

COMPANY REGISTRATION NUMBER 3533689 (DELAWARE)

**121MEDIA, INC.**

**ANNUAL REPORT AND FINANCIAL STATEMENTS**

**31 DECEMBER 2006**

# 121MEDIA, INC.

## CONTENTS OF THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

---

<b>CONTENTS</b>	<b>PAGES</b>
Company information	1 to 2
Chairman's statement	3 to 4
Chief Executive Officer's report	5
Directors and Officers	6
Report of the directors	7 to 9
Directors' remuneration report	10
Corporate governance report	11 to 12
Statement of directors' responsibilities	13
Independent auditors' report to the shareholders	14
Group profit and loss account	15
Statement of total recognized gains and losses	16
Group balance sheet	17
Company balance sheet	18
Group cash flow statement	19
Notes to the financial statements	20 to 34

---

# 121MEDIA, INC.

## COMPANY INFORMATION

YEAR ENDED 31 DECEMBER 2006

---

**THE BOARD OF DIRECTORS**

D Svendsen  
K Ertugrul  
D Gwozdz  
G Baz

**COMPANY SECRETARY**

J Bottomley

**COMPANY NUMBER**

3533689 (Delaware)

**REGISTERED OFFICE**

2711 Centerville Road  
Suite 400  
City of Wilmington 19808  
County of New Castle  
Delaware  
USA

**AUDITOR**

H.W Fisher & Company  
Chartered Accountants  
& Registered Auditors  
Acre House  
11/15 William House  
London  
NW1 3ER  
United Kingdom

**SOLICITORS**

Nabarro  
Lacon House  
Theobald's Road  
London  
WC1X 8RW  
United Kingdom

# 121MEDIA, INC.

## COMPANY INFORMATION *(continued)*

YEAR ENDED 31 DECEMBER 2006

---

**HEAD OFFICE**

Golden Cross House  
8 Duncannon Street  
London  
WC2N 4JF  
United Kingdom

**LONDON STOCK EXCHANGE  
COMPANY CODE**

OTO and OTOM

**NOMINATED ADVISOR  
AND BROKER**

Canaccord Adams Limited  
7<sup>th</sup> Floor, Cardinal Place  
80 Victoria Street  
London  
SW1E 5JL  
United Kingdom

**REGISTRAR**

Capita IRG (Offshore) Limited  
Victoria Chambers  
Liberation Square  
1/3 The Esplanade  
St Helier  
Jersey

**TRANSFER AGENT**

Capita IRG plc  
The Registry  
34 Beckenham Road  
Beckenham  
Kent  
BR3 4TU  
United Kingdom

# 121MEDIA, INC.

## CHAIRMAN'S STATEMENT

YEAR ENDED 31 DECEMBER 2006

---

### RESULTS AND DIVIDEND / FINANCIALS

I am pleased to announce the results of 121Media, Inc. ("121Media" or the "Group") for the year ending 31 December 2006. During 2006, we made a strategic shift away from the desktop based business in order to fully pursue our ISP relationship strategy. As anticipated, this move has impacted our short-term financial performance and thus the results we are now publishing do not reflect the prospects that our recent investments in people and technology represent.

Turnover for the Group for the year to 31 December 2006 decreased by 76% to \$1.27 million (2005: \$5.2 million). Operating losses were \$11.5 million (2005 loss: \$3.5 million), as a result of the business model shift to online behavioural and contextual advertising through arrangements with global ISP's.

Losses before taxation were \$11.5 million (2005 loss: \$3.5 million). Losses per share were 1.12 cents (2005: 0.47 cents).

The Board is not recommending the payment of a dividend with respect to 2006. It is the Board's intention to pursue a prudent dividend policy, taking into account the Group's business objectives.

### STRATEGY & BUSINESS UPDATE

We announced at the end of 2005 that the Group would focus on its ISP strategy for the financial year ended 31 December 2006. The decision to concentrate management effort and financial resource has enabled 121Media to make significant progress in its talks with global ISP providers, most notably in the UK and the US.

We look forward to updating the market once more formal agreements with ISPs have been set in place.

### PEOPLE

We have continued to invest in our management infrastructure during 2006, in particular building out our global operations, planning and business development presence. Senior appointments in 2006 included David Dorman, Virasb Vahidi, Hugo Drayton and Marc Rothschild. 121Media now has a world-class team on which to build and with whom it will deliver on the ISP opportunity globally

David Dorman, former chairman and chief executive officer of AT&T Corp. joined the company in July 2006 as an advisor. In September the Group was also delighted to welcome Marc Rothschild as senior vice president, Strategic Alliances, and Hugo Drayton, formerly managing director of advertising.com, as CEO of the UK business. The year was completed with the appointment of Virasb Vahidi, a former senior AT&T executive, who joined as group chief operating officer.

The Group is immensely proud to have attracted leading industry executives of such high calibre and, on behalf of the Board, I would like to thank them all for their significant contribution to 121Media's progress during 2006.

### PROSPECTS

Investment in the business has continued during 2006 and we have received tremendous support from our investors for our ongoing programme of strengthening ties with the ISP community and developing our technology.

During 2006 we raised over £5.9m (\$10.2m) (before expenses) via three share placings with UK and US-based institutional investors. These have enabled the Group to continue development of its behavioural advertising platform and its prospects for use amongst global ISPs.

Since the year end, the Group has received significant further endorsement of its strategy, with Morgan Stanley Principal Investments investing £2.56m (\$5m) to strengthen the Company's capital structure and underpin its global development. This development has been very well received by the ISP community and 121Media's other investors.

This is my last statement as Chairman of the Company since I will step from the Board at our forthcoming annual general meeting.

It has been a Chairmanship of which I am immensely proud. The company's growth and evolution from its IPO in 2004, to where it is now, with the opportunity of being a potential significant force in the next phase of revenues for ISPs has been impressive, well managed and inspiring.

# **121MEDIA, INC.**

## **CHAIRMAN'S STATEMENT**

**YEAR ENDED 31 DECEMBER 2006**

---

I have greatly enjoyed my time working in such a forward-looking company within such a dynamic Industry. I hand the reins over to Kent and his extremely capable team and look forward to watching the Group's progress over the coming years, which I am sure will see it well placed to capture the heart of the global digital advertising space.

**David Svendsen**  
**Chairman**  
**23 April 2007**

# **121MEDIA, INC.**

## **CHIEF EXECUTIVE OFFICER'S REPORT**

**YEAR ENDED 31 DECEMBER 2006**

---

The Company continues to strengthen its relationships with global ISPs in order to reach agreements to deploy the Company's innovative behavioural advertising technology platform. The Company is pleased to report its platform is in the final stage of evaluation by numerous major global ISPs. This significant development advances our objective of playing a major role in reshaping ISP revenue models.

It has been a year of significant progress on the technology front. The Company has built on its existing PageSense platform to create a new server-based architecture called ProxySense. In Q4 of 2006, we conducted a live user trial of PageSense with a UK ISP, and we are about to start a larger trial of ProxySense with a test base of several hundred thousand users.

We have developed the first version of a user interface that connects advertisers, agencies, ad networks and publishers into a global, real-time advertising exchange. We have completed a major development of our ad server system to support the interface and we are trialling the system with partners from all of these sectors and working with them to develop future versions.

In order to facilitate our anticipated growth the Company has continued to build its infrastructure and invest in senior management -- attracting leading industry figures from AT&T and AOL, amongst others.

I would like to thank David Svendsen for his outstanding contribution to the Group ever since its IPO in 2004. We wish him well in his future endeavours. I am looking forward to assuming the responsibilities of chairman and to steering 121Media's expansion and growth.

I would like to pay tribute to all our staff who have helped to build the company to the strong position in which we now find ourselves. We enter 2007 with a high level of excitement and confidence.

**Kent Ertugrul**  
**Chief Executive Officer**

**23 April 2007**

# 121MEDIA, INC.

## DIRECTORS AND OFFICERS

YEAR ENDED 31 DECEMBER 2006

---

### **David Svendsen, Non-executive Chairman**

David Svendsen has over 30 years of business management experience. Until February 2000, David was chairman of Microsoft UK and vice president of Microsoft EMEA (Europe, Middle-East & Africa) and prior to that was managing director of Microsoft UK from 1988 to 1998. Before joining Microsoft UK, he was marketing director of Microsoft Australia, where he oversaw the development of the business from inception in 1984.

### **Kent Ertugrul, Chief Executive Officer**

Kent Ertugrul has been an innovator and entrepreneur in finance and technology for nearly two decades. Kent has led 121Media through its history of tremendous growth, including its successful public offering. Prior to starting 121Media, he founded Life.com, a desktop software and online interactive diary, as well as Voxster, a company enabling Instant Messaging for email, MIGs Etc., and other ventures. Kent oversaw, as director and chief financial officer, the growth of Compass Technology from 5 to 170 employees. As it became a leading PC-based voice mail company in the US, Compass merged in 1991 with Octel, which in turn was later acquired by Lucent Technology. He began his career with positions at JP Morgan, Credit Suisse First Boston and Morgan Stanley in London.

### **David Gwozdz, Director and SVP, Business Development and Sales**

David Gwozdz joined 121Media in August 2005. He has spent 18 years in advertising and was part of the founding team of DoubleClick, the NASDAQ-listed internet advertising solutions corporation recently acquired for \$1.1 billion by Private Equity interests in the US. He devised and implemented DoubleClick's original media sales products and strategies and built, trained and managed multiple industry-leading sales teams in all areas of online advertising, sponsorships, and promotions.

### **Gerard Baz, Non-Executive Director**

Gerard Baz spent 11 years at Microsoft Corporation in Redmond, WA where he held several positions. Most notably, he headed the Microsoft Word program management group for several years with overall responsibility for product design and project management for all versions of Word. Later, he joined the newly created MSN group to be in charge of business development and relations with content providers, before moving to Paris to prepare the European launch of MSN in the major European markets. An 'angel' investor since 1998, he has invested in several European and US based internet and high technology ventures.

# 121MEDIA, INC.

## REPORT OF THE DIRECTORS

YEAR ENDED 31 DECEMBER 2006

---

The Directors present their report and the financial statements of the Group for the year ended 31 December 2006. The company is a Delaware corporation, however as the company's shares are quoted on the Alternative Investment Market in London, the financial statements have been prepared using United Kingdom Generally Accepted Accounting Practice.

### PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The principal activity of the parent company and of the Group during the year was to develop a platform for the delivery and management of targeted, contextual and behavioural online advertising campaigns on behalf of its clients. The Review of Business is included in the Chairman's and CEO's reports.

### PRINCIPAL RISKS AND UNCERTAINTIES

The Directors recognise that within the business there are a number of risks which may affect the performance of the Group. These risks are subjected to regular review and where appropriate processes are established to minimise the level of exposure.

#### *ISP Risk*

The Group's plan to deploy its service utilizing the network of numerous ISPs is wholly dependent on reaching arrangements with such ISPs. There can be no assurance that we will be able to reach satisfactory agreements with said ISPs.

#### *Financial Risks*

The Group's financial instruments comprise cash and other items, including trade debtors and trade creditors that arise directly from its operations. The Group seeks to reduce or eliminate financial risk and to invest cash assets safely and profitably. It operates within policies and procedures approved by the Board, which include strict controls on the use of financial instruments in managing the Group's risk. The Group has transactional currency exposure as it deals in multi-currencies however the Directors do seek to limit this risk as much as possible.

#### *Adequacy of Finance*

The directors have conducted a review of the forecasts for the next 12 months. Having considered future financing possibilities, the directors have a reasonable expectation that the Group has adequate ability to fund its operational existence for the foreseeable future. For this reason, the Directors continue to adopt the going concern basis in preparing the financial statements.

#### *People*

One of the key assets of the Group is the commitment and skill of its staff. The retention of these people is therefore key to the success of the business. The Group monitors closely the satisfaction of its employees and that their remuneration packages match both contribution and the wider employment market. In addition the Group has a share option scheme which allows employees to participate in the success of the Group as a whole.

#### *Technology and market changes*

121Media, Inc. operates at the forefront of the digital advertising technology marketplace. The Directors acknowledge that this is a rapidly evolving environment and the Group monitors closely how changes will impact the Group. During 2006 the Directors made a strategic decision to redirect the focus of the Group towards the ISP marketplace. The Group has needed to expend considerable capital in pursuing its strategy with the global ISP community prior to obtaining any significant revenues from this business.

#### *Competition*

The Group continuously monitors new product offerings into the market place and the Directors believe 121Media's technical team have a strong track record in maintaining competitive advantage.

### RESEARCH AND DEVELOPMENT

Research and development is undertaken on an ongoing basis in order to further develop and enhance the Group's software products.

# 121MEDIA, INC.

## REPORT OF THE DIRECTORS

YEAR ENDED 31 DECEMBER 2006

---

### THE DIRECTORS AND THEIR INTERESTS

The Directors at the end of the year together with their beneficial interests in the shares of the Company were as follows:

	Ordinary Shares of \$0.001 each	
	At 31 December 2006	At 1 January 2006 or later date of appointment
D Svendsen	57,308	18,824
K Ertugrul <sup>1</sup>	2,594,412	1,215,073
G Baz <sup>2</sup>	1,729,161	1,729,161
D Gwozdz	7,700	3,400

<sup>1</sup> Of the 2,594,412 shares, 629,527 are held in the name of Dartley Holdings Inc. a company in which K Ertugrul has a beneficial interest.

<sup>2</sup> These shares are held by Gestrust SA, a trust in which G Baz has a beneficial interest.

In addition T. Bowen served as a Director during the year until he resigned on 8 November 2006.

Details of share options held by the Directors are included in the Directors' Remuneration Report on page 10.

### SUBSTANTIAL SHAREHOLDINGS

As at 31 December 2006 the Company was aware of the following interests in 3% or more of its issued share capital:

Shareholder	Number of Shares	% Holding
Kent Ertugrul	1,964,885	17.52%
Gestrust SA	1,729,161	15.42%
Fidelity Investments Services Limited	1,065,580	9.50%
Societe General Asset Management S.A.	752,843	6.71%
Dartley Holdings	629,527	5.61%
AXA Framlington Limited	629,983	5.62%
Madjedie Asset Management Limited	525,305	4.68%
Valerie Boffy	400,000	3.57%

### EMPLOYEE CONSULTATION

The policy of informing and consulting with employees is maintained by means of regular team briefs, conference calls and meetings. Employees are encouraged to present their views and suggestions in respect of the Group's performance.

### POST BALANCE SHEET EVENTS

During February 2007, 169,808 shares were issued for a consideration (before expenses) of \$5,000,000.

### CREDITOR PAYMENT POLICY

The Group's current policy concerning the payment of trade creditors is to:

- (i) settle the terms of payment with suppliers when agreeing the terms of each transaction.
- (ii) ensure that suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts.
- (iii) pay in accordance with the Group's contractual or other legal obligations.

The average trade creditor days for the year were 18 days (2005: 35 days).

### DISCLOSURE OF INFORMATION TO AUDITORS

Each of the directors has confirmed that there is no information of which they are aware which is relevant to the audit, but of which the auditor is unaware. They have further confirmed that they have taken appropriate steps to identify such relevant information and to establish that the auditors are aware of such information.

# 121MEDIA, INC.

## REPORT OF THE DIRECTORS

YEAR ENDED 31 DECEMBER 2006

---

### AUDITORS

It is proposed that H.W Fisher & Company remain as auditors for a further year.

Registered office:  
2711 Centerville Road  
Suite 400  
City of Wilmington 19808  
County of New Castle  
Delaware  
USA

Signed on behalf of the Directors

K Ertugrul

Chief Executive Officer

Dated: 23 April 2007

# 121MEDIA, INC.

## DIRECTORS' REMUNERATION REPORT

YEAR ENDED 31 DECEMBER 2006

### REMUNERATION COMMITTEE

The Remuneration Committee operates within defined terms of reference. The Remuneration Committee comprises the Non-Executive Directors and is chaired by David Svendsen.

### REMUNERATION POLICY

The policy of the Group is to set levels of remuneration to attract, retain and motivate Executive Directors and key staff. The packages are designed to be competitive in value to those offered to the Directors of similar sized public companies in related sectors.

### NON-EXECUTIVE DIRECTORS

The Board, based on a recommendation by the Non-Executive Chairman or, in the case of the Chairman, the remainder of the Board, determines the remuneration of the Non-Executive Directors. The Non-Executive Directors are not eligible to join the pension scheme.

### SERVICE CONTRACTS

On 1 January 2007 K. Ertugrul went on the company's payroll (prior to such time he was paid as a consultant). D. Gwozdz has a standard 121Media employment contract. The other Directors' services are retained on a consultancy basis.

### SHARE OPTIONS

Director	At start of year	Granted during year	Exercised	Lapsed	At end of year	Exercise price
K Ertugrul	227,092	-	227,092	-	-	\$0.61327
K Ertugrul	227,092	-	227,092	-	-	\$0.61327
K Ertugrul <sup>1</sup>	180,707	-	-	-	180,707	£2.45
K Ertugrul <sup>2</sup>	-	200,000	-	-	200,000	£2.115
K Ertugrul <sup>3</sup>	-	500,000	-	-	500,000	£5.40
D Svendsen <sup>4</sup>	60,236	-	38,484	-	21,752	£2.45
D Gwozdz <sup>4</sup>	75,000	-	-	-	75,000	£1.715
D Gwozdz <sup>5</sup>	50,000	-	-	-	50,000	£1.715
D Gwozdz <sup>2</sup>	-	75,000	-	-	75,000	£2.115
T Bowen <sup>6</sup>	100,000	-	62,500	-	37,500	£1.580

Vesting Criteria:

<sup>1</sup> Conditional on the Group reaching \$3.5M annualized EBITDA on a given quarter showing sustained growth over at least 2 consecutive quarters.

<sup>2</sup> Conditional upon the Group reaching an average of \$3M in monthly net revenue, over a period of 6 consecutive months from date of grant.

<sup>3</sup> Options vest at the rate of 1/5<sup>th</sup> for achieving each incremental increase of £100 in the share price from £100 up to £500 per share.

<sup>4</sup> Options vest at the rate of 1/36th per month for total of 36 months from date of grant.

<sup>5</sup> 25,000 vest conditional on revenue being greater than \$1.5m for 2 months and the balance after revenue is greater than \$3.0m per month for 2 months

<sup>6</sup> Options vest 30,000 upon grant, 20,000 6 months later, remaining 50,000 at the rate of 2,500 per month for 20 months.

The mid market price at the close of business on 31 December 2006 was 1,092.5p and the high and low share prices during the year were 1,480p and 137.5p respectively.

### DIRECTORS REMUNERATION

Director	Salary \$'000	Consultancy \$'000	Benefits \$'000	Total 2006 \$'000	Total 2005 \$'000
D Svendsen	-	47	-	47	45
K Ertugrul	-	308	35	343	305
T Bowen <sup>1</sup>	-	133	-	133	11
D Gwozdz	205	-	7	212	18
G Baz	-	29	-	29	28

<sup>1</sup> The remuneration for T Bowen is for the full year and includes amounts paid subsequent to his resignation as a Director.

# 121MEDIA, INC.

## CORPORATE GOVERNANCE REPORT

YEAR ENDED 31 DECEMBER 2006

---

The Group is committed to applying the highest principles of corporate governance commensurate with its size. The Board confirms that the Group has voluntarily complied with the provisions set out in Section 1 of the Combined Code on Corporate Governance ("Combined Code") published by the Financial Reporting Council in the United Kingdom in July 2003, with certain exceptions where the Board considers the provisions not to be appropriate for the Group at the present time, given the small size of the board. The exceptions include:

- Code provision B.2.1, which requires the Remuneration Committee be comprised of independent Non-Executive Directors
- Code provision C.3.1, whereby the Audit Committee comprises two Non-Executives rather than three as recommended.
- Code provision A.3.2, and A.3.3 whereby, the Group has not identified a senior independent Non-Executive Director.

Given the current size and scope of the operations of the Group, the full Board has assumed those responsibilities that are ordinarily assigned to a Nomination Committee.

### INTERNAL CONTROLS

The Company has voluntarily complied with the Combined Code provisions on internal control having established the procedures necessary to implement the guidance issued in July 2003 and by reporting in accordance with that guidance.

The Board takes overall responsibility for establishing and maintaining reliable systems of control in all areas of the Group's operations. These systems of control, especially of financial control, are designed to manage rather than eliminate the risk of failure to achieve business objectives. In pursuing these objectives, internal controls can only provide reasonable and not absolute, assurance against the occurrence of material loss or misstatement.

The Board's policy has been determined by reference to:

- (a) 'Combined Code': the principles of good governance and code of best practice prepared by the Committee on Corporate Governance, issued in July 2003.
- (b) 'Internal Control': Guidance for Directors on the Combined Code (the "Turnbull Guidance")

Throughout the year, and up to the date of this report, the Board has applied various processes for identifying, evaluating and managing the risks faced by the Group.

The key features of the system of internal control are set out below:

- 121Media, Inc. has established an operational management structure with clearly defined responsibilities and regular performance reviews
- The Group operates a financial reporting system, where actual results are monitored against budgets, forecasts and other performance indicators with action dictated accordingly at least monthly
- A structured approval process based on assessment of risk and value delivered
- Sufficient resource is focused to maintain and develop internal control procedures and information systems, especially in financial management
- The Group has an ongoing process for identifying, evaluating and managing the significant risks that it faces
- During the year the Board considers reports from management and external audit on the system of internal control and any material control weaknesses and discusses with management the actions taken on problem areas identified by the Board members and the auditors

The Board considers that there have been no substantial weaknesses in internal financial controls that have resulted in any material losses, contingencies or uncertainties, which need to be disclosed in the accounts. The Board has considered the need for an internal audit function and concluded that there is no current need for such a function within the Group. The Board confirms that there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Group, and that this process has been in place for the year under review and up to the date of approval of the Annual Report and Accounts. This process is regularly reviewed by the Board and is consistent with the Turnbull Guidance.

# **121MEDIA, INC.**

## **CORPORATE GOVERNANCE REPORT**

**YEAR ENDED 31 DECEMBER 2006**

---

### **ACCOUNTING POLICIES**

The Board considers the appropriateness of its accounting policies on an annual basis and in respect of research and development, bi-annually. The Board believes that its accounting policies and estimation techniques are appropriate in particular in relation to income recognition and research and development.

### **BOARD OF DIRECTORS**

The Board, comprising two Executive Directors, a Non-Executive Chairman and a further Non-Executive Director, is responsible for the overall strategy and direction of 121Media, Inc. as well as for approving potential acquisitions, major capital expenditure items and financing matters. The Board has a formal schedule of business reserved to it and meets regularly during the year. The Board is supplied in a timely manner with information in a form and of a suitable quality appropriate to enable it to discharge its duties. Advice from independent sources is available if required. The Board monitors exposure to key business risks and reviews the strategic direction of the Group, the annual budgets as well as their progress against those budgets.

The Board members and their roles are described on page 6.

### **SHAREHOLDER RELATIONS**

121Media, Inc is committed to open communication with all its shareholders. The Directors hold periodical meetings with institutional shareholders to discuss and review the Group's activities and objectives. Communication with private shareholders is principally through the Annual General Meeting, where participation is encouraged and where the Board is available to answer questions.

Every shareholder is sent a full annual report each year-end and at the half-year they are sent an interim report. Care is taken to ensure that any price sensitive information is released to all shareholders, institutional and private, at the same time in accordance with London Stock Exchange requirements.

121Media, Inc strives to give a full, timely and realistic assessment of its business in a balanced way, in all price-sensitive reports and presentations.

### **AUDIT COMMITTEE**

The Audit Committee is formally constituted with terms of reference. The Committee is chaired by David Svendsen who is the Non-Executive Chairman, and the other member Gerard Baz who is a Non-Executive Director of the Group. The Committee meets at least once a year and receives reports from the Group's auditors. The Committee also reviews the interim and final accounts prior to approval by the Board. Additionally the Committee also ensures the independence and objectivity of the external auditors and also reviews the provision of non-audit services by external auditors.

### **GOING CONCERN**

The Directors have reviewed the Group's budget and cash flows for 2007 and the medium term plan, produced to the year 2008 and have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Directors continue to prepare the accounts on a going concern basis.

# 121MEDIA, INC.

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

---

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

The rules of the Alternative Investment Market require the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the group and of the company and of the profit or loss of the group for that period. The directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice

In preparing these financial statements, the directors are required to:

- \* select suitable accounting policies and then apply them consistently;
- \* make judgements and estimates that are reasonable and prudent;
- \* state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the accounts;
- \* prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the group and of the company and to enable them to ensure that the financial statements comply with United Kingdom Generally Accepted Accounting Practice. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are also responsible for ensuring that the Annual Report includes information required by the AIM Market Rules.

United Kingdom Generally Accepted Accounting Practice which governs the preparation and the dissemination of the financial statements and other information included in annual reports may differ from the requirements in other jurisdictions.

# 121MEDIA, INC.

## INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS

YEAR ENDED 31 DECEMBER 2006

---

We have audited the financial statements of 121Media, Inc for the year ended 31 December 2006 set out on pages 15 to 34. These financial statements have been prepared under the accounting policies set out on pages 20 and 21.

This report is made solely to the company's members, as a body. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The directors' responsibilities for preparing the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice are as described on page 13.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice. We also report to you whether, in our opinion, the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited group financial statements. The other information comprises only, the Chairman's Statement, the Report of the Chief Executive Officer, the Report of the Directors, the Directors' Remuneration Report, the Corporate Governance Report and the Statement of Directors' Responsibilities. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the group financial statements. Our responsibilities do not extend to any other information.

### BASIS OF AUDIT OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

### OPINION

In our opinion:

- The financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the affairs of the group and the company as at 31 December 2006 and of the group's loss for the year then ended.
- The information given in the Directors' Report is consistent with the financial statements.

### H W Fisher & Company

Chartered Accountants  
Registered Auditor  
Acre House  
11-15 William Road  
London  
NW1 3ER  
United Kingdom  
Dated: 23 April 2007

# 121MEDIA, INC.

## GROUP PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 31 DECEMBER 2006

---

	Notes	2006 \$	2005 (As restated) \$
<b>Turnover</b>	2	1,272,254	5,207,136
Cost of Sales		(403,306)	(2,171,486)
<b>Gross Profit</b>		<b>868,948</b>	<b>3,035,650</b>
Sales and Administrative Expenses			
- General		(10,498,913)	(6,352,667)
- Share Based Payments		(1,906,674)	(195,848)
<b>Operating Loss</b>	3	<b>(11,536,639)</b>	<b>(3,512,865)</b>
Other Income	6	82,312	15,695
Interest Payable and Similar Charges	7	(16,186)	(27,962)
<b>Loss on Ordinary Activities Before Taxation</b>		<b>(11,470,513)</b>	<b>(3,525,132)</b>
Taxation on Loss on Ordinary Activities	8	(12,705)	-
<b>Loss on Ordinary Activities After Taxation</b>		<b>(11,483,218)</b>	<b>(3,525,132)</b>
<b>Standard / Diluted Loss per Share - Basic</b>	11	<b>(1.12)</b>	<b>(0.47)</b>

All activities of the Group are classed as continuing.

# 121MEDIA, INC.

## STATEMENT OF TOTAL RECOGNIZED GAINS AND LOSSES

FOR THE YEAR ENDED 31 DECEMBER 2006

---

	Notes	2006 \$	2005 \$
Loss for the financial year		<b>(11,483,218)</b>	<b>(3,525,132)</b>
Share option charge taken to option reserve		1,254,065	203,299
Currency translation difference on foreign currency net investments		(106,675)	(174,221)
Total recognized gains and losses relating to the year		<b>(10,335,828)</b>	<b>(3,496,054)</b>
Prior year adjustments	9	(29,050)	
Total gains and losses recognized since last annual report		<b>(10,364,878)</b>	

# 121MEDIA, INC.

## GROUP BALANCE SHEET

AS AT 31 DECEMBER 2006

---

		2006	2005
	Notes	\$	(As restated) \$
<b>Fixed Assets</b>			
Intangible assets	12	48,827	-
Tangible assets	13	384,857	504,803
		<u>433,684</u>	<u>504,803</u>
<b>Current Assets</b>			
Debtors	15	594,063	1,975,086
Cash at bank and in hand		3,804,771	570,533
		<u>4,398,834</u>	<u>2,545,619</u>
<b>Creditors: Amounts Falling Due Within One Year</b>	16	(1,495,420)	(1,002,472)
<b>Net Current Assets</b>		<u>2,903,414</u>	<u>1,543,147</u>
<b>Total Assets Less Current Liabilities</b>		<b>3,337,098</b>	<b>2,047,950</b>
<b>Creditors: Amounts Falling Due After One Year</b>	17	(11,303)	(76,714)
<b>Net Assets</b>		<u>3,325,795</u>	<u>1,971,236</u>
<b>Capital and Reserves</b>			
Called Up Share Capital	19	11,217	8,190
Share Premium Account	20	18,706,233	6,734,601
Other Reserves	20	1,128,838	663,576
Profit and Loss Account	20	(16,520,493)	(5,435,131)
<b>Shareholders' Funds</b>		<u>3,325,795</u>	<u>1,971,236</u>

The financial statements were approved by the Directors on 23 April 2007 and are signed on their behalf by:

**David Svendsen**  
Chairman

# 121MEDIA, INC.

## COMPANY BALANCE SHEET

AS AT 31 DECEMBER 2006

---

		2006	2005
	Notes	\$	(As restated) \$
<b>Fixed Assets</b>			
Intangible assets	12	48,827	-
Tangible Assets	13	384,857	498,483
Investments	14	186	186
		<u>433,870</u>	<u>498,669</u>
<b>Current Assets</b>			
Debtors	15	2,905,287	4,555,067
Cash at bank and in hand		3,804,771	271,363
		6,710,058	4,826,430
<b>Creditors: Amounts Falling Due Within One Year</b>	16	<u>(1,495,420)</u>	<u>(955,263)</u>
<b>Net Current Assets</b>		<u>5,214,638</u>	<u>3,871,167</u>
<b>Total Assets Less Current Liabilities</b>		<b>5,648,508</b>	<b>4,369,836</b>
<b>Creditors: Amounts Falling Due After One Year</b>	17	<u>(11,303)</u>	<u>(76,714)</u>
<b>Net Assets</b>		<u><u>5,637,205</u></u>	<u><u>4,293,122</u></u>
<b>Capital and Reserves</b>			
Called Up Share Capital	19	11,217	8,190
Share Premium Account	20	18,706,233	6,734,601
Other Reserves	20	1,409,734	837,797
Profit and Loss Account	20	(14,489,979)	(3,287,466)
<b>Shareholders' Funds</b>		<u><u>5,637,205</u></u>	<u><u>4,293,122</u></u>

The financial statements were approved by the Directors on 23 April 2007 and are signed on their behalf by:

**David Svendsen**  
Chairman

# 121MEDIA, INC.

## GROUP CASH FLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2006

---

		2006	2005
	Notes	\$	(As restated) \$
<b>Net Cash Outflow from Operating Activities</b>	25	<b>(7,898,599)</b>	<b>(1,821,605)</b>
Returns on Investments and Servicing of Finance	26	66,126	(12,267)
Taxation	26	(12,705)	-
Capital Expenditure and Financial Investment	26	(566,211)	(288,321)
<b>Net Cash Outflow Before Financing</b>		<b>(8,411,389)</b>	<b>(2,122,193)</b>
<b>Financing</b>	26	11,645,627	1,814,399
<b>Increase / (Decrease) in Cash in the Period</b>	28	<b>3,234,238</b>	<b>(307,794)</b>

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

---

### 1. ACCOUNTING POLICIES

#### Accounting convention

The financial statements have been prepared under the historical cost convention, on a going concern basis, and in accordance with applicable accounting standards.

#### Basis of going concern

The directors have reviewed the Group's forecasts for the next 12 months and the medium term plan, produced to 2008. They have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, the directors are of the opinion it is appropriate to continue preparing the accounts on a going concern basis.

#### Basis of consolidation

The Group financial statements consolidate the financial statements of 121Media, Inc and its subsidiary undertaking drawn up to 31 December 2006. Intra-group sales and profits are eliminated fully on consolidation.

#### Turnover

Turnover represents amounts receivable for services net of VAT and trade discounts.

#### Research and development

Certain expenditure on software development is capitalised in the year in which it is incurred, if the directors are satisfied as to the technical, commercial and financial viability of the projects. Other research and development expenditure is written off as incurred.

#### Tangible fixed assets

All tangible fixed assets are initially recorded at cost, and then stated at cost less depreciation.

#### Depreciation

Depreciation is calculated so as to write off the cost of an asset, less its estimated residual value, over the useful economic life of that asset as follows:

Computer hardware & machinery	- 50% on cost
Fixtures and fittings	- 33% on cost
Software development costs	- 50% on cost

#### Intangible fixed assets

Acquired intangible fixed assets are initially recorded at cost and amortised over its estimated useful economic life of 3 years.

#### Fixed asset investments

Fixed assets investments are stated at cost less provision for permanent diminution in value.

#### Leasing and hire purchase commitments

Assets held under finance leases and hire purchase contracts are treated as if they had been purchased outright at the present value of the rentals payable, less finance charges, over the primary period of the agreements. The corresponding obligations under these agreements are included in creditors. The finance element of the rentals payable is charged to the profit and loss account so as to produce a constant rate of charge on the outstanding balance in each period.

Rentals applicable to operating leases where substantially all of the benefits and risks of ownership remain with the lessor are charged against profits on a straight-line basis over the period of the lease.

#### Pension costs

The Group operates a defined contribution scheme. Contributions payable for the year are charged in the profit and loss account.

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

---

### ACCOUNTING POLICIES *(Continued)*

#### Share based payments

The group issues equity-settled share-based payments to certain employees and has applied Financial Reporting Standard No. 20 (IFRS2) 'Share-based payments' for the first time.

The cost of employee share-based compensation awards is recognised as an expense. The total amount to be expensed rateably over the vesting period is determined by reference to the fair value of the options determined at the grant date, excluding the impact of non-market vesting conditions (for example, profitability and sales targets). Non-market vesting conditions are included in the assumptions about the number of options that will eventually vest. This estimate is revised at each reporting date and an adjustment is made to the profit and loss account. Fair value is measured by using the Black-Scholes pricing model, except for options with market based vesting conditions, where a binomial model is used.

As per the transitional provisions, the group has applied FRS 20 only to those options granted after 7 November 2002 and that had not yet vested at 1 January 2006.

#### Employer's taxes on share options

Employers' national insurance contributions in the UK, are calculated using the market value of the company's shares at the reporting date, and pro-rated over the vesting period of the options.

#### Deferred taxation

Deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the accounts. Deferred tax is not provided on timing differences arising from the revaluation of fixed assets where there is no commitment to sell the assets. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

#### Foreign currencies

Monetary assets and liabilities in foreign currencies are translated into US dollars at the closing rates of exchange ruling at the balance sheet date. Transactions in foreign currencies are translated into US dollar at the rate of exchange ruling at the date of the transaction. All differences are taken to the profit and loss account.

#### Subsidiary Company

The assets and liabilities of the overseas subsidiary are translated from sterling to US dollar at the rate of exchange ruling at the balance sheet date. Profits and losses of the overseas subsidiary are translated at the monthly average exchange rates during the year. Gains and losses arising on the translation of the net assets of the overseas subsidiary are taken to reserves.

#### Functional currency

The financial statements have been prepared in US dollars as the majority of the Group's trade occurs in this currency.

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 2. TURNOVER

The turnover and loss before tax are attributable to the one principal activity of the Group.

The geographical analysis of turnover is given below:

	<b>2006</b>	2005
	<b>\$</b>	<b>\$</b>
North America	995,184	4,073,132
Europe	277,070	1,134,004
	<u>1,272,254</u>	<u>5,207,136</u>

During 2006 the Directors made a strategic decision to cease the sale and marketing of the desktop software business (Pagesense Desktop), and focus the company's resources on the online behavioural and contextual advertising market through arrangements with global ISPs.

### 3. OPERATING LOSS

Operating loss is stated after charging/(crediting):

	<b>2006</b>	2005
	<b>\$</b>	<b>\$</b>
Research and development expenditure written off	135,239	488,017
Operating lease rentals		
- Other assets	152,070	-
Share Based Payments		
- Charge under FRS 20	1,254,065	203,299
- Employer's NIC	652,609	(7,451)
Depreciation of owned fixed assets	543,106	522,609
Depreciation of tangible fixed assets held under finance lease and hire purchase contracts	50,000	37,500
Auditors' remuneration		
- As auditor	46,400	10,000
- For other services	62,669	13,356
Net loss/(profit) on foreign currency translation	169,860	4,665

### 4. PARTICULARS OF EMPLOYEES

The average number of staff employed by the Group during the financial year amounted to:

	<b>2006</b>	2005
	<b>No.</b>	<b>No.</b>
Number of administrative staff	20	2
Sales	16	18
	<u>36</u>	<u>20</u>

The aggregate payroll costs of the above were:

	<b>2006</b>	2005
	<b>\$</b>	<b>\$</b>
Wages and salaries	5,335,737	2,500,570
Social security costs	869,288	243,592
Other pension costs	16,852	21,127
	<u>6,221,877</u>	<u>2,765,289</u>

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 5. DIRECTORS' EMOLUMENT

The Directors' aggregate emoluments in respect of qualifying services were:

	2006 \$	2005 \$
Emoluments receivable	763,981	606,162

During the year the directors made a notional gain of \$8,617,597 (2005: \$nil) on the exercise of options held by them.

#### Emoluments of highest paid director:

	2006 \$	2005 \$
Total emoluments (excluding pension contributions)	343,320	305,356

### 6. OTHER INCOME

	2006 \$	2005 \$
Interest receivable and similar income	82,312	15,695
	<u>82,312</u>	<u>15,695</u>

### 7. INTEREST PAYABLE AND SIMILAR CHARGES

	2006 \$	2005 \$
Interest payable on:		
Finance lease and hire purchase contracts	16,186	15,000
Other loans	-	12,962
	<u>16,186</u>	<u>27,962</u>

### 8. TAXATION ON ORDINARY ACTIVITIES

	2006 \$	2006 \$	2005 \$	2005 \$
Current tax:				
Delaware state tax	12,705		-	
Total current tax		<u>12,705</u>		<u>-</u>
<b>Factors affecting the tax charge for the period</b>				
Loss on ordinary activities before taxation		<u>(11,470,513)</u>		<u>(3,525,132)</u>
Profit on ordinary activities before taxation multiplied by standard rate of UK corporation tax of 30% (2005: 30%)		(3,441,154)		(1,057,540)
Effects of:				
Expenses not deductible for tax purposes		26,810		78,090
Capital allowances for the period in excess of depreciation		70,465		97,299
Other tax adjustments		12,705		-
Movement on tax losses		3,343,879		882,151
<b>Current Tax charge</b>		<u>12,705</u>		<u>-</u>

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

---

### 9. PRIOR YEAR ADJUSTMENT

The group issues equity-settled share-based payments to certain employees and has applied Financial Reporting Standard No. 20 (IFRS2) 'Share-based payments' for the first time (see note 22). As a result the comparative figures were restated, resulting in an increase in the loss for the year ended 31 December 2005 by \$191,533, comprising the FRS 20 charge of \$203,299, employers' NIC of \$(7,451) and gain on foreign currency translation of \$(4,315). The deficit in the Profit and Loss Reserve increased by \$282,275, with a corresponding increase in employers' NIC accrual of \$29,050 and an increase of \$253,225 in the option reserve.

### 10. LOSS ATTRIBUTABLE TO MEMBERS OF THE PARENT COMPANY

The loss dealt with in the accounts of the parent company was \$11,600,369 (2005: loss of \$1,816,310).

### 11. LOSS PER SHARE

The calculation of the basic loss per share and diluted loss per share is based on the loss attributable to ordinary shareholders of \$11,483,218 (2005: \$3,525,132) divided by the weighted average number of shares in issue during the year.

The weighted average numbers of shares used in the calculation are set out below: -

**Year Ended 31 December 2006**  
**Number of Shares**  
10,257,408

**Year Ended 31 December 2005**  
**Number of Shares**  
7,491,507

### 12. INTANGIBLE FIXED ASSETS

<b>Group and company</b>	<b>Website</b> <b>\$</b>
<b>COST</b>	
Additions	50,222
<b>At 31 December 2006</b>	<u>50,222</u>
<b>AMORTISATION</b>	
Charge for the year	1,395
<b>At 31 December 2006</b>	<u>1,395</u>
<b>NET BOOK VALUE</b>	
<b>At 31 December 2006</b>	<u>48,827</u>

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 13. TANGIBLE FIXED ASSETS

Group	Computer Hardware & Machinery \$	Fixtures & Fittings \$	Software Development \$	Total \$
<b>COST</b>				
At 1 January 2006	500,776	13,720	787,705	1,302,201
Additions	105,747	68,823	341,419	515,989
Disposals	(39,710)	(14,146)	-	(53,856)
<b>At 31 December 2006</b>	<b>566,813</b>	<b>68,397</b>	<b>1,129,124</b>	<b>1,764,334</b>
<b>DEPRECIATION</b>				
At 1 January 2006	331,728	2,854	462,816	797,398
Charge for the year	158,509	24,532	410,065	593,106
On disposal	(7,810)	(3,217)	-	(11,027)
<b>At 31 December 2006</b>	<b>482,427</b>	<b>24,169</b>	<b>872,881</b>	<b>1,379,477</b>
<b>NET BOOK VALUE</b>				
<b>At 31 December 2006</b>	<b>84,386</b>	<b>44,228</b>	<b>256,243</b>	<b>384,857</b>
At 31 December 2005	169,048	10,866	324,889	504,803

#### Finance Leases and Hire Purchase Contracts

The net book value of tangible fixed assets includes an amount of \$12,500 (2005: \$62,500) in respect of assets held under finance lease or hire purchase contracts.

Company	Computer Hardware & Machinery \$	Fixtures & Fittings \$	Software Development \$	Total \$
<b>COST</b>				
At 1 January 2006	494,060	8,269	787,705	1,290,034
Transfer from subsidiary	6,716	5,451	-	12,167
Additions	105,747	68,823	341,419	515,989
Disposals	(39,710)	(14,146)	-	(53,856)
<b>At 31 December 2006</b>	<b>566,813</b>	<b>68,397</b>	<b>1,129,124</b>	<b>1,764,334</b>
<b>DEPRECIATION</b>				
At 1 January 2006	328,505	230	462,816	791,551
Transfer from subsidiary	3,223	2,624	-	5,847
Charge for the year	158,509	24,532	410,065	593,106
On disposal	(7,810)	(3,217)	-	(11,027)
<b>At 31 December 2006</b>	<b>482,427</b>	<b>24,169</b>	<b>872,881</b>	<b>1,379,477</b>
<b>NET BOOK VALUE</b>				
<b>At 31 December 2006</b>	<b>84,386</b>	<b>44,228</b>	<b>256,243</b>	<b>384,857</b>
At 31 December 2005	165,555	8,039	324,889	498,483

#### Finance Leases and Hire Purchase Contracts

The net book value of tangible fixed assets includes an amount of \$12,500 (2005: \$62,500) in respect of assets held under finance lease or hire purchase contracts.

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 14. FIXED ASSET INVESTMENTS

#### Company

<b>Subsidiary undertakings</b>	<b>\$</b>
<b>COST</b>	
At 1 January 2006 and 31 December 2006	186
<b>NET BOOK VALUE</b>	
At 31 December 2006	186
At 31 December 2005	186

	Country of incorporation	Holding	Proportion of voting rights and shares held	Nature of business
Held by the Company: 121Media (Europe) Limited	England	Ordinary shares	100%	Behavioural and contextual online advertising
Held by 121Media (Europe) Limited: 121Media (UK) Limited	England	Ordinary shares	100%	Dormant

### 15. DEBTORS

	Group		Company	
	2006	2005	2006	2005
	\$	\$	\$	\$
Trade debtors	-	1,639,899	-	-
Amounts owed by Group undertakings	-	-	2,311,224	4,270,708
VAT recoverable	211,397	31,521	211,397	26,054
Other debtors	265,628	289,828	265,628	244,467
Prepayments and accrued income	117,038	13,838	117,038	13,838
	<u>594,063</u>	<u>1,975,086</u>	<u>2,905,287</u>	<u>4,555,067</u>

### 16. CREDITORS: Amounts falling due within one year

	Group		Company	
	2006	2005	2006	2005
	\$	\$	\$	\$
Net obligations under finance leases and hire purchase contracts	39,077	18,426	39,077	18,426
Trade creditors	156,736	383,377	156,736	376,001
Other taxation and social security costs	55,956	56,205	55,956	16,372
Other creditors	11,445	-	11,445	-
Accruals and deferred income	1,232,206	544,464	1,232,206	544,464
	<u>1,495,420</u>	<u>1,002,472</u>	<u>1,495,420</u>	<u>955,263</u>

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 17. CREDITORS: Amounts falling due after one year

	<b>Group</b>		<b>Company</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
Net obligations under finance leases and hire purchase contracts	11,303	76,714	11,303	76,714
<b>Net obligations under finance leases and hire purchase contracts</b>				
Repayable within one year	39,077	18,426	39,077	18,426
Repayable between one and five years	11,303	76,714	11,303	76,714
	50,380	95,140	50,380	95,140
Included in liabilities falling due within one year	(39,077)	(18,426)	(39,077)	(18,426)
	11,303	76,714	11,303	76,714

### 18. PROVISIONS FOR LIABILITIES AND CHARGES

Deferred tax is calculated at 30% (2005: 30%) analysed over the following timing differences:

#### Group

	<b>2006</b>	<b>2005</b>
	<b>\$</b>	<b>\$</b>
Accelerated capital allowances	(57,000)	17,000
Short term timing differences	19,000	-
Tax losses available	(4,917,000)	(1,525,000)
	(4,955,000)	(1,508,000)
Unrecognised deferred tax asset	4,955,000	(1,508,000)
	-	-

Deferred tax assets of \$4,955,000 (2005: \$1,508,000) have not been recognised in these accounts because there is insufficient certainty over their recoverability.

#### Company

	<b>2006</b>	<b>2005</b>
	<b>\$</b>	<b>\$</b>
Accelerated capital allowances	(57,000)	17,000
Short term timing differences	19,000	-
Tax losses available	(4,272,000)	(893,000)
	(4,310,000)	876,000
Unrecognised deferred tax asset	4,310,000	876,000
	-	-

Deferred tax assets of \$4,310,000 (2005: \$876,000) have not been recognised in these accounts because there is insufficient certainty over their recoverability.

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 19. SHARE CAPITAL

#### Authorised share capital:

	2006 \$	2005 \$
13,000,000 Common shares of \$0.001 each	<u>13,000</u>	<u>13,000</u>

#### Allotted, called up and fully paid:

	2006 No	\$	2005 No	\$
Common shares of \$0.001 each	<u>11,216,642</u>	<u>11,217</u>	<u>8,190,110</u>	<u>8,190</u>

The following fully paid shares were issued during the period at the consideration shown below: -

6 Feb 2006	1,600,000 placement on AIM for a consideration of £2,400,000
26 Apr 2006	30,000 on the exercise of options granted 01/12/05 at £1.58
26 Apr 2006	8,000 on the exercise of options granted 01/06/04 at \$1.3871
26 Apr 2006	11,817 on the exercise of warrants granted 31/05/04 at £nil
9 Jun 2006	5,000 on the exercise of options granted 03/10/05 at £2.465
9 Jun 2006	10,000 on the exercise of options granted 28/02/05 at £2.465
9 Jun 2006	2,500 on the exercise of options granted 27/04/05 at £2.465
9 Jun 2006	3,100 on the exercise of options granted 01/06/04 at \$1.3871
9 Jun 2006	17,384 on the exercise of warrants granted 19/10/04 at £2.45
19 Jul 2006	88,000 on the exercise of warrants granted 01/08/02 at £nil
19 Jul 2006	207,628 on the exercise of warrants granted 31/08/04 at £nil
19 Jul 2006	227,092 on the exercise of options granted 31/08/03 at \$0.61327
19 Jul 2006	227,092 on the exercise of options granted 31/08/03 at \$0.61327
19 Jul 2006	25,000 on the exercise of options granted 01/12/05 at £1.58
19 Jul 2006	13,836 on the exercise of options granted 31/08/04 at \$1.3871
19 Jul 2006	6,250 on the exercise of options granted 27/04/05 at £2.465
19 Jul 2006	5,000 on the exercise of options granted 01/06/04 at \$1.3871
19 Jul 2006	5,000 on the exercise of options granted 01/06/04 at \$1.3871
19 Jul 2006	10,000 on the exercise of options granted 01/06/04 at \$1.3871
19 Jul 2006	18,023 on the exercise of options granted 01/06/04 at \$1.3871
19 Jul 2006	650 on the exercise of options granted 02/11/05 at £1.705
19 Jul 2006	500 on the exercise of options granted 02/11/05 at £1.705
27 Jul 2006	2,500 on the exercise of options granted 01/06/04 at \$1.3871
27 Jul 2006	15,000 on the exercise of options granted 01/06/04 at \$1.3871
27 Jul 2006	4,500 on the exercise of options granted 01/06/04 at \$1.3871
27 Jul 2006	22,222 on the exercise of options granted 05/09/04 at \$2.84415
17 Aug 2006	14,675 on the exercise of warrants granted 31/08/03 at £nil
28 Sep 2006	175,054 placement on AIM for a consideration of £1,999,992
26 Sep 2006	6,131 on the exercise of warrants granted 01/08/02 at £nil
26 Sep 2006	2,500 on the exercise of warrants granted 31/01/04 at £nil
26 Sep 2006	13,852 on the exercise of warrants granted 19/10/04 at £2.45
16 Nov 2006	2,500 on the exercise of options granted 03/10/05 at £1.715
16 Nov 2006	6,245 on the exercise of options granted 01/06/04 at \$1.3871
16 Nov 2006	5,833 on the exercise of options granted 27/04/05 at £1.54
16 Nov 2006	5,500 on the exercise of options granted 28/02/06 at £1.54
16 Nov 2006	1,400 on the exercise of options granted 28/02/06 at £1.54
16 Nov 2006	1,111 on the exercise of options granted 28/02/06 at £1.54
16 Nov 2006	1,190 on the exercise of options granted 28/02/06 at £2.465
16 Nov 2006	1,667 on the exercise of options granted 27/04/06 at £3.00
16 Nov 2006	4,138 on the exercise of options granted 01/06/04 at \$1.3871
16 Nov 2006	38,484 on the exercise of options granted 23/12/04 at £2.45
16 Nov 2006	3,889 on the exercise of options granted 23/03/06 at £2.065
16 Nov 2006	7,500 on the exercise of options granted 01/12/05 at £1.58
16 Nov 2006	3,200 on the exercise of options granted 02/11/05 at £1.705
16 Nov 2006	7,449 on the exercise of warrants granted 19/10/04 at £2.45
16 Nov 2006	10,000 on the exercise of warrants granted 19/10/04 at £2.45
16 Nov 2006	2,725 on the exercise of warrants granted 19/10/04 at £2.45
16 Nov 2006	8,995 on the exercise of warrants granted 19/10/04 at £2.45
6 Dec 2006	136,400 placement on AIM for a consideration of £1,500,400

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 20. RESERVES

Group	Share premium account \$	Warrants \$	Foreign exchange reserve \$	Option Reserve \$	Profit and loss account \$
Balance brought forward as previously stated	6,734,601	584,572	(174,221)	-	(5,152,856)
Prior year adjustment	-	-	-	253,225	(282,275)
Balance brought forward as restated	6,734,601	584,572	(174,221)	253,225	(5,435,131)
Movement for the year	-	-	-	1,254,065	(11,483,218)
New equity share capital subscribed	11,687,360	-	-	-	-
Currency translation differences on foreign currency net investments	-	-	(106,675)	-	-
Transfers of exercised warrants and options	284,272	(284,272)	-	(397,856)	397,856
<b>Balance carried forward</b>	<b>18,706,233</b>	<b>300,300</b>	<b>(280,896)</b>	<b>1,109,434</b>	<b>(16,520,493)</b>

Company	Share premium account \$	Warrants \$	Option Reserve \$	Profit and loss account \$
Balance brought forward as previously stated	6,734,601	584,572	-	(3,005,191)
Prior year adjustment	-	-	253,225	(282,275)
Balance brought forward as restated	6,734,601	584,572	253,225	(3,287,466)
Movement for the year	-	-	1,254,065	(11,600,369)
New equity share capital subscribed	11,687,360	-	-	-
Transfer of exercised warrants and options	284,272	(284,272)	(397,856)	397,856
<b>Balance carried forward</b>	<b>18,706,233</b>	<b>300,300</b>	<b>1,109,434</b>	<b>(14,489,979)</b>

### 21. WARRANTS

31,473 (2005: 422,629) warrants remain outstanding at the balance sheet date.

The majority of the warrants lapse 5 years from the date of grant.

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 22. SHARE BASED PAYMENTS

The group has a share scheme whereby options over the common shares of the company are granted to employees, consultants and directors. Options are granted at the mid market price on close of the day of grant and must be exercised within 10 years of grant unless the employment is terminated in which case options generally must be exercised within 90 days of termination.

The reconciliation of option movements during the year ended 31 December 2006 is shown below:

	Number	2006 Weighted average exercise price £	Number	2005 Weighted average exercise price £
Outstanding at 1 January 2006	1,825,801	£1.26	1,901,663	£1.02
Granted during the year	1,756,000	£4.99	587,500	£1.94
Lapsed	(325,639)	£3.66	(524,878)	£1.19
Exercised	(723,922)	£0.74	(138,484)	£0.48
Outstanding at 31 December 2006	2,532,240	£3.68	1,825,801	£1.26
Exercisable at 31 December 2006	519,012	£1.38	378,090	£1.10

The following options over ordinary shares were in existence at 31 December 2006:

Range of exercise Price £	Number	2006 Weighted average exercise price £	2006 Weighted average remaining life (years)	Number	2005 Weighted average exercise price £	2005 Weighted average remaining life (years)
£0.01 - £2.49	1,591,546	1.65	8.58	1,825,801	1.26	8.70
£2.50 - £4.99	130,694	4.59	9.40	-	-	-
£5.00 - £9.99	650,000	6.43	9.53	-	-	-
£10.00-£15.00	160,000	11.90	9.56	-	-	-
Total	2,532,240	3.68	8.93	1,825,801	1.26	8.70

The fair value of the options granted during the year was calculated using the following assumptions:

Grant date	28 Feb 2006	28 Feb 2006	23 Mar 2006	19 Apr 2006	27 Apr 2006
Pricing model	BlackScholes	BlackScholes	BlackScholes	BlackScholes	BlackScholes
Share price at grant	£1.540	£1.540	£2.000	£2.130	£2.800
Exercise price	£1.540	£1.540	£2.065	£2.120	£3.000
Vesting criteria	(1)	(2)	(1)	(2)	(1)
Expected volatility	26.2%	26.2%	26.8%	35.8%	35.8%
Expected life	10 Years	10 Years	10 Years	10 Years	10 Years
Risk free rate	4.50%	4.50%	4.50%	4.50%	4.50%
Dividend yield	0%	0%	0%	0%	0%
Estimated forfeiture	30%	30%	30%	30%	30%
Probability criteria is met	1	0.50	1	0.50	1
Fair value per option	£0.735	£0.735	£0.942	£1.160	£1.498

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

---

### 22. SHARE BASED PAYMENTS (continued)

Grant date	1 Jun 2006	1 Jun 2006	7 Jun 2006	24 July 2006	26 July 2006
Pricing model	BlackScholes	BlackScholes	Binomial	BlackScholes	BlackScholes
Share price at grant	£4.824	£4.824	£5.233	£11.050	£12.030
Exercise price	£4.850	£4.850	£5.40	£11.575	£12.450
Vesting criteria	(1)	(2)	(3)	(6)	(4)
Expected volatility	42.5%	42.5%	42.5%	51.5%	51.5%
Expected life	10 Years	10 Years	10 Years	10 Years	10 Years
Risk free rate	4.50%	4.50%	4.50%	4.50%	4.50%
Dividend yield	0%	0%	0%	0%	0%
Estimated forfeiture	30%	30%	0%	30%	30%
Probability criteria is met	1	0.5	1	1	1
Fair value per option	£2.923	£2.923	£2.171	£5.852	£6.850

Grant date		1 Nov 2006	1 Nov 2006
Pricing model		BlackScholes	Binomial
Share price at grant		£9.550	£9.550
Exercise price		£9.875	£9.875
Vesting criteria		(4)	(5)
Expected volatility		55.1%	55.1%
Expected life		10 Years	10 Years
Risk free rate		4.75%	4.75%
Dividend yield		0%	0%
Estimated forfeiture		30%	30%
Probability criteria is met		1	1
Fair value per option		£5.361	£5.200

Vesting criteria:

- (1) At the rate of 1/6<sup>th</sup> after 6 months, and 1/36<sup>th</sup> subsequently, for a total vesting period of 36 months
- (2) Conditional upon achieving average monthly net revenues of \$3m over a period of 6 months consecutive. It is estimated this will be met within 3 years from date of grant.
- (3) At the rate of 1/5<sup>th</sup> for achieving each incremental increase of £100 in the share price up to a maximum of £500. It is estimated this will be met within 5 years from date of grant.
- (4) At the rate of 1/8<sup>th</sup> after 6 months, and 1/48<sup>th</sup> subsequently, for a total vesting period of 48 months
- (5) Conditional that 5-day average share price is not above £50.00 prior to 11 July 2007. If so, 25% vests immediately and remainder over 36 months. If condition is not met, options are cancelled.
- (6) At the rate of 1% for each 1% of targeted number subscribers becoming subject to qualifying agreements.

The expected volatility was based upon historical volatility of the company's share price from IPO to date of grant. The expected life is the expected period to exercise.

At the year end the company has accrued \$720,750 (2005: \$29,050) in respect of potential employers' National Insurance Contribution arising on exercise of the options by United Kingdom employees, calculated in line with the FRS 20 charge. This is included in accruals in creditors falling due within less than one year.

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

---

### 23. RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

	2006	2005
	\$	(As restated) \$
Loss for the financial year	(11,483,218)	(3,525,132)
New share capital subscribed	11,690,387	1,819,259
Other recognized gains and losses	1,147,390	29,078
	<hr/>	<hr/>
Net addition/(reduction) to shareholders' funds	1,354,559	(1,676,795)
Opening shareholders' funds (originally \$2,000,286 (2005: \$3,688,847) before deducting prior year adjustment of \$29,050 (2005: \$40,816))	1,971,236	3,648,031
	<hr/>	<hr/>
Closing shareholders' funds	<u>3,325,795</u>	<u>1,971,236</u>

### 24. FINANCIAL INSTRUMENTS

The Group's financial instruments consist principally of cash, liquid resources and various other items such as trade debtors and trade creditors. At 31 December 2006 there were no material differences between the net book value and the fair value of the Group's financial assets and liabilities. The Group's main risks in respect of financial instruments are interest rate and liquidity risk.

#### Financial Liabilities

The interest rate risk and financial maturity of the Group's financial liabilities, excluding short term trading items are set out in note 17.

#### Financial Assets

The interest rate risk profile of the Group's financial assets, excluding short term trading items, are floating rate interest earnings, amounting to \$82,312 (2005: \$15,695).

### 25. RECONCILIATION OF OPERATING LOSS TO NET CASH OUTFLOW FROM OPERATING ACTIVITIES

	2006	2005
	\$	\$
Operating Loss	(11,536,639)	(3,512,865)
Amortization	1,395	-
Depreciation Charges	593,106	560,109
Loss on Disposal	42,829	-
Transfer to Option Reserve	1,254,065	203,299
Exchange Difference Taken to Reserves	(106,675)	(174,221)
Decrease in Debtors	1,381,023	666,843
Increase in Creditors	472,297	435,230
	<hr/>	<hr/>
Net cash Outflow from Operating Activities	<u>(7,898,599)</u>	<u>(1,821,605)</u>

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

### 26. NOTES TO CASH FLOW STATEMENT

#### RETURNS ON INVESTMENTS AND SERVICING OF FINANCE

	2006	2005
	\$	\$
Interest received	82,312	15,695
Interest paid	(16,186)	(27,962)
Net cash inflow/(outflow) from returns on investments and servicing of finance	<u>66,126</u>	<u>(12,267)</u>

#### TAXATION

	2006	2005
	\$	\$
Taxation	<u>12,705</u>	<u>-</u>

#### CAPITAL EXPENDITURE

	2006	2005
	\$	\$
Payments to acquire tangible fixed assets	(515,989)	(388,321)
Payments to acquire intangible fixed assets	(50,222)	-
Receipts from sale and leaseback	-	100,000
Net cash outflow from capital expenditure	<u>(566,211)</u>	<u>(288,321)</u>

#### FINANCING

	2006	2005
	\$	\$
Issue of equity share capital	11,690,387	1,819,259
Capital element of finance lease	(44,760)	(4,860)
Net cash inflow from financing	<u>11,645,627</u>	<u>1,814,399</u>

### 27. RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET FUNDS

	2006		2005	
	\$	\$	\$	\$
Increase/(decrease) in cash in the period	3,234,238		(307,794)	
Net cash outflow/(inflow) from changes in net debt	<u>44,760</u>		<u>(95,140)</u>	
		3,278,998		(402,934)
Change in net funds		3,278,998		(402,934)
Net funds at 1 January 2006		475,393		878,327
Net funds at 31 December 2006		<u>3,754,391</u>		<u>475,393</u>

# 121MEDIA, INC.

## NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2006

---

### 28. ANALYSIS OF CHANGES IN NET FUNDS

	At 1 Jan 2006 \$	Cash flows \$	At 31 Dec 2006 \$
Cash in hand and at bank	570,533	3,234,238	3,804,771
	<u>570,533</u>	<u>3,234,238</u>	<u>3,804,771</u>
Debt:			
Finance Leases and Hire Purchase Contracts	(95,140)	44,760	(50,380)
	<u>(95,140)</u>	<u>44,760</u>	<u>(50,380)</u>
Net funds	<u>475,393</u>	<u>3,278,998</u>	<u>3,754,391</u>

### 29. PENSIONS

The Company operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the Company in an independently administered fund. The pension cost charge represents contributions payable by the Company to the fund and amounted to \$16,852 (2005: \$21,127). At the year end a creditor of \$10,775 (2005: \$nil) was owed in respect of unpaid contributions.

### 30. COMMITMENTS UNDER OPERATING LEASES

At 31 December 2006 the Group and the Company had annual commitments under non-cancellable operating leases as set out below: -

Group	Land and buildings	
	2006 \$	2005 \$
Operating leases which expire:		
Within 1 year	-	-
Within 2 to 5 years	-	139,398
More than 5 years	175,016	-
	<u>175,016</u>	<u>139,398</u>

### 31. RELATED PARTY TRANSACTIONS

During the year consultancy payments of \$307,852 (2005: \$305,356) were made to K. Ertugrul, \$132,967 (2005: \$11,106) to Bowen Limited on behalf of T. Bowen, \$46,893 (2005: \$45,412) to D. Svendsen, \$28,801 to G. Baz.

As at 31 December 2006, \$2,083 was still owed to D. Svendsen, \$14,693 to G. Baz and \$21,307 to K. Ertugrul.

### 32. ULTIMATE CONTROLLING PARTY

The Directors are of the opinion that no one party has sufficient interest in the share capital of the Company to be able to control the Group.

### 33. POST BALANCE SHEET EVENTS

During February 2007 169,808 shares were placed with Morgan Stanley Principal Investments, Inc. for a consideration (before expenses) of \$5,000,000.