \$2.95 per share. The fair market value of the warrants, using the Black-Scholes pricing model, was \$68,000 with an assumed expected volatility of 48.63%, a risk-free rate of return of 4.76%, no dividend yield, and an expected life of 3.0 years. This amount will be expensed as a consulting expense over the six month term of the agreement.

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In January 2007, UCN amended the convertible term note and revolving credit note agreement. In conjunction with this amendment, UCN issued warrants to ComVest Capital, LLC to purchase 55,000 shares of common stock at \$2.90 per share. In addition to the warrants, UCN also paid \$35,000 in consideration, which was applied to the revolving credit facility. The fair market value of the warrants, using the Black-Scholes pricing model, was \$83,000 with an assumed expected volatility of 58.21%, a risk-free rate of return of 4.87%, no dividend yield, and an expected life of 4.3 years. These warrants were included in a registration statement filed with the SEC on Form S-1 to register for resale on April 6, 2007. The registration statement became effective on April 19, 2007.

**NOTE 9 STOCK-BASED COMPENSATION**

The Condensed Consolidated Financial Statements, for the three and six months ended June 30, 2007 and 2006, reflect the impact of SFAS 123(R). UCN has allocated the stock-based compensation to the respective departments based on location of where the employee's regular compensation is charged as follows (in thousands):

	Three months ended June 30, 2007		Six months ended June 30, 2006	
Costs of revenue	\$ 1	\$ 1	\$ 2	\$ 3
Selling and promotion	155	65	229	134
General and administrative	214	77	321	147
Research and development	33	1	47	13
Total	\$ 403	\$ 144	\$ 599	\$ 297

UCN estimated the fair value of options granted under its employee stock-based compensation arrangements at the grant date using the Black-Scholes model with the following weighted-average assumptions for the six months ended June 30, 2007 and 2006:

	June 30, 2007	June 30, 2006
Dividend yield	None	None
Volatility	59%	79%
Risk-free interest rate	4.48%	4.64%
Expected life (years)	3.5	4.4
Weighted average fair value of option grants	\$ 1.63	\$ 1.32
Forfeiture rate	5.3%	5.3%

The following tables summarize all stock option activity during the three months ended June 30, 2007 and 2006, respectively (in thousands, except per share data):

	Options	Price range (\$)	Weighted Average Exercise Price	Intrinsic Value
Balance at April 1, 2007	4,261	\$ 2.00 - \$5.39	\$ 2.37	\$ 4,390
Granted	58	4.00 - 4.45	4.17	
Exercised	(115)	2.00 - 2.64	2.38	187
Balance at June 30, 2007	4,204	\$ 2.00 - \$5.39	\$ 2.75	\$ 6,580

	Options	Price range	Weighted Average Exercise Price	Intrinsic Value
Balance at April 1, 2006	3,489	\$ 2.00-\$5.39	\$ 2.36	\$ 717
Granted	50	\$ 2.26	\$ 2.60	
Exercised	(66)	\$ 2.00	\$ 2.00	41

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Cancelled or expired	(68)	\$ 2.40-\$2.79	\$	2.57	
Balance at June 30, 2006	3,405	\$ 2.00-\$5.39	\$	2.36	\$ 1,196

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The following tables summarize all stock option activity during the six months ended June 30, 2007 and 2006, respectively (in thousands, except per share data):

	<b>Options</b>	<b>Price range (\$)</b>	<b>Weighted Average Exercise Price</b>	<b>Intrinsic Value</b>
Balance at January 1, 2007	3,163	\$ 2.00-\$5.39	\$ 2.39	\$ 1,627
Granted	1,342	2.93 - 3.45	3.52	
Exercised	(235)	2.00 - 2.64	2.44	148
Cancelled or expired	(66)	2.50 - 3.17	2.62	
<b>Balance at June 30, 2007</b>	<b>4,204</b>	<b>\$ 2.00-\$5.39</b>	<b>\$ 2.75</b>	<b>\$ 6,580</b>

	<b>Options</b>	<b>Price range</b>	<b>Weighted Average Exercise Price</b>	<b>Intrinsic Value</b>
Balance at January 1, 2006	3,526	\$ 2.00-\$5.39	\$ 2.37	\$ 1,627
Granted	178	\$ 2.00-\$2.26	\$ 2.16	
Exercised	(71)	\$ 2.00	\$ 2.00	2
Cancelled or expired	(228)	\$ 2.00-\$3.69	\$ 2.41	
<b>Balance at June 30, 2006</b>	<b>3,405</b>	<b>\$ 2.00-\$5.39</b>	<b>\$ 2.36</b>	<b>\$ 1,196</b>

A summary of the options outstanding and options exercisable at June 30, 2007 is as follows (in thousands, except per share amounts):

<b>Exercise price range</b>	<b>Options</b>	<b>Options Outstanding</b>		<b>Options Exercisable</b>	
		<b>Average Remaining Contractual Life</b>	<b>Weighted Average Exercise Price</b>	<b>Options Exercisable</b>	<b>Weighted Average Exercise Price</b>
\$2.00-\$ 2.30	1,503	2.8 years	\$ 2.04	1,038	\$ 2.03
\$2.31-\$ 2.66	667	2.0 years	2.50	635	2.50
\$2.67-\$ 3.07	575	2.3 years	2.81	505	2.79
\$3.08-\$ 3.99	1,355	4.6 years	3.48		
\$4.00-\$ 5.39	104	4.7 years	4.71	51	5.27
	4,204	3.2 years	\$ 2.75	2,229	\$ 2.43
<b>Intrinsic Value</b>	<b>\$ 6,580</b>			<b>\$ 4,262</b>	



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A summary of the activity for non-vested share awards as of June 30, 2007 and changes during the three and six month periods are as follows (in thousands, except per share amounts):

	Options	Weighted Average Option Fair Value
Balance at April 1, 2007	1,987	\$ 1.43
Granted	58	1.74
Vested	(70)	1.10
Balance at June 30, 2007	1,975	\$ 1.45

  

	Options	Weighted Average Option Fair Value
Balance at January 1, 2007	797	\$ 1.10
Granted	1,342	1.63
Vested	(136)	1.24
Cancelled or expired	(28)	1.44
Balance at June 30, 2007	1,975	\$ 1.45

As of June 30, 2007, there was \$1,875,000 of total unrecognized compensation cost related to non-vested share-based compensation awards granted under UCN's stock option plans, which is expected to be recognized over a weighted average period of 1.4 years. All shares are excluded from the EPS dilution calculation because they are anti-dilutive.

**NOTE 10 MAJOR SUPPLIERS**

Approximately 57% and 55% of UCN's cost of revenue for the six months ended June 30, 2007 and 2006, respectively, was paid to three of the largest U.S. telecommunication service providers. UCN owed \$2.3 million and \$4.8 million to these three providers as of June 30, 2007 and December 31, 2006, respectively.

**NOTE 11 SEGMENTS**

Effective January 1, 2006, UCN managed its business based on two customer segments: Telecom and inContact. The Telecom segment includes all voice and data long distance services provided to customers not utilizing any inContact services. The inContact segment includes revenues from customers using any inContact services as well as their long distance voice and data services. InContact services include automatic call distribution, interactive voice response, data storage, email, chat, computer telephony integration, call recording, conferencing and reporting. In mid February 2007, UCN closed two strategic acquisitions which have been added to the inContact segment. The BenchmarkPortal, Inc. acquisition allowed UCN to provide customers a hosted process for measuring the effectiveness of agent interactions with clients. The ScheduleQ, LLC acquisition allowed UCN to provide its customers a hosted solution for automating the scheduling, forecasting and alert notification functions common to most contact center/customer service type operations. These additions augment UCN's all-in-one hosted inContact solution.

Subsequent to the issuance of UCN's Form 10-Q for the period ended June 30, 2007, UCN has determined that the revenue and results of operations for a total of six user accounts previously included in the segment disclosure of UCN's inContact segment in prior periods should have been included in UCN's Telecom segment because, in substance, the revenue was substantially either long distance or still in a trial period for inContact. As a result, UCN has restated the accompanying disclosures in these condensed consolidated financial statements.

The effects of the restatement of the condensed consolidated financial statements are limited to the disclosure of segment results and do not affect the Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Operations, Condensed Consolidated Statements of Stockholders' Equity, and Condensed Consolidated Statements of Cash Flows of UCN for the affected periods. The restatement includes the reallocation of the long distance charges, along with insignificant amounts of the inContact software and related service revenue, from the six

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identified accounts from the inContact segment to the Telecom segment.

The following summarizes the effect of the restatement on the segment results of operations previously reported for the three and six month periods ended June 30, 2007 and 2006:

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Telecom Segment	Three months ended June 30, 2007			Three months ended June 30, 2006		
	As Previously		As	As Previously		As
	Reported	Adjustment	Restated	Reported	Adjustment	Restated
Revenue	\$ 12,768	\$ 1,247	\$ 14,015	\$ 17,349	\$ 160	\$ 17,509
Costs of revenue (excluding depreciation and amortization shown separately below)	8,576	832	9,408	11,751	107	11,858
Selling and promotion	1,461	120	1,581	1,983	12	1,995
General and administrative	2,322	227	2,549	2,323	23	2,346
Depreciation and amortization	733	31	764	1,352	4	1,356
Research and development						
Loss from operations	\$ (324)	\$ 37	\$ (287)	\$ (60)	\$ 14	\$ (46)

inContact Segment	Three months ended June 30, 2007			Three months ended June 30, 2006		
	As Previously		As	As Previously		As
	Reported	Adjustment	Restated	Reported	Adjustment	Restated
Revenue	\$ 7,207	\$ (1,247)	\$ 5,960	\$ 3,619	\$ (160)	\$ 3,459
Costs of revenue (excluding depreciation and amortization shown separately below)	2,552	(832)	1,720	1,829	(107)	1,722
Selling and promotion	2,641	(120)	2,521	1,449	(12)	1,437
General and administrative	1,842	(227)	1,615	900	(23)	877
Depreciation and amortization	762	(31)	731	513	(4)	509
Research and development	447		447	352		352
Loss from operations	\$ (1,037)	\$ (37)	\$ (1,074)	\$ (1,424)	\$ (14)	\$ (1,438)

Consolidated	Three months ended June 30, 2007			Three months ended June 30, 2006		
	As Previously		As	As Previously		As
	Reported	Adjustment	Restated	Reported	Adjustment	Restated
Revenue	\$ 19,975	\$	\$ 19,975	\$ 20,968	\$	\$ 20,968
Costs of revenue (excluding depreciation and amortization shown separately below)	11,128		11,128	13,580		13,580
Selling and promotion	4,102		4,102	3,432		3,432
General and administrative	4,164		4,164	3,223		3,223
Depreciation and amortization	1,495		1,495	1,865		1,865
Research and development	447		447	352		352
Loss from operations	\$ (1,361)	\$	\$ (1,361)	\$ (1,484)	\$	\$ (1,484)

UCN previously reported for the three months ended June 30, 2007, that inContact revenue included \$3.7 million of related long distance and voice and data revenue and \$3.5 million of inContact technology services, and for the same period in 2006 included \$2.7 million of related long distance voice and data service revenue and \$.9 million of inContact technology services. The restated inContact revenue for the three months ended June 30, 2007, includes \$2.5 million of related long distance voice and data service revenue and \$3.5 million of inContact technology services, and for the same period in 2006 includes \$2.6 million of related long distance voice and data service revenue and \$.9 million of inContact technology services.

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Telecom Segment	Six months ended June 30, 2007			Six months ended June 30, 2006		
	As Previously		As	As Previously		As
	Reported	Adjustment	Restated	Reported	Adjustment	Restated
Revenue	\$ 26,517	\$ 2,444	\$ 28,961	\$ 37,016	\$ 196	\$ 37,212
Costs of revenue (excluding depreciation and amortization shown separately below)	17,502	1,607	19,109	25,665	132	25,797
Selling and promotion	3,200	253	3,453	4,203	15	4,218
General and administrative	4,569	423	4,992	4,874	28	4,902
Depreciation and amortization	1,850	63	1,913	2,741	5	2,746
Research and development						
Loss from operations	\$ (604)	\$ 98	\$ (506)	\$ (467)	\$ 16	\$ (451)

inContact Segment	Six months ended June 30, 2007			Six months ended June 30, 2006		
	As Previously		As	As Previously		As
	Reported	Adjustment	Restated	Reported	Adjustment	Restated
Revenue	\$ 13,278	\$ (2,444)	\$ 10,834	\$ 6,574	\$ (196)	\$ 6,378
Costs of revenue (excluding depreciation and amortization shown separately below)	5,163	(1,607)	3,556	3,398	(132)	3,266
Selling and promotion	4,752	(253)	4,499	2,847	(15)	2,832
General and administrative	3,293	(423)	2,870	1,604	(28)	1,576
Depreciation and amortization	1,438	(63)	1,375	1,003	(5)	998
Research and development	875		875	664		664
Loss from operations	\$ (2,243)	\$ (98)	\$ (2,341)	\$ (2,942)	\$ (16)	\$ (2,958)

Consolidated	Six months ended June 30, 2007			Six months ended June 30, 2006		
	As Previously		As	As Previously		As
	Reported	Adjustment	Restated	Reported	Adjustment	Restated
Revenue	\$ 39,795	\$	\$ 39,795	\$ 43,590	\$	\$ 43,590
Costs of revenue (excluding depreciation and amortization shown separately below)	22,665		22,665	29,063		29,063
Selling and promotion	7,952		7,952	7,050		7,050
General and administrative	7,862		7,862	6,478		6,478
Depreciation and amortization	3,288		3,288	3,744		3,744
Research and development	875		875	664		664
Loss from operations	\$ (2,847)	\$	\$ (2,847)	\$ (3,409)	\$	\$ (3,409)

UCN previously reported for the six months ended June 30, 2007, that inContact revenue included \$7.6 million of related long distance and voice and data revenue and \$5.7 million of inContact technology services, and for the same period in 2006 included \$5.0 million of related long distance voice and data service revenue and \$1.6 million of inContact technology services. The restated inContact revenue for the six months ended June 30, 2007, includes \$5.2 million of related long distance voice and data service revenue and \$5.6 million of inContact technology services, and for the same period in 2006 includes \$4.8 million of related long distance voice and data service revenue and \$1.6 million of inContact technology services.

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**NOTE 12 SUBSEQUENT EVENT**

On August 2, 2007, UCN amended the ComVest revolving credit and term loan agreement to eliminate the most significant financial covenants as well as other non-financial covenants. The financial covenants eliminated through the amendment were: 1) the capital expenditure limit; 2) the EBITDA (a non-GAAP measure that is specifically defined in the agreement) requirement; and 3) the minimum cash and availability requirement. UCN did not incur any costs associate with the amendment.

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

The following management discussion and analysis gives effect to the restatement discussed in Note 11 to the accompanying condensed consolidated financial statements.

**Basis of presentation**

The following discussion and analysis of financial condition and results of operations should be read in conjunction with the December 31, 2006 consolidated financial statements and notes thereto, along with the Management s Discussion and Analysis of Financial Condition and Results of Operations included in UCN s 2006 Annual Report on Form 10-K, filed separately with the U.S. Securities and Exchange Commission.

**Overview**

UCN, Inc. ( UCN or the Company ) offers a wide range of hosted contact handling and performance management software services, in addition to a variety of connectivity options for carrying an inbound call into its inContact suite of services or linking agents to inContact, including dedicated T1s, IP connectivity, toll free and inbound local numbers. We sell telecom services unbundled from our inContact service offering, including, dedicated, switched, toll free, and data lines at competitive prices with superior service levels.

UCN is a Network Applications Provider that provides on-demand, hosted, contact handling software (through our inContact applications suite of services) and business telecommunication services delivered over our own, proprietary national Voice over Internet Protocol Network (VoIP Network). The inContact application suite includes an integrated package of advanced contact handling, reporting and administration applications and performance monitoring and management tools along with a unique rapid application development tool.

We offer a set of traditional connectivity products, which include the dedicated voice T1 product, the Intelligent-T , VoIP connectivity services and our switched 1+ services, that enable our customer sites to connect to UCN s VoIP Network and gain access to our inContact services. Our customers publish toll free and inbound local numbers to their customer base, enabling inbound callers to be handled through the inContact applications embedded in the VoIP Network. Our distribution channels pursue multiple marketing avenues, including using independent agents, value-added resellers and direct and inside sales forces.

**Results of Operations**

*Consolidated Revenue*

Consolidated revenues decreased \$1.0 million or 5% to \$20.0 million for the three months ended June 30, 2007 from \$21.0 million compared to the same period in 2006. The decrease is primarily due to the continued revenue decrease in our Telecom segment, which was down \$3.5 million compared to the same period in 2006. The decrease in our Telecom segment is due to the loss of several high volume, low margin customers as well as the movement of revenue between our two segments that occurred during 2006. When current Telecom customers start using our inContact services all of their revenue moves to the inContact segment. These losses were offset by significant increases in inContact segment revenue, which increased \$2.5 million from the second quarter of 2006. The BenchmarkPortal acquisition allows us to provide customers a hosted process for measuring the effectiveness of agent interactions with clients. The ScheduleQ acquisition allows us to provide our customers a hosted solution for automating the scheduling, forecasting and alert notification functions common to most contact center/customer service type operations. These additions augment our all-in-one hosted inContact solution.

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Consolidated revenues decreased \$3.8 million or 8.7% to \$39.8 million for the six months ended June 30, 2007 from \$43.6 million compared to the same period in 2006. The decrease is primarily due to the continued revenue decrease in our Telecom segment, which was down \$8.3 million compared to the same period in 2006. The decrease in our Telecom segment is due to the discontinuation of services to several high volume, low margin customers during the second quarter of 2006 which affected each subsequent quarter. Additionally, we experienced a significant movement of our customers from the Telecom to the inContact segment during 2006 as they added inContact to their services. As mentioned above, when current Telecom customers start using our inContact services, their entire revenue balance moves to the inContact segment. These losses were offset by significant increases in inContact segment revenue, which increased \$4.4 million to \$10.8 million through June 30, 2007 compared to \$6.4 million during the same period in 2006.

We continue focusing marketing efforts on providing on-demand contact center hosted solution and business telecommunications services delivered over our national VoIP network. We believe the opportunity to increase revenues through the sale of enhanced telecommunications services to business customers is much greater than through the sale of traditional long distance services to residential customers. We have developed a menu of enhanced communication services that are marketed to existing and potential customers through our multiple sales channels. As a result of these changes, we are experiencing a transition in sales mix, which will continue with the addition of new products and features.

*Costs of revenue*

Costs of revenue decreased \$2.5 million or 18% to \$11.1 million for the three months ended June 30, 2007 from \$13.6 million for the same period in 2006. Consistent with other telecommunication companies, we do not include amortization and depreciation in our calculation of costs of revenue. Costs of revenue as a percentage of revenue decreased to 55.7% during the quarter compared to 64.8% in the same period in 2006. We have continued to improve our cost of revenue as a percentage of revenue percentage by implementing cost cutting measures, increasing higher margin inContact revenue and terminating our relationship with large-volume low-margin customers. In addition to these measures, the \$1.1 million of additional revenue added through the BenchmarkPortal and ScheduleQ acquisitions had very little cost involved with the creation of such revenue.

Costs of revenue decreased \$6.4 million or 22% to \$22.7 million for the six months ended June 30, 2007 from \$29.1 million for the same period in 2006. Consistent with other telecommunication companies, we do not include amortization and depreciation in our calculation of costs of revenue. Costs of revenue as a percentage of revenue decreased to 57.0% during the six months ended June 30, 2007 compared to 66.7% in the same period in 2006. We have continued to improve our cost of revenue as a percentage of revenue percentage by implementing cost cutting measures, increasing higher margin inContact revenue and terminating our relationship with large-volume low-margin customers. In addition to these measures, the \$1.6 million of additional revenue added through the BenchmarkPortal and ScheduleQ acquisitions had very little cost involved with the creation of such revenue.

As noted above, we continue to focus most of our marketing efforts on promoting our inContact technology services which carry significantly higher margins than the traditional long distance services. As a result, we expect continued improvements in margins from the sales of these technology services as we add higher gross margin inContact customers. We continue to support our telecom reseller channel that markets our telecom products to business users and encourage those resellers to refer inContact opportunities to us.

*Selling and promotion*

Selling and promotion expenses increased 20% or \$670,000 to \$4.1 million during the three months ended June 30, 2007 from \$3.4 million during the same period in 2006 primarily due to an overall increase in the number of sales and lead generation activities related to bringing the inContact suite of services to the market. Our sales force grew substantially through the addition of employees related to the BenchmarkPortal and ScheduleQ acquisitions closed during the first quarter of 2007. During the first quarter of 2007, UCN granted a significant number of stock options to certain senior members of management, which added an additional \$80,000 of stock-based compensation expense for a total of \$155,000 during the second quarter of 2007 compared to \$65,000 during the same period in 2006.

Selling and promotion expenses increased 13% or \$902,000 to \$8.0 million during the six months ended June 30, 2007 from \$7.1 million during the same period in 2006 primarily due to an overall increase in the number of sales and lead generation activities related to bringing the inContact suite of services to the market. Our sales force grew substantially through the addition of employees related to the BenchmarkPortal and ScheduleQ acquisitions closed during the first quarter of 2007. During the first quarter of 2007, UCN granted a significant number of stock options to certain senior members of management which added an additional \$95,000 of stock-based compensation expense for a total of \$229,000 during the six months ended June 30, 2007 compared to \$134,000 during the same period in 2006.



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As noted above, we continue to focus most of our marketing efforts on promoting our inContact technology. As a result, we expect our selling and promotion expense will continue to increase going forward as we continue bringing the inContact suite of services to the market.

### *General and administrative*

General and administrative expenses for the three months ended June 30, 2007 increased 29% or \$1.0 million to \$4.2 million compared to \$3.2 million in the same period in 2006. The increase is primarily due to an overall increase in salaries and benefits during the year due to the growth of the company. Our general and administrative staff grew substantially through the addition of employees related to the BenchmarkPortal and ScheduleQ acquisitions closed during the first quarter of 2007. During the first quarter of 2007, UCN granted a significant number of stock options to certain senior members of management, which added and an additional \$137,000 of stock-based compensation expense for a total of \$214,000 during the three months ended June 30, 2007 compared to \$77,000 during the same period in 2006.

General and administrative expenses for the six months ended June 30, 2007 increased 21% or \$1.4 million to \$7.9 million compared to \$6.5 million in the same period in 2006. The increase is primarily due to an overall increase in salaries and benefits during the year due to the growth of the company. Our general and administrative staff grew substantially through the addition of employees related to the BenchmarkPortal and ScheduleQ acquisitions closed during the first quarter of 2007. During the first quarter of 2007, UCN granted a significant number of stock options to certain senior members of management, which added and an additional \$174,000 of stock-based compensation expense for a total of \$321,000 during the six months ended June 30, 2007 compared to \$147,000 during the same period in 2006.

### **Segment Reporting**

We manage our business based on two customer segments: Telecom and inContact. The Telecom customer segment includes all voice and data long distance services provided to customers not utilizing any inContact services. The inContact customer segment includes revenues from customers using any inContact services as well as their related long distance voice and data services. The inContact segment services include automatic call distribution, interactive voice response, data storage, email, chat, computer telephony integration, call recording, conferencing and reporting. In mid February 2007, UCN closed two strategic acquisitions which have been added to our inContact segment. The BenchmarkPortal, Inc. acquisition allows us to provide customers a hosted process for measuring the effectiveness of agent interactions with clients. The ScheduleQ, LLC acquisition allows us to provide our customers a hosted solution for automating the scheduling, forecasting and alert notification functions common to most contact center/customer service type operations. These additions augment our all-in-one hosted inContact solution. We will continue to evaluate the components of the inContact segment as future strategic initiatives are implemented.

### *Audit Committee Independent Investigation and Restatement*

In January 2008, the Audit Committee of UCN received an allegation that its Executive Vice President of Global Alliances had engaged in improper sales activities that resulted to a misallocation of revenue between UCN's Telecom Segment and inContact Segment. Upon receipt of the allegation, the Audit Committee engaged outside counsel to investigate the allegations. Management also conducted its own review of matters related to the recognition and allocation of revenue between segments.

The independent investigators engaged by the Audit Committee have completed the investigation and management has completed its review of segment allocations and results. UCN has determined that the revenue and results of operations for a total of six user accounts previously included in the segment disclosure of UCN's inContact segment in prior periods should have been included in UCN's Telecom segment because, in substance, the revenue was substantially either long distance or still in a trial period for inContact. Accordingly, on March 10, 2008, the Board of Directors concluded that no further reliance should be placed on the condensed consolidated financial statements of UCN filed with its quarterly reports on Form 10-Q for the quarters ended September 30, June 30, and March 31, 2007, and its consolidated financial statements for the year ended December 31, 2006, filed with its annual report on Form 10-K for the year ended December 31, 2006. Accordingly, UCN is restating its previously issued financial statements for those periods.

The effects of the restatement of the consolidated financial statements are limited to the footnote disclosure of segment results and do not affect the Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Operations, Condensed Consolidated Statements of Stockholders' Equity, and Consolidated Statements of Cash Flows of UCN for the affected periods. The restatement includes the reallocation of the long distance charges, along with insignificant amounts of the inContact software and related service revenue, from the six identified accounts from the inContact segment to the Telecom segment. The amounts set forth below for the inContact and Telecom segments have been adjusted to give effect to the restatement.

### *inContact Customer Segment Quarterly Results*



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The inContact segment revenue increased to \$6.0 million during the quarter ended June 30, 2007, which is a 72% increase from the same period in 2006 as a result of the selling and promotion effort we have undertaken to bring these products to market. The BenchmarkPortal and ScheduleQ acquisitions that were closed during the first quarter of 2007 added an additional \$1.1 million of revenue during the quarter. Excluding the \$1.1 million of acquisition revenue, the segment increased 40% compared to the same quarter in 2006.

For the three months ended June 30, 2007, the inContact segment revenue of \$6.0 million includes \$2.5 million of related long distance voice and data services and \$3.5 million of inContact technology services. For the three months ended June 30, 2006, the inContact segment revenue of \$3.5 million includes \$2.6 million of long distance voice and data services and \$.9 million of inContact technology services.

Costs of revenue as a percentage of revenue decreased during the three months ended June 30, 2007 to 28.9% from 49.8% during the same period in 2006. These significant improvements are primarily due to closing higher margin inContact deals with new customers as well as the addition of BenchmarkPortal and ScheduleQ, which produce revenue with very few direct costs. We anticipate that margins will continue to improve as we add customers with more inContact technology services. We continue to focus a significant amount of resources related to bringing inContact to market. As a result, selling and promotion expenses in the segment increased \$1.1 million or 75% during the quarter compared to the same period in 2006. We also continue to develop the services provided in the segment by investments in research and development. During the quarter, we spent \$447,000 in research and development costs and have capitalized an additional \$268,000 of costs related to our internally developed software.

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### ***inContact Customer Segment Year-to-Date Results***

The inContact segment revenue increased to \$10.8 million during the six months ended June 30, 2007, which is a 70% increase from the same period in 2006 as a result of the selling and promotion effort we have undertaken to bring these products to market. The BenchmarkPortal and ScheduleQ acquisitions that were closed during the first quarter of 2007 added an additional \$1.6 million of revenue during the quarter. Excluding the \$1.6 million of acquisition revenue, the segment increased 44% compared to the same quarter in 2006.

For the six months ended June 30, 2007, the inContact segment revenue of \$10.8 million includes \$5.2 million of related long distance voice and data services and \$5.6 million of inContact technology services. For the six months ended June 30, 2006, the inContact segment revenue of \$6.4 million includes \$4.8 million of long distance voice and data services and \$1.6 million of inContact technology services.

Costs of revenue as a percentage of revenue improved during the six months ended June 30, 2007 to 32.8% from 51.2% during the same period in 2006. These significant improvements are primarily due to closing higher margin inContact deals with new customers as well as the addition of BenchmarkPortal and ScheduleQ, which produce revenue with very few direct costs. We anticipate that margins will continue to improve as we add customers with more inContact technology services. We continue to focus a significant amount of resources related to bringing inContact to market. As a result, selling and promotion expenses in the segment increased to \$4.5 million or 59% during the six months ended June 30, 2007 compared to the same period in 2006. We also continue to develop the services provided in the segment by investments in research and development. During the six months ended June 30, 2007, we spent \$875,000 in research and development costs and have capitalized an additional \$375,000 of costs related to our internally developed software.

### ***Telecom Customer Segment Quarterly Results***

While we continue to see decreases in the Telecom segment, the attrition rates are in line with our expectations. Overall segment revenue decreased 20% to \$14.0 million during the quarter compared to the same period in 2006. These decreases were primarily due to UCN terminating its relationship with several large-volume low-margin customers during the second quarter of 2006 as well as up selling inContact services to several legacy Telecom customers, which occurred during 2006 that affected each subsequent period. When an existing Telecom customer turns up inContact services, all of their Telecom revenue is moved to the inContact segment. We expect that revenue from the Telecom Segment will continue to decrease due to normal attrition rates as well as movement of customers from the Telecom customer segment to the inContact customer segment. With the decline in revenues from the segment, we have been able to reduce overall costs in the segment. Our costs of revenue and selling and promotion expenses each decreased 21% during the quarter compared to the same period in 2006.

### ***Telecom Customer Segment Year-to-Date Results***

We continue to see decreases in the Telecom segment; however the attrition rates are in line with our expectations. Overall segment revenue decreased 22% to \$29 million during the period compared to the same period in 2006. These decreases were primarily due to UCN terminating its relationship with several large-volume low-margin customers during the second quarter of 2006 as well as up selling inContact services to several legacy Telecom customers, which occurred during 2006 that affected each subsequent period. When an existing Telecom customer turns up inContact services, all of their Telecom revenue is moved to the inContact segment. We expect that revenue from the Telecom Segment will continue to decrease due to normal attrition rates as well as movement of customers from the Telecom customer segment to the inContact customer segment. With the decline in revenues from the segment, we have been able to reduce overall costs in the segment. Our costs of revenue and selling and promotion expenses decreased 26% and 18%, respectively, during the quarter compared to the same period in 2006.

## **Liquidity and Capital Resources**

On August 2, 2007, we amended the ComVest revolving credit and term loan agreement to eliminate the most significant financial covenants as well as some other non-financial covenants. The financial covenants eliminated through the amendment were: 1) the capital expenditure limit; 2) the EBITDA (a non-GAAP measure that is specifically defined in the agreement) requirement; and 3) the minimum cash and availability requirement. This amendment provides us increased flexibility to aggressively grow the business through additional investments in the inContact segment.

On June 29, 2007, UCN filed a shelf registration on Form S-3 with the SEC. Under the terms of this shelf registration, UCN may offer from time to time up to \$12 million in common shares. The registration statement became effective on July 13, 2007 and UCN has not sold any shares registered under the registration statement.

On April 18, 2007, ComVest Capital exercised its right to convert the term note to common stock. UCN issued 1,126,664 shares of common stock on conversion of approximately \$3.4 million in principal amount of the convertible term note and paid, in cash, \$15,000 of interest as

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complete payment and satisfaction of that note. This conversion will save UCN an estimated \$468,000 in cash payments during 2007 and will significantly improve the current ratio in future periods by eliminating the associated current portion of long-term debt.

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In January 2007, UCN amended the convertible term note and revolving credit note agreement. In conjunction with this amendment, UCN issued warrants to ComVest Capital, LLC to purchase 55,000 shares of common stock at \$2.90 per share. The fair market value of the warrants, using the Black-Scholes pricing model, was \$83,000 with an assumed expected volatility of 58.21%, a risk-free rate of return of 4.87%, no dividend yield, and an expected life of 4.3 years. These warrants were included in a registration statement filed with the SEC on Form S-1 to register for resale on April 6, 2007. The registration statement became effective on April 19, 2007.

In conjunction with the BenchmarkPortal acquisition, UCN entered a consulting agreement with the founder of BenchmarkPortal and issued warrants to purchase a total of 60,000 share of UCN common stock at \$2.95 per share. The fair market value of the warrants, using the Black-Scholes pricing model, was \$68,000 with an assumed expected volatility of 48.63%, a risk-free rate of return of 4.76%, no dividend yield, and an expected life of 3.0 years.

During the six months ended June 30, 2007, former employees and members of UCN's Board of Directors exercised options to purchase a total of 235,336 shares of common stock and UCN received total proceeds of \$574,000.

In March 2007, a warrant holder converted 164,125 warrants in a cashless exercise into 36,810 shares of UCN common stock.

In conjunction with the BenchmarkPortal acquisition that was closed in February 2007, UCN issued a total of 1,535,836 shares of its restricted common stock to BenchmarkPortal stockholders.

In conjunction with the ScheduleQ acquisition that was closed in February 2007, UCN issued a total of 108,912 shares of its restricted common stock to ScheduleQ stockholders.

We experienced net losses of \$3.2 million and \$4.3 million for the six months ended June 30, 2007 and 2006, respectively. Included within the net loss during the six months ended 6/30/07 were: 1) \$3.3 million of depreciation and amortization; 2) \$599,000 of non-cash stock-based compensation expense; and 3) \$168,000 in non-cash expense related to two consulting agreements that were satisfied through the issuance of warrants.

Our working capital surplus of \$1.6 million at December 31, 2006 decreased to \$1.0 million at June 30, 2007. The primary reason for the reduction in working capital was due to a \$2.2 million decrease in cash. This decrease in cash was driven by a \$1.2 million reduction in accounts payable as well as an increase of \$445,000 in accounts receivable due to the normal business timing of cash payments and collections. This decrease in cash was partially offset by an \$117,000 decrease in the current portion of long-term debt due to the conversion of the of the ComVest \$3.4 million convertible term note. This conversion will save us an estimated \$468,000 in cash payments during 2007 and will significantly improve the current ratio in future periods by eliminating the associated current portion of long-term debt.

In addition to the cash amount listed on the condensed consolidated balance sheets, we also have access to additional available borrowings under the revolving credit facility. The available borrowings under the revolving credit facility increased \$1.5 million to \$3.6 million at June 30, 2007 compared to only \$2.2 million available at December 31, 2006, resulting in total cash and additional availability under the revolving credit facility of \$6.1 million at the end of the quarter.

The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should we be unable to continue as a going concern. Our continuation as a going concern is dependent upon the ability to generate sufficient cash flow to meet obligations on a timely basis and ultimately to achieve successful operations.

We have taken the following steps to continue to meet our obligations:

On June 29, 2007, we filed a shelf registration on Form S-3 with the SEC. Under the terms of this shelf registration, we may offer from time to time up to \$12 million in common shares. The registration statement became effective on July 13, 2007 and we have not sold any shares under the registration statement.

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In February 2007, we closed two acquisitions (Note 3), which improved the overall inContact product offering suite. With these new products, we provide customers the ability to monitor agent effectiveness through its customer survey tools and the ability to efficiently monitor their agent needs. These new service offerings provide us additional contact and service opportunities to potential customers as well as provide up-sale opportunities to existing customers. These acquisitions added an additional \$1.1 million and \$1.6 million of higher-margin inContact revenue during the three and six months ended June 30, 2007.

The inContact segment revenue increased to \$6.0 million during the quarter ended June 30, 2007, a 72% increase from the same period in 2006 for a year to date total of \$10.8 million. This increase was a result of the selling and promotion effort we have undertaken to bring these products to market. Excluding the \$1.1 million in revenue from the acquisitions, the segment increased 40% compared to the second quarter of 2006. We expect to see continued revenue growth in the inContact segment in 2007.

We believe these actions will allow us to have sufficient cash flows available to meet short-term requirements and to enable us to continue as a going concern.

### **Critical accounting policies and estimates**

A summary of our significant accounting policies is discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations and in Note 1 of our Annual Report on Form 10-K for the year ended December 31, 2006.

The preparation of the financial statements in accordance with U.S. generally accepted accounting principles requires us to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts of assets and liabilities. Significant areas of uncertainty that require judgments, estimates and assumptions include the accounting for income taxes and other contingencies as well as asset impairment, inventory valuation and collectibility of accounts receivable. We use historical and other information that we consider to be relevant to make these judgments and estimates. However, actual results may differ from those estimates and assumptions that are used to prepare our financial statements.

### **Adoption of New Accounting Pronouncements**

**Adoption of FIN 48:** In June 2006, the Financial Accounting Standards Board issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement 109* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing a recognition threshold for tax positions taken or expected to be taken in a tax return. FIN 48 requires that entities recognize in their financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. FIN 48 is effective for fiscal years beginning after December 15, 2006. Interest and penalties, if incurred, would be recognized as components of income tax expense. The Company's adoption of FIN 48 on January 1, 2007 had no impact on the Company's condensed consolidated financial statements as the Company does not have any uncertain income tax positions that would require adjustment.

### **Recent Accounting Pronouncements**

**Fair Value Measurements** - In September 2006, the FASB issued Statement of Financial Accounting Statement (SFAS) 157, *Fair Value Measurements*. SFAS 157 defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on assumptions that market participants would use in pricing the asset or liability. The Company is required to adopt SFAS 157 in the first quarter of 2008. The Company does not expect that the implementation of SFAS 157 will have a material effect on the Company's results of operations or financial position.

**Fair Value Option** - In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Liabilities – Including an amendment of FASB Statement No. 115*. SFAS 159 permits entities to choose to measure certain financial assets and liabilities at fair value (the fair value option). Unrealized gains and losses, arising subsequent to adoption, are reported in earnings. The Company is required to adopt SFAS 159 in the first quarter of 2008. The Company does not expect that the implementation SFAS 159 will have a material effect on the Company's results of operations or financial position.

## **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

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Our exposure to market risk is limited to interest rate sensitivity, which is affected by changes in the general level of U.S. interest rates. Our cash equivalents are invested with high quality issuers and limit the amount of credit exposure to any one issuer. Due to the short-term nature of the cash equivalents, we believe that we are not subject to any material interest rate risk as it relates to interest income. All outstanding debt instruments at June 30, 2007 have fixed interest rates and are therefore not subject to interest rate risk.

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We did not have any foreign currency hedges or other derivative financial instruments as of June 30, 2007. We do not enter into financial instruments for trading or speculative purposes and do not currently utilize derivative financial instruments. Our operations are conducted in the United States and as such are not subject to foreign currency exchange rate risk.

### **ITEM 4. CONTROLS AND PROCEDURES**

This Report includes the certifications of our Chief Executive Officer and Chief Financial Officer required by Rule 13a-14 of the Securities Exchange Act of 1934 (the Exchange Act). See Exhibits 31.1 and 31.2. This Item 4 includes information concerning the controls and control evaluations referred to in those certifications.

#### **Background**

The Audit Committee of the Board of Directors recently received the results of an independent investigation into certain accounting and financial reporting matters. The results of the investigation as well as issues identified in additional reviews and procedures conducted by management were reported to the Board of Directors. As a result, the Board of Directors determined that our previously issued condensed consolidated financial statements filed with our quarterly reports on Form 10-Q for the quarters ended September 30, June 30, and March 31, 2007, and our consolidated financial statements for the year ended December 31, 2006, should no longer be relied upon because of certain accounting errors in the footnotes to the financial statements. Accordingly, we are restating our previously issued financial statements for those periods. The effects of the restatements of the condensed consolidated financial statements are limited to the footnote disclosure of operating segment results and does not affect our Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Operations, Condensed Consolidated Statements of Stockholders' Equity and Condensed Consolidated Statements of Cash Flows. For a discussion of the accounting errors and the adjustments made as a result of the restatement, see Note 11 of Notes to Condensed Consolidated Financial Statements included in Part I Item 1 - Financial Statements and Part I Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations - Segment Reporting.

#### **Evaluation of Disclosure Controls and Procedures**

Disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) are designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in rules and forms adopted by the Securities and Exchange Commission (SEC), and that such information is accumulated and communicated to management, including the chief executive officer and the chief financial officer, to allow timely decisions regarding required disclosures.

In connection with the preparation of this amended report, UCN's management, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, reassessed the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as a result of the restatement of previously issued financial and the identification of certain material weaknesses in the internal controls over financial reporting described below, which we view as an integral part of our disclosure controls and procedures, our disclosure controls and procedures were not effective as of June 30, 2007.

Nevertheless, based on the completion of the Audit Committee's investigation, management's internal review of our processes and procedures, and the performance of additional procedures by management designed to ensure the reliability of our financial reporting for the interim period ended June 30, 2007, we believe that the consolidated condensed financial statements in this report fairly present, in all material respects, our financial position, results of operations and cash flows as of the dates, and for the periods, presented.

#### **Changes in Internal Control over Financial Reporting**

During the second quarter of 2007, except for the material weaknesses identified below, there have been no significant changes (including corrective actions within regard to significant deficiencies or material weaknesses) in our internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) that has materially affected or is reasonably likely to materially affect our internal control over financial reporting.

#### **Description of Material Weaknesses**

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A material weakness is defined under SEC rules as a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of a company's annual or interim financial statements will not be prevented or detected on a timely basis by the company's internal controls. As a result of management's review of the investigation issues and results, and other internal reviews and evaluations it was completing in the fourth quarter of 2007 and beginning of 2008 related to the preparation of management's first report on internal controls over financial reporting required for UCN's 2007 annual report on Form 10-K, management concluded that UCN had material weaknesses in its control environment and financial reporting process.

### Control Environment

We did not maintain an effective tone at the top that would have facilitated an effective control environment for internal control over financial reporting. This material weakness in our control environment was as result of the following control deficiencies:

We failed to establish a proper tone for internal control over financial reporting in 2006 and 2007 while we were transitioning from a traditional long distance reseller, which is our Telecom segment, to being a network applications provider that provides on-demand, hosted, contact handling software and related services, which is our inContact segment.

Members of senior management had the ability to override the proper functioning of our sales and provisioning process for our services, because we failed to recognize and segregate duties that are incompatible from the standpoint of establishing effective checks and balances between senior management.

We did not establish a tone and control consciousness in the Company that fostered effective operation of our "open door" policy for encouraging employees to communicate issues or concerns with any member of senior management or that instilled in our employees a belief that senior management respected and valued the silent whistleblower process as an important tool for receiving information about UCN and its operations.



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### **Financial Reporting Process**

We identified certain control deficiencies in the financial reporting process as it related to segment reporting, that gave rise to a material weakness. The control deficiencies include the following:

We did not design and maintain effective financial processes to report and verify at the end of each reporting period that for each inContact customer there was a substantive contract for purchase of inContact Services, inContact services were being used or delivered, and that an appropriate price was actually paid for those services after taking into consideration price adjustments or credits that were not reasonably related to other legitimate and customary sales practices, customer maintenance, or Telecom service.

We did not generate for senior management and persons with responsibility for accounting controls period-end financial reports on inContact service usage and total service price adjustments or credits on a comparative basis with inContact and Telecom revenue, so that senior management and persons with responsibility for accounting controls had the type of information that would enable them to reasonably be able to detect purported inContact service sales for which there was no or little service usage and/or inContact revenue that was completely or substantially offset by pricing adjustments or credits that were given to effect a spurious inContact sale.

### ***Impact of Material Weaknesses***

These material weaknesses resulted in the misallocation of Telecom and inContact revenue in 2006 and 2007, and the misreporting of Telecom segment and inContact segment revenue and results in our consolidated financial statements with respect to the footnote disclosure of segment results for the interim periods ended September 30, June 30, and March 31, 2007, and the year ended December 31, 2006. This is significant in light of the fact that UCN has focused its business strategy since the end of 2005 on transitioning from a traditional long distance reseller, which is our Telecom segment, to being a network applications provider that provides on-demand, hosted, contact handling software and related services, which is our inContact segment. We do not believe the material weaknesses described above had any impact on our consolidated revenues or results of operations for 2006 and 2007. We note, however, that the material weaknesses are in our control environment and financial reporting process and could negatively impact our revenue and operating controls and procedures in future periods if they remain unaddressed by management.

### **Management Plan to Remediate Material Weaknesses**

In the first quarter of 2008, our management and the Audit Committee are pursuing the implementation of corrective measures to address the material weaknesses described above. These measures, outlined below, are intended both to address the identified material weaknesses and to enhance our overall financial control environment.

The material weaknesses create an environment where a person in a position of responsibility can take advantage of the circumstances to engage in misconduct, but there must actually be that person who acts improperly to create the result where segment revenue is misallocated. The Executive Vice President for Global Alliances who acted improperly was removed from his position in February 2008 and his employment with UCN terminated in March 2008.

We are restructuring responsibility for duties with respect to incompatible functions in the sales and provisioning processes so that these duties are not assigned to a single person. Under the restructuring and related internal policy, no one person will have authority to enter into contracts for the sale of our services, set the pricing for those services outside of established parameters, grant price adjustments or credits, and supervise the implementation and delivery of services. We will have a senior management person with the duty and authority to supervise sales activity who is responsible for ensuring all customer accounts have signed contracts that accurately specify the services purchased, state whether there is a trial or test period, state the price for each service, and lists any sales incentives given to obtain the customer. UCN's executive committee will establish, evaluate and approve standard pricing and allowable non-standard pricing ranges. A different senior management person will have the duty and authority to supervise and verify the implementation, pricing structures and delivery of services to the customer per the written contract for service.

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We are reformatting monthly reports so that senior management and persons with responsibility for accounting controls receive information by customer on revenue for each service provided during the preceding three months, actual service usage for each month during the period and total service price adjustments or credits for each month during the period, so that they can reasonably determine whether any of these measures exceed parameters set by the executive committee or are otherwise unusual.

We will evaluate and implement training for our employees to enhance awareness and understanding of standards and principles for the way we will do business, contract with our customers, deliver our services, and account for the revenue we receive.

We will reemphasize to all our employees the importance of our silent whistleblower program and affirm to our employees that we believe it to be the duty of each employee as part of his or her employment to report questionable or suspicious conduct or activity, and that senior management encourages and approves of such reporting.

We believe the remediation measures described above will remediate the material weaknesses we have identified and strengthen our internal control over financial reporting. We are committed to continuing to improve our internal control processes and will continue to diligently and vigorously review our financial reporting controls and procedures. As we continue to evaluate and work to improve our internal control over financial reporting, we may determine to take additional measures to address control deficiencies or determine to modify, or in appropriate circumstances not to complete, certain of the remediation measures described above.

**Table of Contents****PART II****ITEM 1A. RISK FACTORS**

The Private Securities Litigation Reform Act of 1985 provides a safe harbor for forward-looking statements made by UCN, except where such statements are made in connection with an initial public offering. All statements, other than statements of historical fact, which address activities, actions, goals, prospects, or new developments that we expect or anticipate will or may occur in the future, including such things as expansion and growth of our operations and other such matters are forward-looking statements. Any one or a combination of factors could materially affect our operations and financial condition. These factors include competitive pressures, success or failure of marketing programs, changes in pricing and availability of services and products offered to customers, legal and regulatory initiatives affecting customer marketing and rebate programs or long distance service, and conditions in the capital markets. Forward-looking statements made by us are based on knowledge of our business and the environment in which we operate as of the date of this report. Because of the factors discussed below, as well as other factors set forth under the Item 1A. Risk Factors in our Annual Report on Form 10-K for 2006, actual results may differ from those in the forward-looking statements.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

At the Annual Meeting of Stockholders held on June 7, 2007, the stockholders voted on the following matters:

1. Election of Theodore Stern, Steve Barnett, Paul F. Koeppel, Blake O. Fisher, Jr., and Paul Jarman as directors of UCN to serve until their successors are duly elected and qualified; and
2. Ratify the selection by the Audit Committee of the firm of Deloitte & Touche LLP as the independent auditors to examine UCN's financial statements for the year 2007.

Each of the foregoing matters was approved by the stockholders. The number of votes cast on the foregoing matters is as follows:

	<b>For</b>	<b>Against</b>	<b>Abstain</b>
Election of Directors:			
Theodore Stern	20,914,297	209,653	
Steve Barnett	21,100,744	23,206	
Paul Koeppel	21,100,744	23,206	
Blake Fisher, Jr.	21,100,744	23,206	
Paul Jarman	20,914,297	209,653	
Ratification of selection of Deloitte & Touche, LLP	19,681,566	1,194,315	248,069

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**ITEM 6. EXHIBITS**

<b>Exhibit No.</b>	<b>Title of Document</b>
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certifications of the Chief Executive Officer and Chief Financial Officer pursuant to 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, thereunto duly authorized.

**UCN, INC.**

Date: March 31, 2008

By: /s/ Paul Jarman  
Paul Jarman  
Chief Executive Officer

Date: March 31, 2008

By: /s/ Brian S. Moroney  
Brian S. Moroney  
Principal Financial and Accounting Officer