



BURST.COM, INC. AND SUBSIDIARY

**Consolidated Financial Statements
December 31, 2009 and 2008**

BURST.COM, INC. AND SUBSIDIARY

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December 31, 2009 and 2008

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Independent Auditors' Report

To the Board of Directors and Shareholders of
Burst.com, Inc. and Subsidiary

We have audited the accompanying consolidated balance sheet of Burst.com, Inc. (a Delaware Corporation) and subsidiary (the "Company") as of December 31, 2009, and the related consolidated statements of operations, shareholders' equity, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The financial statements as of December 31, 2008, were audited by Smith, Lange & Phillips LLP, who merged with Daoro, Zydel & Holland LLP as of July 1, 2009, to form DZH Phillips LLP, and whose report dated April 1, 2009, expressed an unqualified opinion on those statements.

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 provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2009, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

DZH Phillips LLP

San Francisco, California
March 19, 2010

BURST.COM, INC. AND SUBSIDIARY

Consolidated Balance Sheets

December 31, 2009 and 2008

Assets

	2009	2008
Current assets		
Cash and cash equivalents	\$ 181,927	\$ 4,757,691
Investments in Treasury notes	6,442,297	1,179,053
Income tax recoverable	789,679	-
Interest receivable	108,534	-
Note receivable, related party	10,759	-
Prepaid expenses and advances	2,948	2,948
	7,536,144	5,939,692
Property and equipment, net	-	-
Other assets		
Income tax recoverable	-	723,744
Other assets	8,740	8,740
	8,740	732,484
	\$ 7,544,884	\$ 6,672,176
Liabilities		
Current liabilities		
Accrued expenses and accounts payable	\$ 70,239	\$ 15,667
Income tax payable	52,702	800
	122,941	16,467
Shareholders' equity		
Convertible preferred stock, \$.00001 par value; 20,000,000 shares authorized; none issued and outstanding	-	-
Common stock, \$.00001 par value; 100,000,000 shares authorized; 42,500,480 and 40,900,480 shares issued and outstanding, respectively	426	410
Additional paid-in-capital	67,382,442	68,094,042
Accumulated deficit	(59,149,753)	(59,813,950)
Shareholders' notes receivable, including accrued interest of \$153,942 and \$224,950, respectively	(820,232)	(1,637,890)
Accumulated other comprehensive income:		
Unrealized gain on marketable securities	9,060	13,097
	7,421,943	6,655,709
	\$ 7,544,884	\$ 6,672,176

See auditors' report and accompanying notes.

BURST.COM, INC. AND SUBSIDIARY

Consolidated Statements of Operations

Years Ended December 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Revenue	\$ 2,600,000	\$ 533,500
Costs and expenses:		
General and administrative	1,414,323	1,656,981
Research and development	573,722	-
Legal fees and costs associated with licensing revenue	52,514	132,536
	<u>2,040,559</u>	<u>1,789,517</u>
Income (loss) from operations	559,441	(1,256,017)
Other income (expenses):		
Interest income	148,439	160,888
Other income	368	104
Interest expense	(73,983)	(6)
Gain on sale of securities	17,746	41,045
Other taxes	65,768	(6,142)
	<u>158,338</u>	<u>195,889</u>
Income (loss) before income taxes	717,779	(1,060,128)
Income taxes	53,582	18,866
Net income (loss)	<u>\$ 664,197</u>	<u>\$ (1,078,994)</u>
Unrealized loss	<u>(4,037)</u>	<u>(11,517)</u>
Total comprehensive income (loss)	<u>\$ 660,160</u>	<u>\$ (1,090,511)</u>
Net income (loss) per share, basic	<u>\$ 0.0437</u>	<u>\$ (0.0265)</u>
Net income (loss) per share, diluted	<u>\$ 0.0436</u>	<u>\$ (0.0265)</u>
Weighted average number of common shares outstanding	<u>42,057,740</u>	<u>40,842,398</u>

See auditors' report and accompanying notes.

BURST.COM, INC. AND SUBSIDIARY

Consolidated Statements of Shareholders' Equity

Years Ended December 31, 2009 and 2008

	Common Stock	Amount	Shareholders' Notes	Accumulated Other Comprehensive Income	Additional Paid-In Capital	Accumulated Deficit	Total
Balance, December 31, 2007, as restated	38,250,480	\$ 383	\$ (1,438,022)	\$ 24,614	\$ 67,908,569	\$ (58,734,956)	\$ 7,760,588
Sale of stock, \$.07 per share	2,650,000	27	(148,400)	-	185,473	-	37,100
Net loss	-	-	-	-	-	(1,078,994)	(1,078,994)
Unrealized gain on securities	-	-	-	(11,517)	-	-	(11,517)
Interest earned on shareholders' notes	-	-	(51,468)	-	-	-	(51,468)
Balance, December 31, 2008	40,900,480	410	(1,637,890)	13,097	68,094,042	(59,813,950)	6,655,709
Sale of stock, \$.09 per share	3,150,000	32	(28,350)	-	56,668	-	28,350
Cancellation of shares and notes receivable	(1,550,000)	(16)	775,000	-	(774,984)	-	-
Write off interest earned on cancelled notes receivable	-	-	123,489	-	-	-	123,489
Options granted	-	-	-	-	6,716	-	6,716
Net income	-	-	-	-	-	664,197	664,197
Unrealized loss on securities	-	-	-	(4,037)	-	-	(4,037)
Interest earned on notes receivable	-	-	(52,481)	-	-	-	(52,481)
Balance, December 31, 2009	<u>42,500,480</u>	<u>\$ 426</u>	<u>\$ (820,232)</u>	<u>\$ 9,060</u>	<u>\$ 67,382,442</u>	<u>\$ (59,149,753)</u>	<u>\$ 7,421,943</u>

See auditors' report and accompanying notes.

BURST.COM, INC. AND SUBSIDIARY

Consolidated Statements of Cash Flows

Years Ended December 31, 2009 and 2008

	2009	2008
Cash flows from operating activities:		
Net income (loss)	\$ 664,197	\$ (1,078,994)
Adjustments to reconcile net income (loss)		
to net cash used by operating activities:		
Decrease in comprehensive income	(4,037)	(11,517)
Compensation expense for options granted	6,716	-
Realized gain on securities	17,746	41,045
Write off interest earned on cancelled notes receivable	123,489	-
(Increase) decrease in assets:		
Prepaid expenses and advances	-	16,513
Income tax recoverable	(65,935)	-
Interest receivable on income tax recoverable	(108,534)	-
Interest receivable on shareholders' notes	(52,481)	(51,468)
Increase (decrease) in liabilities:		
Accounts payable and accrued expenses	54,572	(80,040)
State income taxes payable	51,902	(139,395)
Net cash provided (used in) by operating activities	687,635	(1,303,856)
Cash flows from investing activities:		
(Investments in) proceeds from		
sale of securities available-for-sale, net	(5,280,990)	203,909
Payment to note receivable, shareholder	(10,759)	-
Cash (used in) provided by investing activities	(5,291,749)	203,909
Cash flows provided by financing activities:		
Proceeds from sale of common stock	28,350	37,100
Net cash provided by financing activities	28,350	37,100
Net (decrease) increase in cash and cash equivalents	(4,575,764)	(1,062,847)
Cash and cash equivalents, beginning of year	4,757,691	5,820,538
Cash and cash equivalents, end of year	\$ 181,927	\$ 4,757,691
Supplemental disclosures:		
Cash paid for income taxes	\$ 1,640	\$ 18,066
Cash paid for interest	\$ -	\$ 6
Non-cash transactions:		
Sale of stock applied to shareholders' notes	\$ (28,350)	\$ (148,400)
Cancellation of stock applied to shareholders' notes	775,000	-
	\$ 746,650	\$ (148,400)

See auditors' report and accompanying notes.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Description of Business and Summary of Significant Accounting Policies

Organization and capitalization - Burst.com, Inc., a Delaware corporation (together with its subsidiary unless the context otherwise requires, the "Company") and its subsidiary was incorporated in the State of Delaware as Instant Video Technologies, Inc. On January 27, 2000, the Certificate of Incorporation 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 shareholders, 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, 2009 and 2008.

Business - The Company monetizes, via licensing and sales, burst transmission technology and other intellectual property for use within commercial, multimedia and interactive environments. The burst technology allows for burst transmission of video/audio programming that result in time-savings, network efficiency and superior quality production.

Principles of consolidation - The consolidated financial statements include the accounts of Burst.com, Inc. and its wholly-owned subsidiary, Timeshift-TV, Inc. All significant intercompany balances and transactions have been eliminated. For the years ended December 31, 2009 and 2008, the subsidiary was inactive.

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.

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

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Description of Business and 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 (FDIC) up to \$250,000. From time to time, the Company had cash in financial institutions in excess of federally insured limits. As of December 31, 2009 and 2008, there were no cash balances in excess of FDIC limits.

Investments - The Company's investments consisted of debt securities classified as available-for-sale. Accordingly, they were carried at fair value. Unrealized gains and losses for available-for-sale securities are excluded from earnings and reported, net of deferred income taxes, as other comprehensive income.

Comprehensive income - The Company reports 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 years ended December 31, 2009 and 2008, the Company's comprehensive income consists of unrealized gains and losses on securities available for sale, net of the related estimated deferred income tax effect associated with those gains and losses.

Revenue recognition - Revenue from the sale of patents are recognized when received. License fees are generally recognized as revenue ratably over the license period. Revenue from settlements is recognized when received. The revenue from settlements is reported gross of legal fees and costs.

Research and development costs - Research and development costs represent salaries, related benefits, costs, expenses incurred for the design and testing of new products and processing methods and other expenses related to the research development of new products. Research and development costs are expensed as incurred.

Property, equipment and depreciation - 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.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)

Fair value of financial instruments - The Company's financial instruments consist primarily of cash and cash equivalents and available-for-sale securities. 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 income (loss) per common share and dilutive securities - Basic earnings (loss) per share is computed by dividing net income, after deducting preferred stock dividends accumulated during the period, if any, by the weighted-average number of shares of common stock outstanding during each period. Diluted earnings (loss) 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.

For the years ended December 31, 2009 and 2008, there were no incremental shares.

Income taxes - The Company recognizes deferred tax assets and liabilities for future tax consequences of events that have been previously recognized in the Company's financial statements or tax returns. The measurement of deferred tax assets and liabilities is based on provisions on the enacted tax law; the effects of future changes in tax laws or rates are not anticipated.

The Company is required to evaluate its uncertain tax positions, if any. The evaluation of a tax position is a two-step process. Step one is *Recognition*. *Recognition* occurs when a company concludes that a tax position, based solely on technical merits, will more likely than not be sustained upon challenge by a tax authority. Step two is *Measurement*. *Measurement* can only take place if recognition occurs. The measurement process provides that when the more likely than not threshold is met, the position must be analyzed to determine the amount of benefit to recognize in the financial statements. "Highly certain positions" are fully recognized but require an independent evaluation that the position is in fact highly certain; all other positions are measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement with a tax authority.

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Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)

Income taxes (continued) - The Company's present policy is to evaluate all tax positions based on either having substantial authority for a tax position taken on a return or where substantial authority does not exist, then the Company discloses the tax treatment of the item and ensures that there is a reasonable basis for the treatment. The Company has not taken tax positions for any years open under the various statutes of limitations that required disclosure because they were not supported by substantial authority. The Company believes that most if not all of its positions supported by substantial authority would meet the recognition standard. The Company has not evaluated any tax positions with respect to the "measurement" standard and believes there are no tax position taken that is required to be treated as "uncertain".

Advertising costs - Advertising costs are expensed as incurred. For the years ended December 31, 2009 and 2008, there were no advertising costs.

Patent expenses - The Company charges the costs of internally developing patents to expense as they are incurred.

Stock-based compensation - All share-based payments to employees (or to non-employee directors as compensation for service on the Board of Directors) are recognized as compensation expense in the consolidated financial statements, based on the fair values of such payments.

The Company estimates the value of the options granted to employees using the Black-Scholes model. The expected term represents the period of time that options granted are expected to be outstanding, which is usually the time until the option expires. The risk-free interest rate for each option is based on the Treasury bill yield in effect at the date of each grant assuming the expected term to maturity.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Description of Business and Summary of Significant Accounting Policies (continued)

Stock-based compensation (continued) - For the year ended December 31, 2009, the Company granted 3,978,450 shares of stock options to the Company's employees. The terms of the awards include service, market and performance conditions. Compensation cost is recognized only if the performance and service condition is satisfied. Market conditions are reflected in the fair value of the stock options. As of December 31, 2009, management determined that performance conditions were not probable for all stock option awards, except one award where performance condition occurred before December 31, 2009. Consequently, for the year ended December 31, 2009, the Company has recorded stock options compensation expense for the 92,000 stock options vested upon completion of the performance condition, or \$6,716. The values of the stock option awards range from \$0.020 to \$0.091, depending on the grant date and the expected term, with the weighted average fair value of \$0.076.

For the year ended December 31, 2008, there were no stock options granted.

The assumptions used in the calculation of the fair value of the options granted in 2009, using the Black-Scholes model, were as follows:

Weighted average exercise price	\$0.25
Weighted average expected term (in years)	1-5
Expected volatility	137%
Weighted average risk-free interest rate	1.8%-2%

For the years ended December 31, 2009 and 2008, there were no warrants granted.

Stock-based compensation arrangements to nonemployees are accounted for using a fair value approach. The compensation costs of these arrangements are booked as consulting expense. Awards granted to directors appointed by employer's shareholders for their services as directors will be treated as awards to employees. Awards granted to directors for other services are accounted for as awards to nonemployees. For the years ended December 31, 2009 and 2008, no options were granted to nonemployees.

Subsequent events - Management has evaluated events and transactions for potential recognition or disclosure through March 19, 2010, which represents the date the financial statements were available to be issued. Management has determined that, as of that date, there were no subsequent events, except as disclosed in Note 12.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 2 - Investments in Securities Available-For-Sale

Investments consist exclusively of US Treasury notes. As of December 31, 2009 and 2008, the aggregate market value of investments exceeded their aggregate cost by \$9,060 and \$13,097, respectively.

As of December 31, 2009, investments consisted of the following:

	<u>Cost</u>	<u>Gross Unrealized Gain</u>	<u>Gross Unrealized Loss</u>	<u>Fair Market Value</u>
US Treasury notes, due within one year	\$ <u>6,433,237</u>	\$ <u>9,060</u>	\$ <u>-</u>	\$ <u>6,442,297</u>

As of December 31, 2008, investments consisted of the following:

	<u>Cost</u>	<u>Gross Unrealized Gain</u>	<u>Gross Unrealized Loss</u>	<u>Fair Market Value</u>
US Treasury notes, due within one year	\$ <u>1,165,956</u>	\$ <u>13,097</u>	\$ <u>-</u>	\$ <u>1,179,053</u>

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 3 - Fair Value Measurements

As of December 31, 2009, the Company's assets at fair value set forth by level, within the fair value hierarchy, were as follows:

	<u>Level 1</u>
U.S. government securities	\$ <u>6,442,297</u>
Total assets at fair value	\$ <u><u>6,442,297</u></u>

U.S. government securities: Valued at the closing price reported on the active market on which the individual securities are traded.

As of the year ended December 31, 2009, there were no level 2 or level 3 investments.

Note 4 - Property and Equipment

As of December 31, 2009 and 2008, property and equipment consisted of the following:

	<u>2009</u>	<u>2008</u>
Computer equipment	\$ 65,612	\$ 65,612
Furniture	20,669	20,669
Office equipment	5,000	5,000
Software	55,644	55,644
Trade show booth	<u>5,000</u>	<u>5,000</u>
	151,925	151,925
Less accumulated depreciation	<u>(151,925)</u>	<u>(151,925)</u>
	\$ <u>-</u>	\$ <u>-</u>

For the years ended December 31, 2009 and 2008, there was no depreciation expense.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 5 - Notes Receivable - Shareholders

Stock subscriptions receivable that resulted from stock option exercises are reported as a deduction from shareholders' equity. As of December 31, 2009 and 2008, notes receivable-shareholders consisted of the following:

	<u>2009</u>	<u>2008</u>
Note receivable from employee bears interest at 3.65% per annum; secured by 500,000 shares of stock in the Company; due September 22, 2012.	\$ 376,982	\$ 376,982
Note receivable from employee bears interest at 3.65% per annum; secured by 156,975 shares of stock in the Company; due September 20, 2012.	112,558	112,558
Note receivable from employee, bears interest at 3.65% per annum; secured by 1,250,000 shares of stock in the company; cancelled on April 11, 2009, as discussed below.	-	625,000
Note receivable from employee bears interest at 3.65% per annum; secured by 250,000 shares of company stock; cancelled on April 11, 2009, as discussed below.	-	125,000
Note receivable from employee bears interest at 3.65% per annum; secured by 50,000 shares of company stock; cancelled on April 11, 2009, as discussed below.	-	25,000
Note receivable from employee bears interest at 3.58% per annum; secured by 1,400,000 shares of company stock; due December 28, 2016.	78,400	78,400
Note receivable from director bears interest at 3.58% per annum; secured by 400,000 shares of company stock; due December 28, 2016.	22,400	22,400

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 5 - Notes Receivable - Shareholders (continued)

	<u>2009</u>	<u>2008</u>
Note receivable from director bears interest at 3.58% per annum; secured by 400,000 shares of company stock; due December 28, 2016.	22,400	22,400
Note receivable from director bears interest at 3.58% per annum; secured by 400,000 shares of company stock; due December 28, 2016.	22,400	22,400
Note receivable from employee bears interest at 3.58% per annum; secured by 50,000 shares of company stock; due December 28, 2016.	2,800	2,800
Note receivable from employee bears interest at 2.05% per annum; secured by 2,000,000 shares of company stock; due March 11, 2018.	18,000	-
Note receivable from employee bears interest at 2.05% per annum; secured by 300,000 shares of company stock; due March 11, 2018.	2,700	-
Note receivable from director bears interest at 2.05% per annum; secured by 250,000 shares of company stock; due March 11, 2018.	2,250	-
Note receivable from director bears interest at 2.05% per annum; secured by 250,000 shares of company stock; due March 11, 2018.	2,250	-
Note receivable from director bears interest at 2.05% per annum; secured by 250,000 shares of company stock; due March 11, 2018.	2,250	-
Note receivable from employee bears interest at 2.05% per annum; secured by 100,000 shares of company stock; due March 11, 2018.	<u>900</u>	<u>-</u>
	666,290	1,412,940

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

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Note 5 - Notes Receivable - Shareholders (continued)

	<u>2009</u>	<u>2008</u>
Accrued interest on notes receivable	<u>153,942</u>	<u>224,950</u>
	\$ <u>820,232</u>	\$ <u>1,637,890</u>

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 executed notes payable to the Company for \$839,475 and \$126,107, respectively. The shares served as collateral on the notes. On December 20, 2007, the Company reformed the notes from being non-recourse to full recourse. In addition, the Company repurchased 1,651,761 shares of common stock from Richard Lang and reduced the principal amount of his note by \$462,493. The Company also repurchased 48,392 shares of common stock from Eric Walters and reduced the principal amount of his note by \$13,550. The shares were tendered at the December 20, 2007 share price of \$.28 per share.

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 officers and employees executed non-recourse notes payable to the Company for \$625,000, \$125,000 and \$25,000, respectively. The shares were collateral on the notes. On April 11, 2009, the Company cancelled these shares, including the notes receivable, as discussed below.

On January 28, 2008, the Company issued 1,200,000 shares of non-lapse restriction stock to three of its board members; each board member received 400,000 shares of stock. Also, on January 28, 2008, the Company issued 1,450,000 to two of its employees; one employee received 1,400,000 shares and another received 50,000 shares. The shares are subject to a non-lapse restriction in the nature of substantially discounted right of first refusal. The shares sold are burdened with a perpetual right of first refusal pursuant to which the purchasers are required to first offer the shares to the Company for a period of five business days at a discount of \$.34 from whatever price a third party offers before they can be sold to that third party. The purchase price for the stock burdened with that right of first refusal was \$.07, payable 20% in cash and 80% by execution and delivery of a non-recourse promissory note due on December 31, 2016. The total amount of cash received by the Company for the issued shares was \$37,100. The total amount of non-recourse notes executed by the Board of Directors and employees of the Company was \$148,400.

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Notes to Consolidated Financial Statements

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Note 5 - Notes Receivable - Shareholders (continued)

On April 11, 2009, the Company issued 750,000 shares of non-lapse restriction stock to three of its board members; each board member received 250,000 shares of stock. Also, on April 11, 2009, the Company issued 2,400,000 to three of its employees; Richard Lang received 2,000,000 shares, Eric Walters received 300,000 and Colt Briner received 100,000 shares. The shares are subject to a non-lapse restriction in the nature of substantially discounted right of first refusal. The shares sold are burdened with a perpetual right of first refusal pursuant to which the purchasers are required to first offer the shares to the Company for a period of five business days at a discount of \$.102 from whatever price a third party offers before they can be sold to that third party. The purchase price for the stock burdened with that right of first refusal was \$.018, payable 50% in cash and 50% by execution and delivery of a non-recourse promissory note due on March 11, 2018. The total amount of cash received by the Company for the issued shares was \$28,350. The total amount of non-recourse notes executed by the Board of Directors and Employees of the Company was \$28,350.

On April 11, 2009, the Company cancelled 1,250,000 shares of common stock of Richard Lang, 250,000 shares of common stock of Eric Walters, and 50,000 shares of common stock of Colt Briner in exchange for their outstanding nonrecourse notes in the amounts of \$625,000, \$125,000 and \$25,000, respectively. As of April 11, 2009, accrued interest related on the notes was \$123,489. For the year ended December 31, 2009, the Company wrote off accrued interest of \$123,489 on its consolidated statements of operations.

Note 6 - Stock Options

On April 11, 2009, the Company adopted a 2009 Nonqualified Stock Option Plan (the "Plan"). The number of shares that may be subject to options under the Plan and sold under the Plan is 4,000,000 shares of common stock of the Company. The options are not transferrable and can only be exercised by the optionee. The options expire in 10 years. The grant of the options under the Plan is discretionary and can be authorized individually by the Board of Directors.

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Notes to Consolidated Financial Statements

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Note 6 - Stock Options (continued)

The following is a summary of all options and warrants activity for the years ended December 31, 2009 and 2008.

	<u>Options Outstanding</u>		<u>Warrants Outstanding</u>	
	Number of	Weighted	Number of	Weighted
	Shares	Average	Shares	Average
		Exercise		Exercise
		Price		Price
Balance, December 31, 2007	672,100	\$ 1.48	683,334	\$ 1.55
Options/warrants expired	<u>(412,100)</u>	\$ 0.52	<u>(38,000)</u>	\$ 1.50
Balance, December 31, 2008	260,000	\$ 2.99	645,334	\$ 1.56
Options/warrants granted	3,978,450	\$ 0.25	-	
Options/warrants expired	<u>(207,000)</u>	\$ 0.25	-	
Balance, December 31, 2009	<u>4,031,450</u>	\$ 2.99	<u>645,334</u>	\$ 1.56

As of December 31, 2009, stock options and warrants exercisable were as follows:

Options:

Exercise Price Per Share	<u>Options Outstanding</u>			<u>Options Exercisable</u>		
	Options Granted	Number Outstanding	Weighted Average Exercise Price	Weighted Average Contractual Remaining Life (Years)	Number Exercisable	Weighted Average Exercise Price
\$2.50	200,000	200,000	\$ 2.50	0.57	200,000	\$ 2.50
\$4.63	60,000	60,000	\$ 4.63	0.74	60,000	\$ 4.63
\$0.25	3,978,450	3,771,450	\$ 0.25	4.50	164,450	\$ 0.25
	<u>4,238,450</u>	<u>4,031,450</u>	\$ 0.33	4.42	<u>424,450</u>	\$ 0.33

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 6 - Stock Options (continued)

For the year ended December 31, 2009, 3,978,450 options were granted and 207,000 options were cancelled. For the year ended December 31, 2008, no options were granted.

Warrants:

Exercise Price per Share	Warrants Outstanding			Warrants Exercisable		
	Warrants Granted	Number Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Number Exercisable	Weighted Average Exercise Price
\$1.50	45,334	45,334	\$ 1.50	0.74	45,334	\$ 1.50
\$1.56	600,000	600,000	\$ 1.56	2.39	600,000	\$ 1.56
	<u>645,334</u>	<u>645,334</u>	\$ 1.56	2.21	<u>645,334</u>	\$ 1.56

For the years ended December 31, 2009 and 2008, no warrants were granted. All warrants previously granted were fully vested at the date of the grant.

Note 7 - Lease Commitments

The Company leased its office space under a one-year operating lease, which provided for one-year extensions. On November 15, 2009, the Company executed a new office lease, which provides for a 36 month term and is effective starting February 1, 2010 and expires on February 1, 2013. Under the terms of the lease agreement, the Company has the option of terminating the lease after the first year with 120 days notice.

Future minimum rental payments of these leases are as follows:

Year Ending December 31,

2010	\$ 52,400
2011	57,100
2012	57,100
2013	<u>4,800</u>
	\$ <u>171,400</u>

For the years ended December 31, 2009 and 2008, rent expense was \$37,071 and \$32,778, respectively.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 8 - Income Taxes

For the years ended December 31, 2009 and 2008, the provisions for federal and state income taxes are as follows:

	2009	2008
Current	\$ 53,582	\$ 18,866
Deferred	-	-
	\$ 53,582	\$ 18,866

As of December 31, 2009 and 2008, the Company had net operating loss carry-forwards for federal income tax purposes of approximately \$12,700,000 and \$13,000,000, respectively, subject to annual limitations, and are available to offset future taxable income, if any, through 2029.

As of December 31, 2008, the Company had a net operating loss carryforward for state income tax purposes of approximately \$1,000,000, subject to annual limitations, and is available to offset future taxable income, if any, through 2029.

As of December 31, 2009 and 2008, deferred tax assets, net, were comprised of the following:

	2009	2008
Deferred tax assets (liabilities):		
Net operating losses	\$ 4,377,067	\$ 4,620,795
Research and experimentation credit	449,832	421,900
Income tax recoverable	(74,743)	-
State income tax effect	17,062	816
Stock option compensation expense	2,877	-
Other	3,505	2,418
Total deferred tax assets, net	4,775,600	5,051,304
Less valuation allowance	(4,775,600)	(5,051,304)
	\$ -	\$ -

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 years presented.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 8 - Income Taxes (continued)

For the year ended December 31, 2009, the reconciliation between the federal statutory income tax rate and the Company's effective tax rate was as follows:

	<u>2009</u>
Income tax provision at federal statutory rates	\$ 244,059
Current state income taxes, net of federal benefits	41,880
Net operating loss offset by valuation allowance	(240,738)
Permanent differences	9,387
Other	<u>(1,006)</u>
	\$ <u>53,582</u>

Note 9 - Business Risks

The Company's sources of revenue include the sale of patents and licensing of its proprietary technology. Changes in desirability of this technology in the marketplace may significantly affect the Company's future operating results.

For the years ended December 31, 2009 and 2008, the Company had no foreign revenues.

Note 10 - Revenue

Revenue from patents - During 2009, the Company sold its DVR patent (U.S. Patent no. 7,272,298), as well as several DVR-related pending U.S. patent applications to a non-affiliated company for a total one-time payment of \$2.3 million.

BURST.COM, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 10 – Revenue (continued)

Revenue from settlements - During 2009, the Company entered into a settlement agreement with a major technology company. This settlement agreement provided the technology company with a non-exclusive license in exchange for a one-time payment to the Company of \$300,000. Legal fees and costs associated with this settlement totaled approximately \$52,500 (equal to 17.5% of the remaining gross settlement of \$300,000).

During 2008, the Company entered into a settlement agreement with a major technology company. This settlement agreement provided the technology company with a non-exclusive license in exchange for a one-time payment to the Company of \$533,500. Legal fees and costs associated with this settlement totaled \$132,536 (equal to \$44,947 in initial costs plus 17.5% of the remaining gross settlement of \$488,553 plus \$2,092 of additional costs associated with the lawsuit).

Note 11 - Related Party Transaction

In January 2009, a director borrowed \$46,000 from the Company. As of December 31, 2009, the outstanding balance was \$10,759.

Note 12 - Subsequent Event

On January 28, 2010, the Company received the California tax refund of approximately \$900,000 which includes the income tax recoverable amount plus accrued interest of approximately \$108,000.

In March 2010, the Company changed its name to Democrasoft, Inc.