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BURST.COM AND SUBSIDIARIES
FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
FOR THE YEARS ENDED
DECEMBER 31, 2006 AND 2005

BURST.COM AND SUBSIDIARIES
FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Stockholders
Of Burst.com, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheet of Burst.Com, Inc. (a Delaware Corporation) and Subsidiaries (the "Company") as of December 31, 2006 and 2005, and the related consolidated Statements of Income, Retained Earnings, and Cash Flows for the years then ended. These Financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Burst.com, Inc. as of December 31, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in cursive script that reads "Sterck Kulik O'Neill".

San Francisco, California
February 22, 2006

BURST.COM, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
<u>Assets</u>		
Current assets		
Cash and cash equivalents	\$ 169,318	\$ 79,605
Accrued interest on Notes Receivable	109,951	64,207
Treasury Bills available-for-sale	3,320,883	5,483,916
Prepaid expenses	<u>12,200</u>	<u>-</u>
Total current assets	<u>3,612,352</u>	<u>5,627,728</u>
Property and equipment, net of accumulated depreciation of \$146,256 and \$146,256, respectively	-	-
Note Receivable - Employees	1,740,583	1,740,583
Other assets	<u>2,740</u>	<u>8,116</u>
Total assets	<u>\$ 5,355,675</u>	<u>\$ 7,376,427</u>
<u>Liabilities and Stockholders' Equity</u>		
Current liabilities		
Accounts payable	\$ -	\$ 2,395
Accrued expenses	49,921	50,268
State income taxes payable	<u>-</u>	<u>1,448,909</u>
Total current liabilities	<u>49,921</u>	<u>1,501,572</u>
Stockholders' Equity		
Convertible preferred stock, \$.00001 par value, 20,000,000 shares authorized; none issued outstanding	-	-
Common stock, \$.00001 par value; 100,000,000 shares authorized; 39,950,633 shares issued and outstanding during 2006 and 2005	400	400
Additional paid-in-capital	68,008,864	68,008,864
Accumulated deficit	(62,698,508)	(62,165,299)
Accumulated other comprehensive income:		
Unrealized holding gain/ (loss) on marketable securities	<u>(5,002)</u>	<u>30,890</u>
Total stockholders' equity	<u>5,305,754</u>	<u>5,874,855</u>
Total Liabilities and Stockholders' Equity	<u>\$ 5,355,675</u>	<u>\$ 7,376,427</u>

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See accompanying notes and accountants' report

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BURST.COM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
Revenue	\$ -	\$ 60,300,000
Costs and expenses:		
General and administrative	762,965	1,690,387
Legal fees and costs associated with licensing revenue	<u>-</u>	<u>22,262,685</u>
Total costs and expenses	<u>762,965</u>	<u>23,953,072</u>
Income (Loss) from operations	<u>(762,965)</u>	<u>36,346,928</u>
Other income (expenses):		
Interest income	174,054	125,622
Interest expense	(3,123)	(37,294)
Gain on sale of securities	59,675	41,995
Total other income (expenses)	<u>230,606</u>	<u>130,323</u>
Income tax (expense)	<u>(850)</u>	<u>(1,450,560)</u>
Net Income (Loss)	<u>\$ (533,209)</u>	<u>\$ 35,026,691</u>
Unrealized Gain/ (Loss)	<u>(35,892)</u>	<u>30,890</u>
Total comprehensive income	<u>\$ (569,101)</u>	<u>\$ 35,057,581</u>
Net income (loss) per share, basic and diluted	<u>\$ (0.01)</u>	<u>\$.86</u>
Weighted average number of common shares outstanding	<u>35,391,968</u>	<u>35,391,968</u>

BURST.COM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)
FOR THE YEARS ENDED
DECEMBER 31, 2006 AND 2005

	Common Stock	
	Shares	Amount
Balance, December 31, 2004	27,072,871	271
Stock options exercised	2,911,896	29
Warrants exercised	9,965,866	100
Common Stock issued to investors	-	-
Balance, December 31, 2005	<u>39,950,633</u>	<u>400</u>
Stock options exercised	-	-
Warrants exercised	-	-
Common Stock issued to investors	-	-
Balance, December 31, 2006	<u>39,950,633</u>	<u>400</u>

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BURST.COM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)
FOR THE YEARS ENDED
DECEMBER 31, 2006 AND 2005 (CONTINUED)

	<u>Common Stock</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Additional Paid-In Capital</u>	<u>Deficit</u>	<u>Total</u>
Balance, December 31, 2004	\$ 271	\$ -	\$61,556,618	\$(62,676,420)	\$ (1,119,531)
Compensation related to sale of common stock to investors	-	-	-	-	-
Options exercised	29	-	3,222,456	-	2,705,211
Warrants exercised	100	-	3,229,790	-	3,229,890
Dividends paid to shareholders	-	-	-	(34,515,570)	(34,515,570)
Net income	-	-	-	35,026,691	35,543,965
Unrealized holding gain on Marketable securities	-	<u>30,890</u>	<u>-</u>	<u>-</u>	<u>30,890</u>
Balance, December 31, 2005	\$ 400	\$ 30,890	\$68,008,864	\$(62,165,299)	\$ 5,874,855
Compensation related to sale of common stock to investors	-	-	-	-	-
Options exercised	-	-	-	-	-
Warrants exercised	-	-	-	-	-
Dividends paid to shareholders	-	-	-	-	-
Net income (loss)	-	-	-	(533,209)	(533,209)
Unrealized holding (loss) on Marketable securities	-	<u>(35,892)</u>	<u>-</u>	<u>-</u>	<u>(35,892)</u>
Balance, December 31, 2006	<u>\$ 400</u>	<u>\$ (5,002)</u>	<u>\$68,008,864</u>	<u>\$(62,698,508)</u>	<u>\$ 5,305,754</u>

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See accompanying notes and accountants' report

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BURST.COM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006	2005
Cash flows from operating activities:		
Net income (loss)	\$ (533,209)	\$ 35,543,965
Adjustments to reconcile net loss to net cash used by operations activities:		
Depreciation and amortization	2,300	938
Compensation from options exercised	-	849,654
Change in operating assets and liabilities:		
Prepaid expenses	(12,200)	800
Interest receivable	(45,744)	(35,266)
Other current assets	5,376	(5,416)
Accounts Payable	(2,395)	(193,274)
Accrued expenses	(347)	(313,388)
State income taxes payable	<u>(1,448,909)</u>	<u>1,448,909</u>
Net cash provided (used) by operating activities	<u>(2,035,128)</u>	<u>37,296,922</u>
Cash flows from investing activities:		
Purchase of Treasury Bills available for sale	(2,730,525)	(6,453,026)
Proceeds from sale of Treasury Bills available for sale	4,857,666	1,000,000
Purchase of Equipment	<u>(2,300)</u>	<u>-</u>
Net cash provided (used) by investing activities	<u>2,124,841</u>	<u>(5,453,026)</u>
Cash flows from financing activities:		
Exercise of warrants and stock options	-	2,457,048
Dividend distributions	-	(34,515,570)
Repayment of Long-term Debt	<u>-</u>	<u>(365,471)</u>
Net cash provided (used) by financing activities	<u>-</u>	<u>(32,423,993)</u>
Increase (Decrease) in cash and cash equivalents	89,713	(580,097)
Cash and cash equivalents, beginning of year	<u>79,605</u>	<u>659,702</u>
Cash and cash equivalents, end of year	<u>\$ 169,318</u>	<u>\$ 79,605</u>

Supplemental Disclosures of Cash Flow Information

Cash paid during the year for income taxes	\$ <u>800</u>	\$ <u>800</u>
Cash paid during the year for interest	\$ <u>3,123</u>	\$ <u>37,294</u>

BURST.COM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

Supplemental Schedule of Non-Cash Investing and Financing Activities

Long term debt, including accrued interest, totaling \$1,853,399 was used to exercise approximately 2,850,000 warrants during 2005.

Additionally, 1,550,000 stock options were exercised by employees during 2005. The company took notes in the amount of \$775,000, secured by the stock, in exchange for this stock.

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See accompanying notes and accountants' report

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION AND CAPITALIZATION

Burst.com, Inc. and subsidiaries ("The Company") was incorporated in the State of Delaware as Instant Video Technologies, Inc. On January 27, 2000, the Certificate of Incorporations was amended to change the Company's name to Burst.com, Inc.

The Company's authorized capital stock consists of 100,000,000 shares of common stock, \$0.00001 par value per share, and 20,000,000 shares of preferred stock, \$0.00001 per share.

The board of directors has the authority, without action by the Company's stockholders, to provide for the issuance of preferred stock in one or more classes or series and to designate the rights, preferences and privileges of each class or series, which may be greater than the rights of the common stock. The Company had no preferred stock outstanding as of December 31, 2006 and 2005.

BUSINESS

The Company licenses burst transmission technology and intellectual property for use within commercial, multimedia and interactive environments. The burst technology allows for burst transmission of video/audio programming that results in time-savings, network efficiency and superior quality products.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Burst.com, Inc and its wholly-owned subsidiaries, Explore Technology, Inc. and Timeshift-TV. All significant intercompany balances and transactions have been eliminated.

USE OF ESTIMATES

The accompanying consolidated financial statements have been prepared in conformity with U.S generally accepted accounting principles. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and operations for the period. Although these estimates are based on management's knowledge of current events and actions it may undertake in the future, they may ultimately differ from actual results. The Company's most significant estimates are those related to the valuation of stock, stock options, and warrants in connection with equity and financing transactions.

Cash and cash equivalents consist of money market accounts and other short-term investments with an original or remaining term of three months or less.

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BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CONCENTRATION OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash.

The Company maintains cash balances at several banks. Accounts at each institution are insured by the Federal Deposit Insurance Corporation up to \$100,000. From time to time, the Company had cash in financial institutions in excess of federally insured limits.

INVESTMENTS

In accordance with Statement of Financial Accounting Standards (SFAS No. 115) "Accounting for Certain Investments in Debt and Equity Securities", securities are classified into three categories: held-to maturity, available-for-sale and trading. The Company's investments consisted of equity securities classified as available-for-sale. Accordingly, they were carried at fair value in accordance with SFAS No. 115. Further, SFAS No. 115 requires that unrealized gains and losses for available-for-sales securities be excluded from earnings and reported, net of deferred income taxes, as other comprehensive income. As of December 31, 2006 and 2005, the Company had disposed of all of its available for sale securities.

COMPREHENSIVE INCOME

Statement of Financial Accounting Standards No. 130, reporting comprehensive income (SFAS 130), requires the reporting of comprehensive income in addition to net income from operations. Comprehensive income is a more inclusive financial reporting methodology that includes disclosures of certain financial information that historically has not been recognized in the calculation of net income. For the year ended December 31, 2006 and 2005, the Company's comprehensive income is presented on the Statements of Income and Comprehensive Income, and includes unrealized gains and losses on marketable securities net of the related estimated deferred income tax effect associated with those gains and losses.

There was no comprehensive income in 2004.

LONG-LIVED ASSETS

The Company periodically evaluates whether events and circumstances have occurred that may warrant revision of the estimated life of intangible and other long-lived assets, or whether the remaining balance of intangible and other long-lived assets should be evaluated for possible impairment. If and when such factors, events or circumstances indicate that intangible or other long-lived assets should be evaluated for possible impairment, the Company would make an estimate of undiscounted cash flows over the remaining lives of the respective assets in measuring recoverability.

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

REVENUE RECOGNITION

The Company recognizes revenue in accordance with Statement of Position (SOP) No. 97-2, "Software Revenue Recognition". Under the guidance of SOP No. 97.2, no revenue is recognized until evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collection is probable. License fees and services are generally recognized as revenue ratably over the license period.

PROPERTY AND EQUIPMENT

Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets that range from three to five years. Replacements, maintenance and repairs, which do not extend the lives of the respective assets are charged to expense as incurred.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company's financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, and debt. The carrying amounts of such financial instruments approximate their respective estimated fair value due to the short-term maturities and approximate market interest rates of these instruments.

NET LOSS PER COMMON SHARE AND DILUTIVE SECURITIES

Earnings (loss) per share is computed in accordance with SFAS No. 128, "Earnings per Share". Basic earnings per share is computed by dividing net income, after deducting preferred stock dividends accumulated during the period, by the weighted-average number of shares of common stock outstanding during each period. Diluted earnings per share is computed by dividing net income by the weighted-average number of shares of common stock, common stock equivalents and other potentially dilutive securities outstanding during the period.

The following is a summary of the securities that could potentially dilute basic loss per share in the future that were not included in the computation of diluted loss per share because to do so would be anti-dilutive.

	<u>2006</u>	<u>2005</u>
Options	673,100	675,600
Warrants	<u>211,818</u>	<u>211,818</u>
Total	<u>884,918</u>	<u>887,418</u>

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

INCOME TAXES

The Company accounts for income taxes using SFAS No. 109, "Accounting for Income Taxes," which requires recognition of deferred tax liabilities and assets for expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. A valuation allowance is recorded for deferred tax assets if it is more likely than not that some portion or all of the deferred tax assets will not be realized.

ADVERTISING COSTS

There were no advertising costs expensed or incurred in 2006 and 2005.

RESEARCH AND DEVELOPMENT

Research and development costs are charged to operations as incurred until such time as both technological feasibility is established and future economic benefit is assured. To date, such conditions have not been satisfied, and, accordingly, all software engineering and development costs have been expensed as incurred.

STOCK-BASED COMPENSATION

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations, in accounting for its employee stock options rather than the alternative fair value accounting followed by SFAS No. 123 "Accounting for Stock-Based Compensation." APB No. 25 provides that the compensation expense relative to the Company's employee stock options is measured based on the intrinsic value of the stock option. SFAS No. 123 requires companies that continue to follow APB No. 25 to provide a pro-forma disclosure of the impact of applying the fair value method of SFAS No. 123.

Equity instruments issued to non-employees are accounted for at fair value. The fair value of the equity instrument is determined using either the fair value of the underlying stock or the Black-Scholes option pricing model.

RECLASSIFICATIONS

Certain items have been reclassified to conform to current year presentation.

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

OTHER APPLICABLE ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board ("FASB") issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 requires companies to recognize all derivative contracts as either assets or liabilities in the balance sheet and to measure them at fair value. If certain conditions are met, a derivative may be specifically designated as a hedge, the objective of which is to match the timing of the gain or loss recognition on the hedging derivative with the recognition of (i) the changes in the fair value of the hedge asset or liability that are attributable to the hedge risk or (ii) the earnings effect of the hedge forecasted transaction. For a derivative not designated as a hedging instrument, the gain or loss is recognized in income in the period of change. On June 30, 1999, the FASB issued SFAS No. 137, "*Accounting for Derivative Instruments and Hedging Activities – Deferral of the Effective Date of FASB Statement No. 133*". SFAS No. 133 as amended by SFAS No. 137 is effective for all fiscal years beginning after June 15, 2000. In June 2000, the FASB issued SFAS No. 138, "*Accounting for Certain Derivatives Instruments and Certain Hedging Activities*". SFAS No. 133 as amended by SFAS No. 137 and 138 is effective for all fiscal quarters of fiscal years beginning after June 15, 2000.

The Company has not entered into derivatives contracts to hedge existing risks or for speculative purposes. Accordingly, SFAS 133, 137 and 138 do not affect the Company's financial statements.

In March 2000, the FASB issued Interpretation No. 44 (FIN 44), "Accounting for Certain Transactions Involving Stock Compensation", an interpretation of APB No. 25. FIN No. 44 clarifies the application of APB No. 25 for (a) the definition of an employee for purposes of applying APB No. 25, (b) the criteria for determining whether a plan qualifies as a non-compensatory plan, (c) the accounting consequences of various modifications to the terms of a previously fixed stock option or award, and (d) the accounting for an exchange of stock compensation awards in a business combination. FIN No. 44 became effective in July 2000, but certain conclusions cover specific events that occur after either December 15, 1998, or January 12, 2000. FIN 44 did not have a material impact on the Company's financial position, results of operations, or cash flows.

In June 2001, the FASB issued Statement No. 142 "Goodwill and Other Intangible Assets". This Statement addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, Intangible Assets. It provides guidance on how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition. This Statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. FASB Statement No. 142 does not affect the Company's financial statements.

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 - INVESTMENTS

The Company has invested in securities as of December 31, 2006 and 2005 valued at \$ 3,320,883 and \$5,483,916, respectively. These securities consisted exclusively of US Treasury Bills.

NOTE 3 - PROPERTY AND EQUIPMENT

	December 31	
	2006	2005
Computer equipment	\$ 65,612	\$ 63,311
Furniture	15,000	15,000
Office equipment	5,000	5,000
Software	55,644	55,644
Trade show booth	<u>5,000</u>	<u>5,000</u>
	146,256	143,955
Less accumulated depreciation	<u>(146,256)</u>	<u>(143,955)</u>
	<u>\$ -</u>	<u>\$ -</u>

Depreciation expense was \$2,300 and \$938, for the years ended December 31, 2006 and 2005, respectively.

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 - NOTES RECEIVABLE - EMPLOYEES

	<u>December 31</u>	
	<u>2006</u>	<u>2005</u>
Notes receivable from Employee, originally due December 31, 2005, bears interest at 2.5%, secured by 2,151,761 shares of stock in the company; this note was extended to May 14, 2009.	\$ 839,475	\$ 839,475
Notes receivable from Employee, originally due December 31, 2005, bears interest at 2.5%, secured by 198,392 shares of stock in the company; this note was extended to May 14, 2009.	126,108	126,108
Note receivable from Employee, due May 18, 2009, bears interest at 2.5%, secured by 1,250,000 shares of stock in the company	625,000	625,000
Note receivable from Employee, due May 18, 2009, bears interest at 2.5%, secured by 250,000 shares of company stock	125,000	125,000
Note receivable from Employee, due May 18, 2009, bears interest at 2.5%, secured by 50,000 shares of company stock	<u>25,000</u>	<u>25,000</u>
	<u>\$ 1,740,583</u>	<u>\$1,740,583</u>

NOTE 5 - ACCRUED LIABILITIES

	<u>December 31</u>	
	<u>2006</u>	<u>2005</u>
Accrued severance costs	\$ 11,250	\$ 11,250
Accrued wages and vacation	<u>22,067</u>	<u>39,017</u>
	<u>\$ 33,317</u>	<u>\$ 50,267</u>

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BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 - NOTES AND OBLIGATIONS PAYABLE

All notes and interests related thereto notes were repaid in 2005.

NOTE 7 - EQUITY

EXERCISE OF STOCK OPTIONS AND WARRANTS

During 2005, options and warrants to purchase 2,911,895 and 9,840,906 shares of stock were exercised for \$5,620,721.

NOTE 8 - STOCK OPTIONS

During 2000, the Company repriced all options held by the 20 remaining employees and Board members. The revised exercise price was \$0.2812 per share.

During 2000, the Company issued stock options in lieu of cash for services performed, covering 8,621,242 shares of the Company's common stock at exercise prices ranging from \$.2812 to \$4.50 per share, expiring by December 2005. \$849,654 was recorded as a general and administrative expenses based on the fair value of the stock options issued. These shares either exercised or expired in December 31, 2005.

During 2001, the Company granted options to purchase 150,000 shares of common stock exercisable at \$0.2812 per share to an independent contractor. In addition, during 2001, existing options granted to employees under variable plan accounting and unvested options being earned by contractors were revalued, resulting in a net reduction in stock-based compensation of \$280,400. Furthermore, as a result of severance agreements with certain senior officials, the lives of their options were extended to one year after termination or the full contractual life instead of expiring within a shorter time. These extensions resulted in a stock-based compensation charge of approximately \$127,947. These two adjustments resulted in a net reduction in stock-based compensation of approximately \$152,453. These options were exercised in 2005.

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 – STOCK OPTIONS (CONTINUED)

During 2001, the Company granted options to purchase 250,000 shares of common stock at an exercise price of \$0.18 to John Micek III, a member of the Board of Directors. The Company also granted options to purchase 100,000 options of common stock to an employee at an exercise price of \$0.1875 per share. The Company also granted a former employee options to purchase 50,000 shares of common stock at an exercise price of \$0.30 per share in connection with a settlement agreement. See note 7. These options were exercised in 2005.

During 2003, the Company granted a total of 200,000 options to purchase shares of common stock at an exercise price of \$.75 to two board members. These options were exercised in 2005.

During 2005, the company granted a total of 450,000 options to purchase shares of common stock at an exercise price of \$.50 to three board members.

During 2003, Richard Lang and Eric Walters exercised all their vested options totaling 2,151,761 and 198,392 shares, respectively. As part of this transaction, the company officers signed notes payable to the company for \$839,475 and \$126,107, respectively. These non-recourse notes were originally due December 31, 2005. These shares are collateral on the notes. These notes bear interest at the rate 2.5% per annum and were extended to a new due date of May 14, 2009.

During 2005, Richard Lang, Eric Walters and Colt Briner exercised all their vested options totaling 1,250,000, 250,000 and 50,000 shares, respectively. As part of this transaction, the company took notes payable to the company from these officers/employees for \$625,000, \$125,000 and \$25,000, respectively. These non-recourse notes are due May 18, 2009. These shares are collateral on the notes.

The Company applies APB opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations in accounting for options issued to employees. Compensation cost for stock options is measured at the intrinsic value, which is the excess of the market price of the Company's common stock at the date of grant over the amount the recipient must pay to acquire the common stock. Statement of Financial Accounting Standards No. 123 (SFAS 123), "Accounting for Stock-Based Compensation", requires the Company to provide pro forma information regarding net income (loss) and earnings (loss) per share as if compensation cost for employee stock options has been determined in accordance with the fair value based method prescribed by SFAS 123.

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 – STOCK OPTIONS (CONTINUED)

The option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In addition, valuation models require input of highly subjective assumptions, including the expected price volatility. Since the Company's stock options have characteristics significantly different from those of traded options, and since variations in the subjective input assumptions can materially affect the fair value estimate, the actual results can vary significantly from estimated results.

	<u>Number of Shares</u>	<u>Weighted Average Exercise Price</u>
Balance on December 31, 2004	<u>2,146,745</u>	<u>\$1.00</u>
Options granted	2,200,000	\$0.68
Options exercised	(2,911,895)	\$0.49
Options expired	(759,250)	\$0.00
Options forfeited	<u>-0-</u>	<u>\$0.00</u>
Balance on December 31, 2005	<u>675,600</u>	<u>\$1.29</u>
Options expired	<u>2,500</u>	<u>\$0.00</u>
Balance on December 31, 2006	<u>673,100</u>	<u>\$1.48</u>

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8 – STOCK OPTIONS (CONTINUED)

Stock options outstanding and exercisable at December 31, 2006 are as follows:

	<u>Options Outstanding</u>			<u>Options Exercisable</u>		
	<u>Shares Outstanding</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Life</u>	<u>Shares Outstanding</u>	<u>Weighted Average Exercise Price</u>	
\$0.50-\$0.99	400,000	\$0.50	1.38	400,000	\$0.50	
\$1.00-\$1.50	13,100	\$1.41	1.20	13,100	\$1.41	
\$2.50	200,000	\$2.50	3.57	200,000	\$2.50	
\$4.63	<u>60,000</u>	<u>\$4.63</u>	<u>3.74</u>	<u>60,000</u>	<u>\$4.63</u>	
	<u>673,100</u>	<u>\$1.48</u>	<u>2.24</u>	<u>673,100</u>	<u>\$1.48</u>	

	<u>Warrants Outstanding</u>			<u>Warrants Exercisable</u>		
	<u>Shares Outstanding</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Life</u>	<u>Shares Outstanding</u>	<u>Weighted Average Exercise Price</u>	
\$1.50	83,334	\$1.50	2.78	83,334	\$1.50	
\$3.50	<u>128,484</u>	<u>\$3.50</u>	<u>1.00</u>	<u>128,484</u>	<u>\$3.50</u>	
	<u>211,818</u>	<u>\$2.71</u>	<u>1.70</u>	<u>211,818</u>	<u>\$2.71</u>	

NOTE 9 – LEASE COMMITMENTS

The Company leases its office space under a one year operating lease, which provides for one-year extensions. The lease was extended to April 30, 2007.

Rent paid in the years ended December 31, 2006 and 2005 was \$16,054 and \$13,205, respectively.

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10 – INCOME TAXES

The provisions for federal and state income taxes for the years ended December 31, 2006 and 2005 are as follows:

	December 31	
	<u>2006</u>	<u>2005</u>
Current	\$ -	\$ 14,986,102
Deferred	<u>-</u>	<u>(13,535,542)</u>
Total provision for income taxes	<u>\$ -</u>	<u>\$ 1,450,560</u>

At December 31, 2006 and 2005, the Company had net operating loss carry-forwards for federal income tax purposes of approximately \$16,000,000 and \$15,460,000, respectively which are subject to annual limitations, and are available to offset future taxable income, if any, through 2022.

As of December 31, 2004 net operating loss carry-forwards for state income tax purposes were approximately \$22,670,000 of which \$20,465,487 were used to offset state taxable income for 2005. At December 31, 2006 net operating loss carry-forwards for state income tax purposes are approximately \$2,770,000.

The temporary differences that give rise to deferred tax assets and liabilities at December 31, 2006 and 2005 are as follows:

	<u>2006</u>	<u>2005</u>
Deferred tax assets:		
Net operating losses	\$ 5,692,211	\$ 5,451,623
Research and experimentation credit	421,900	421,900
State income tax effect on federal	<u>398,314</u>	<u>398,161</u>
Total deferred tax assets	6,512,426	6,271,684
Less valuation allowance	<u>(6,512,426)</u>	<u>(6,271,684)</u>
Net deferred tax assets	<u>\$ -</u>	<u>\$ -</u>

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10 – INCOME TAXES (CONTINUED)

In assessing the amount of deferred tax assets to be recognized, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. It is not possible at this time to determine that the deferred tax assets are more likely to be realized than not. Accordingly, a full valuation allowance has been established for all periods presented.

The Tax Reform Act of 1986 imposed substantial restrictions on the utilization of net operating losses and tax credits in the event of an “ownership change”, as defined by the Internal Revenue Code. All federal and state net operating loss carryforwards are subject to limitations as a result of these restrictions. If there should be a subsequent ownership change, as defined, the Company’s ability to utilize its carryforwards could be reduced.

NOTE 11 – BUSINESS RISKS AND SEGMENT DISCLOSURES

The Company’s primary source of revenue is the licensing of Burst technology, and its success is largely dependent on this licensing effort. Changes in desirability of this technology in the marketplace may significantly affect the Company’s future operating results.

The Company operates in one segment and accordingly has provided only the required enterprise wide disclosure. The Company recognized no foreign revenues in 2006 and 2005.

NOTE 12 – SETTLEMENTS

The Company settled various long-standing account payable balances. These settlements resulted in a recovery of \$0 and \$180,000 in 2006 and 2005 respectively. In addition, the Company received a one-time payment of \$300,000 for the release of a claim that was resolved by settlement. The payment was reduced by attorneys' fees and costs.

NOTE 13 - REVENUE FROM LICENCING AGREEMENT

In 2005, the company entered into a settlement agreement with a major software company. This settlement provided the software company with a non-exclusive licensing agreement in exchange for a one-time payment to Burst of \$60,000,000. Legal costs associated with this settlement totaled \$22,147,333 (including attorney's fees and \$1,789,705 in costs).

BURST.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 14 - CORRECTION TO THE 2005 FINANCIAL STATEMENTS

During the period ended December 31, 2005, the Company's net income was understated by \$248,707. This understatement consisted of the following:

	<u>Effect on Net Income</u> <u>Increase (Decrease)</u>
Federal income tax expense	\$ 725,296
State income tax expense	41,490
General and Administrative expenses	<u>(518,079)</u>
Total	<u>\$ 248,707</u>

The change in general and administrative expenses arose from an error in the computation resulting from the exercise of 2,911,895 options. This error resulted in the reduction of the state income taxes and part of the reduction of the federal income tax expense. In addition, after the financial statements were prepared, the company discovered that it qualified for a federal exemption to the Alternative Minimum Tax which was not provided for in the financial statements as originally prepared.