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ICEWEB INC
Form SB-2/A
January 31, 2006

AS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON JANUARY 31, 2006

Registration No. 333-126898

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

FORM SB-2

REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933
(AMENDMENT NO. 2)

ICEWEB, INC.
(Name of small business issuer in its charter)

| | | |
|--|---|---|
| Delaware (State or jurisdiction of incorporation or organization) | 7389 (Primary Standard Industrial Classification Code Number) | 13-2640971 (I.R.S. Employer Identification No.) |
|--|---|---|

205 Van Buren Street
Herndon, Virginia 20170
703-964-8000
(Address and telephone number of principal executive offices)
(Address of principal place of business or intended principal place of business)

Mr. John R. Signorello
Chief Executive Officer
IceWEB, Inc.
205 Van Buren Street
Herndon, Virginia 20170
703-964-8000
(Name, Address and Telephone Number of Agent For Service)

Copies of all communications to:
James M. Schneider, Esq.
Schneider Weinberger & Beilly LLP
2200 Corporate Boulevard, N.W.
Suite 210
Boca Raton, Florida 33431
Telephone: 561-362-9595
Facsimile No: 561-361-9612

Approximate Date of Proposed Sale to the Public: As soon as practicable after the effective date of this registration statement.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. []

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. []

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If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration number of the earlier effective registration statement for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.

CALCULATION OF REGISTRATION FEE

| Title of each class of securities to be registered ----- | Amount to be registered ----- | Dollar offering price per security ----- | Proposed maximum aggregate offering price(1) ----- |
|---|-------------------------------------|---|--|
| Common stock, par value \$.001 per share (1) | 250,000 | \$ 0.92 | \$ 230,000 |
| Common stock, par value \$.001 per share (1) (2) | 1,666,667 | \$ 0.92 | \$ 1,533,334 |
| Common stock, par value \$.001 per share (3) | 2,000,000 | \$ 2.00 | \$ 4,000,000 |
| Common stock, par value \$.001 per share (4) | 1,250,000 | \$ 4.80 | \$ 6,000,000 |
| Common stock, par value \$.001 per share (5) | 1,250,000 | \$ 9.60 | \$ 12,000,000 |
| Common stock, par value \$.001 per share (6) | 287,500 | \$ 4.00 | \$ 1,150,000 |
| Common stock, par value \$.001 per share (7) | 287,500 | \$ 8.00 | \$ 2,300,000 |
| Common stock, par value \$.001 per share (8) | 175,000 | \$ 0.70 | \$ 122,500 |
| Common stock, par value \$.001 per share (9) | 5,000 | \$ 2.00 | \$ 10,000 |
| | ----- 7,171,667 | | |

Total Registration Fee

(1) Estimated solely for purposes of calculating the registration fee pursuant

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to Rule 457 under the Securities Act of 1933 based on the average of the high and low sale price of the common stock as reported on the OTC Bulletin Board on July 20, 2005.

- (2) Includes shares of common stock issuable upon conversion of shares of Series A Convertible Preferred Stock.
- (3) Includes shares of common stock issuable upon the exercise of outstanding Common Stock Purchase Warrants "A" issued in March 2005.
- (4) Includes shares of common stock issuable upon the exercise of outstanding Common Stock Purchase Warrants "B" issued in March 2005.
- (5) Includes shares of common stock issuable upon the exercise of outstanding Common Stock Purchase Warrants "C" issued in March 2005.
- (6) Includes shares of common stock issuable upon the exercise of outstanding Series H Common Stock Purchase Warrants.
- (7) Includes shares of common stock issuable upon the exercise of outstanding Series I Common Stock Purchase Warrants.
- (8) Includes shares of common stock issuable upon the exercise of outstanding \$0.70 Common Stock Purchase Warrants "A" issued in March 2005.
- (9) Includes shares of common stock issuable upon the exercise of an outstanding common stock purchase warrant with an exercise price of \$2.00 per share.

To the extent permitted by Rule 416, this registration statement also covers such additional number of shares of common stock as may be issuable as a result of the anti-dilution provisions of the Series A Convertible Preferred Stock and common stock purchase warrants listed above.

THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATE OR DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT SHALL FILE A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THIS REGISTRATION STATEMENT SHALL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8(a) OF THE SECURITIES ACT OF 1933, AS AMENDED, OR UNTIL THE REGISTRATION STATEMENT SHALL BECOME EFFECTIVE ON SUCH DATE AS THE COMMISSION, ACTING PURSUANT TO SAID SECTION 8(a), MAY DETERMINE.

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The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to Completion, dated January 31, 2006

PROSPECTUS

ICEWEB, INC.

7,171,667 Shares of Common Stock

This prospectus covers the resale of a total of 7,171,667 shares being offered by selling security holders listed in the section of this prospectus entitled "Selling Security Holders." Of the shares covered by this prospectus,

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250,000 shares are presently outstanding, 1,666,667 shares are issuable upon the conversion of shares of our Series A Convertible Preferred Stock and 5,255,000 shares are issuable upon exercise of warrants with exercise prices ranging from \$0.70 to \$9.60 per share. We will not receive any of the proceeds from the sale of the shares being offered by the selling security holders.

For a description of the plan of distribution of the shares, please see page 49 of this prospectus.

Our common stock is traded on the OTC Bulletin Board under the trading symbol "IWEB." On January 27, 2006 the last sale price for our common stock was \$0.80

INVESTMENT IN OUR COMMON STOCK INVOLVES A HIGH DEGREE OF RISK. SEE "RISK FACTORS" BEGINNING ON PAGE 4 OF THIS PROSPECTUS TO READ ABOUT RISKS OF INVESTING IN OUR COMMON STOCK.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED THESE SECURITIES OR DETERMINED IF THIS PROSPECTUS IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this Prospectus is _____, 2006

PROSPECTUS SUMMARY

We market proprietary software products, information technology professional services, and third party computer hardware and software. Our mission is to provide value to our customers by delivering a broad range of proven technologies and services that enable organizations to gain competitive advantage, maximize business results and speed innovation.

Our suite of software products and integration service products enable government and other organizations to independently manage, create, publish and deliver content easily and affordably. Our suite of software products, which are centered on knowledge-based support, are scalable and can be implemented on any website. We also provide a range of information technology consulting services and product support services on a project-by-project basis, including software programming and network engineering. Our suite of software products and consulting services enable organizations to reduce time and effort by converging knowledge-based information with easy to manage websites and e-learning portals. We also market third party computer hardware and software as an authorized reseller for a broad array of products, including large power supplies.

Our principal executive offices are located at 205 Van Buren Street, Suite 150, Herndon, Virginia 20170, and our telephone number is 703-964-8000. Our fiscal year end is September 30.

When used in this prospectus, the terms "IceWEB," "we," "our," and "us" refers to IceWEB, Inc., a Delaware corporation, and our subsidiaries. The information which appears on our web site at www.iceweb.com is not part of this prospectus.

All per share information contained in this prospectus gives effect to the ten for one (10:1) forward stock split of our common stock effective October

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13, 2004 and a one for eighty (1:80) reverse stock split effective April 27, 2005.

THE OFFERING

This prospectus covers the resale of a total of 7,171,667 shares of our common stock by the selling security holders. Of the shares covered by this prospectus, 250,000 shares are presently outstanding, 1,666,667 shares are issuable upon the conversion of shares of our Series A Convertible Preferred Stock and 5,255,000 shares are issuable upon exercise of warrants with exercise prices ranging from \$0.70 to \$9.60 per share. The selling security holders may resell their shares from time-to-time, including through broker-dealers, at prevailing market prices. We will not receive any proceeds from the resale of our shares by the selling security holders. We will pay all of the fees and expenses associated with registration of the shares covered by this prospectus.

COMMON STOCK

Outstanding Prior to this Offering: 6,492,286 shares at January 15, 2006.

Outstanding After this Offering: 18,929,266 shares, including an aggregate of 12,436,980 shares which are reserved for possible issuance upon the conversion of outstanding Series A Convertible Preferred Stock and Series B Convertible Preferred Stock, exercise of outstanding common stock purchase warrants or exercise of options granted under our 2000 Management and Director Equity Incentive and Compensation Plan.

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Common Stock Reserved: 12,436,980 shares, including:

- o 1,666,667 shares issuable upon the conversion of our Series A Convertible Preferred Stock, the resale of which is covered by this prospectus,
- o 1,833,334 shares issuable upon the conversion of our Series B Convertible Preferred Stock,
- o 7,765,000 shares upon the exercise of outstanding warrants with exercise prices ranging from \$0.70 to \$16.00 per share, the resale of 5,255,000 shares of which is covered by this prospectus,
- o 1,137,729, shares of our common stock underlying options which are presently outstanding under our 2000 Management and Director Equity Incentive and Compensation Plan with a weighted average exercise price of \$4.91 per share, and
- o 34,250 shares of our common stock

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reserved for issuance under our 2000 Management and Director Equity Incentive and Compensation Plan.

RISK FACTORS

The securities offered hereby involve a high degree of risk and immediate substantial dilution. See "Risk Factors" and "Dilution."

OTC BULLETIN BOARD SYMBOL

IWEB.

SELECTED CONSOLIDATED FINANCIAL DATA

The following summary financial information has been derived from the financial statements that are included elsewhere in this prospectus.

STATEMENT OF OPERATIONS DATA:

| | Year ended September 30, | |
|---|--------------------------|----------------|
| | 2005 | 2004 |
| Revenues | \$ 6,809,590 | \$ 6,662,652 |
| Cost of Sales | 4,753,276 | 5,015,494 |
| Total Operating Expense | 2,884,566 | 3,656,610 |
| Operating income (loss) | (828,252) | (2,009,452) |
| Net income (loss) | \$ (903,508) | \$ (2,035,443) |
| Basic and diluted (loss) per common share | \$ (0.15) | \$ (0.41) |
| Weighted common shares outstanding | 5,865,935 | 5,049,368 |

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BALANCE SHEET DATA:

| | September 30, 2005 |
|----------------------------------|--------------------|
| Working capital | \$ 319,137 |
| Cash | \$ 557,175 |
| Total current assets | \$ 2,221,916 |
| Total assets | \$ 2,788,263 |
| Total current liabilities | \$ 1,902,779 |
| Total liabilities | \$ 2,118,404 |
| Total stockholders' equity | \$ 669,859 |

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

Certain statements in this prospectus contain or may contain forward-looking statements that are subject to known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These forward-looking statements were based on various factors and were derived utilizing numerous assumptions and other factors that could cause our actual results to differ materially from those in the forward-looking statements. These factors include, but are not limited to, our ability to increase our revenues, develop our brands, implement our strategic initiatives, economic, political and market conditions and fluctuations, government and industry regulation, U.S. and global competition, and other factors. Most of these factors are difficult to predict accurately and are generally beyond our control.

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You should consider the areas of risk described in connection with any forward-looking statements that may be made in this prospectus. Readers are cautioned not to place undue reliance on these forward-looking statements and readers should carefully review this prospectus in its entirety, including the risks described in "Risk Factors." Except for our ongoing obligations to disclose material information under the Federal securities laws, we undertake no obligation to release publicly any revisions to any forward-looking statements, to report events or to report the occurrence of unanticipated events. For any forward-looking statements contained in any document, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements speak only as of the date of this prospectus, and you should not rely on these statements without also considering the risks and uncertainties associated with these statements and our business.

RISK FACTORS

Before you invest in our securities, you should be aware that there are various risks. Additional risks and uncertainties not presently known to us or that we currently believe to be immaterial may also adversely affect our business. You should consider carefully these risk factors, together with all of the other information included in this prospectus before you decide to purchase our securities. If any of the following risks and uncertainties develop into actual events, our business, financial condition or results of operations could be materially adversely affected and you could lose your entire investment in our company.

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WE HAVE AN ACCUMULATED DEFICIT AND WE ANTICIPATE CONTINUING LOSSES THAT WILL RESULT IN SIGNIFICANT LIQUIDITY AND CASH FLOW PROBLEMS ABSENT A MATERIAL INCREASE IN OUR REVENUES.

We have an accumulated deficit of \$6,500,655 at September 30, 2005. For the years ended September 30, 2005 and 2004, we had a net loss of approximately \$903,000 and \$2 million, respectively, and cash used in operations was approximately \$920,000 and \$795,000, respectively. The report of our independent registered public accounting firm on our financial statements for the fiscal year ended September 30, 2005 contained a qualification expressing substantial doubt as to our ability to continue as a going concern as a result of our net losses in operations. While we reported a modest increase in our revenues for fiscal 2005 as compared to fiscal 2004, we cannot assure you that our revenues will increase in future periods, nor can we assure you that they will not decrease. As long as our cash flow from operations remains insufficient to fund our operations, we will continue depleting our cash and other financial resources. Our failure to achieve profitable operations in future periods will adversely affect our ability to continue as a going concern. In this event, you could lose all of your investment in our company.

WE WILL NEED ADDITIONAL FINANCING WHICH WE MAY NOT BE ABLE TO OBTAIN ON ACCEPTABLE TERMS. IF WE CANNOT RAISE ADDITIONAL CAPITAL AS NEEDED, OUR ABILITY TO EXECUTE OUR GROWTH STRATEGY AND FUND OUR ONGOING OPERATIONS WILL BE IN JEOPARDY.

Historically, our operations have been financed primarily through the issuance of equity. Capital is typically needed not only to fund our ongoing operations and to pay our existing obligations, but capital is also necessary if we wish to acquire additional assets or companies and for the effective integration, operation and expansion of these businesses. Our future capital requirements, however, depend on a number of factors, including our ability to

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internally grow our revenues, manage our business and control our expenses. At September 30, 2005, we had a working capital surplus of \$319,137 as compared to a working capital deficit of \$1,049,557 at September 30, 2004. This change is primarily attributable to proceeds we received from the sale of equity securities during fiscal 2005. However, we will need to raise additional capital to fund our ongoing operations, pay our existing obligations and for future growth of our company. As described below the terms of the sale of our Series B Convertible Preferred Stock may significantly restrict our ability to raise working capital as needed. We cannot assure you that additional working capital is available to us in the future upon terms acceptable to us. If we do not raise funds as needed, our ability to provide for current working capital needs, make additional acquisitions, grow our company, and continue our existing business and operations is in jeopardy. In this event, you could lose all of your investment in our company.

WHILE THE SHARES OF OUR SERIES B CONVERTIBLE PREFERRED STOCK ARE OUTSTANDING WE ARE PROHIBITED FROM ENTERING INTO CERTAIN TYPES OF EQUITY AND DEBT TRANSACTIONS WHICH MAY ADVERSELY EFFECT OUR ABILITY TO RAISE WORKING CAPITAL AS NEEDED.

Under the terms of our sale of Series B Convertible Preferred Stock in December 2005, we agreed to a number of limitations on our future capital raising activities, including:

- o for a period of three years we will not issue any convertible debt or preferred stock,

for a period of two years we will not enter into any new borrowings of more than twice as much as the sum of EBITDA (earnings before income taxes, depreciation and amortization) from recurring operations over the past four quarters,

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- o for so long as the shares are outstanding we will not issue any debt or equity securities with a floating conversion price or reset feature, and
- o for so long as the shares are outstanding we cannot issue any common stock or securities which are convertible into common stock at an effective price per share less than the conversion value of the Series B Convertible Preferred Stock which is initially \$0.2727 per share.

These restrictions are likely to adversely effect our ability to raise working capital as needed in future periods as the types of financing transactions generally available to us and other comparably-sized public companies often involve the sale of a convertible security with a reset feature, or the sale of common stock at a discount to market.

WHILE SHARES OF OUR SERIES A CONVERTIBLE PREFERRED STOCK ARE OUTSTANDING WE ARE PROHIBITED FROM UNDERTAKING CERTAIN CAPITAL RAISING TRANSACTIONS WHICH MAY MATERIALLY ADVERSELY EFFECT OUR ABILITY TO RAISE FUNDS IN FUTURE PERIODS.

The designations of the Series A Convertible Preferred Stock prohibit us from selling common stock or any other security which is convertible into common stock or issuing any rights, options or warrants which entitle the holder to purchase shares of our common stock at a price less than \$0.60 per share, subject to adjustment as described elsewhere in this prospectus. So long as shares of our Series A Convertible Preferred stock are outstanding, this prohibition will prevent us from raising additional capital at an effective offering price of less than \$0.60 per share. While the market value of our

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common stock as of the date of this prospectus is greater than \$0.60 per share, we do not know if the trading price of our common stock will remain above \$0.60 per share in future periods, particularly in light of the fact that we may be significantly increasing the number of shares of our common stock which will be freely tradeable as a result of sales made by the selling security holders under this prospectus. If the market price of our common stock should fall to a price range which is near or below \$0.60 per share we may be unable to raise capital in future periods as needed which could adversely effect our liquidity, operation of our company and ability to continue as a going concern.

In addition, under the terms of the Preferred Stock Purchase Agreement for the Series A Convertible Preferred Stock for a period of three years beginning March 30, 2005 we have contractually agreed not to issue any additional shares of preferred stock or any convertible debt, not to enter into any transactions which contain a reset provision which could result in additional shares being issued at some future date and not to enter into certain other types of financing transactions. These contractual limitations may limit our ability to raise capital as needed in future periods which could adversely effect our ability to continue our operations.

OUR FACTORING AGREEMENT WITH SAND HILL FINANCE, LLC CONTAINS CERTAIN TERMS WHICH MAY ADVERSELY AFFECT OUR ABILITY TO RAISE CAPITAL IN FUTURE PERIODS.

In December 2005 we entered into a Finance Agreement with Sand Hill Finance, LLC for a \$1 million accounts receivable factoring line. Under the terms of this agreement we agreed not to take certain actions including undertaking a transaction which would result in a change of control of our company or the transfer of more than 20% of our securities and incurring any indebtedness other than trade credit in the ordinary course of business. These restrictions may limit our ability to raise working capital as needed.

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OUR PRIMARY ASSETS SERVE AS COLLATERAL UNDER OUR ACCOUNTS RECEIVABLE FACTORING LINE. IF WE WERE TO DEFAULT ON THIS AGREEMENTS, THE LENDER COULD FORECLOSE ON OUR ASSETS.

In December 2005 we entered into a \$1 million accounts receivable factoring agreement with Sand Hill Finance, LLC. The revolving line is collateralized by a blanket security interest in our assets. If we should default under the terms of this agreement, the lender could seek to foreclose on our primary assets. If the lender was successful, we would be unable to conduct our business as it is presently conducted and our ability to generate revenues and fund our ongoing operations would be materially adversely affected.

WE ARE RELIANT ON REVENUES FROM TWO CUSTOMERS. BECAUSE WE ARE NOT A PARTY TO LONG TERM AGREEMENTS WITH EITHER CUSTOMER, THE LOSS OF ONE OR BOTH OF THESE CUSTOMERS WOULD BE ADVERSE TO OUR FINANCIAL RESULTS IN FUTURE PERIODS.

Revenues from two customers represented approximately 37% and approximately 34% of total revenues for the years ended September 30, 2005 and 2004, respectively, and approximately 53% of our accounts receivable at September 30, 2005 are due from these two customers. Both of these customers purchase products and services from us on a purchase order basis and, accordingly, may elect at any time to purchase similar products or services from our competitors. Until such time, if ever, as we are able to sufficiently expand our sales efforts and remove this dependency on revenues from these two customers, if one or both of them should cease purchasing products and services from us our revenues and results of operations would be materially adversely affected.

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OUR MANAGEMENT MAY BE UNABLE TO EFFECTIVELY INTEGRATE OUR ACQUISITIONS AND TO MANAGE OUR GROWTH AND WE MAY BE UNABLE TO FULLY REALIZE ANY ANTICIPATED BENEFITS OF THESE ACQUISITIONS.

Our business strategy includes growth through acquisition and internal development. We are subject to various risks associated with our growth strategy, including the risk that we will be unable to identify and recruit suitable acquisition candidates in the future or to integrate and manage the acquired companies. Acquired companies' histories, geographical locations, business models and business cultures can be different from ours in many respects. Our directors and senior management face a significant challenge in their efforts to integrate our businesses and the business of the acquired companies or assets, and to effectively manage our continued growth. There can be no assurance that our efforts to integrate the operations of any acquired assets or companies acquired in the future will be successful, that we can manage our growth or that the anticipated benefits of these proposed acquisitions will be fully realized. The dedication of management resources to these efforts may detract attention from our day-to-day business. There can be no assurance that there will not be substantial costs associated with these activities or of the success of our integration efforts, either of which could have a material adverse effect on our operating results.

WE HAVE NOT VOLUNTARILY IMPLEMENTED VARIOUS CORPORATE GOVERNANCE MEASURES, IN THE ABSENCE OF WHICH, STOCKHOLDERS MAY HAVE MORE LIMITED PROTECTIONS AGAINST INTERESTED DIRECTOR TRANSACTIONS, CONFLICTS OF INTEREST AND SIMILAR MATTERS.

Recent Federal legislation, including the Sarbanes-Oxley Act of 2002, has resulted in the adoption of various corporate governance measures designed to promote the integrity of the corporate management and the securities markets. Some of these measures have been adopted in response to legal requirements. Others have been adopted by companies in

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response to the requirements of national securities exchanges, such as the NYSE or The Nasdaq Stock Market, on which their securities are listed. Among the corporate governance measures that are required under the rules of national securities exchanges and Nasdaq are those that address board of directors' independence, audit committee oversight, and the adoption of a code of ethics. Because our stock is not listed on an exchange or quoted on Nasdaq, we are not required to adopt these corporate governance standards. While our board of directors has adopted a Code of Ethics and Business Conduct and our Board has established Audit and Compensation Committees, we have not adopted all of the corporate governance measures which we might otherwise have been required to adopt if our securities were listed on a national securities exchange or Nasdaq. It is possible that if we were to adopt all of these corporate governance measures, stockholders would benefit from somewhat greater assurances that internal corporate decisions were being made by disinterested directors and that policies had been implemented to define responsible conduct. Prospective investors should bear in mind our current lack of corporate governance measures in formulating their investment decisions.

THE EXERCISE OF WARRANTS AND OPTIONS AND THE CONVERSION OF SHARES OF OUR SERIES A CONVERTIBLE PREFERRED STOCK WILL BE DILUTIVE TO OUR EXISTING STOCKHOLDERS.

At January 15, 2006 we had outstanding:

- o 6,492,286 shares of our common stock,
- o 1,666,667 shares of Series A Convertible Preferred Stock which is convertible into 1,666,667 shares of our common

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stock,

- o 1,833,334 shares of our Series B Convertible Preferred Stock which is convertible into 1,833,334 shares of common stock,
- o common stock purchase warrants to purchase a total of 7,765,000 shares of our common stock with exercise prices ranging from \$0.70 to \$16.00 per share, and
- o options granted under our 2000 Management and Director Equity Incentive and Compensation Plan which are exercisable into 1,137,729 shares of our common stock with a weighted average exercise price of \$4.91 per share.

The conversion of the Series A Convertible Preferred Stock or the Series B Convertible Preferred Stock and/or the exercise of outstanding options and warrants may materially adversely affect the market price of our common stock and will have a dilutive effect on our existing stockholders.

CERTAIN OF OUR OUTSTANDING WARRANTS CONTAIN CASHLESS EXERCISE PROVISIONS WHICH MEANS WE WILL NOT RECEIVE ANY CASH PROCEEDS UPON THEIR EXERCISE.

In March 2005 and December 2005, we issued five year common stock purchase warrants to purchase an aggregate of 6,950,000 shares of our common stock with exercise prices ranging from \$2.00 to \$9.60 per share in connection with the sales of shares of our Series A Convertible Preferred Stock and Series B Convertible Preferred Stock. In December 2005 we also issued a seven year common stock purchase warrant to purchase 25,000 shares of our common stock with an exercise price of \$1.00 per share in connection with our accounts receivable financing agreement with Sand Hill Finance, LLC. All of these warrants are exercisable on a cashless basis which means that the holders, rather than paying the exercise price in cash, may surrender a number of warrants equal to the exercise price of the warrants being exercised. The utilization of this cashless exercise feature will deprive us of additional capital which might otherwise be obtained if the warrants did not contain a cashless feature.

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PROVISIONS OF OUR CERTIFICATE OF INCORPORATION AND BYLAWS MAY DELAY OR PREVENT A TAKE-OVER WHICH MAY NOT BE IN THE BEST INTERESTS OF OUR STOCKHOLDERS.

Provisions of our certificate of incorporation and bylaws may be deemed to have anti-takeover effects, which include when and by whom special meetings of our stockholders may be called, and may delay, defer or prevent a takeover attempt. In addition, certain provisions of the Delaware General Corporations Law also may be deemed to have certain anti-takeover effects which include that control of shares acquired in excess of certain specified thresholds will not possess any voting rights unless these voting rights are approved by a majority of a corporation's disinterested stockholders.

In addition, our certificate of incorporation authorizes the issuance of up to 10,000,000 shares of preferred stock with such rights and preferences as may be determined from time to time by our Board of Directors. We presently have outstanding 1,666,667 shares of our Series A Convertible Preferred Stock and 1,833,334 shares of our Series B Convertible Preferred Stock. Our Board of Directors may, without stockholder approval, issue additional series of preferred stock with dividends, liquidation, conversion, voting or other rights that could adversely affect the voting power or other rights of the holders of our common stock.

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IF THE SELLING SECURITY HOLDERS ALL ELECT TO SELL THEIR SHARES OF OUR COMMON STOCK AT THE SAME TIME, THE MARKET PRICE OF OUR SHARES MAY DECREASE.

It is possible that the selling security holders will offer all of the shares for sale. Further, because it is possible that a significant number of shares could be sold at the same time hereunder, the sales, or the possibility thereof, may have a depressive effect on the market price of our common stock.

MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our common stock is quoted on the OTCBB. On April 27, 2005 our symbol was changed from ICEW to IWEB in connection with a 1:80 reverse split of our common stock effective on that date. The reported high and low bid prices for the common stock as reported on the OTCBB are shown below for the periods indicated. The quotations reflect inter-dealer prices, without retail mark-up, markdown or commission, and may not represent actual transactions.

| | High ----- | Low ----- |
|---|---------------|--------------|
| Fiscal 2004 | | |
| First quarter ended December 31, 2003 | \$3.82 | \$1.28 |
| Second quarter ended March 31, 2004 | \$5.20 | \$1.28 |
| Third quarter ended June 30, 2004 | \$4.08 | \$2.56 |
| Fourth quarter ended September 30, 2004 | \$4.72 | \$1.92 |

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Fiscal 2005

| | | |
|---|--------|--------|
| First quarter ended December 31, 2004 | \$5.60 | \$2.40 |
| Second quarter ended March 31, 2005 | \$3.20 | \$1.60 |
| Third quarter ended June 30, 2005 | \$2.20 | \$0.80 |
| Fourth quarter ended September 30, 2005 | \$1.30 | \$0.65 |

Fiscal 2006

| | | |
|---|--------|--------|
| First quarter ended December 31, 2005 | \$1.05 | \$0.65 |
|---|--------|--------|

On January 27, 2006, the last sale price of our common stock as reported on the OTCBB was \$0.80. As of January 15, 2006, there were approximately 360 record owners of our common stock.

DIVIDEND POLICY

We have never paid cash dividends on our common stock. Under Delaware law, we may declare and pay dividends on our capital stock either out of our surplus, as defined in the relevant Delaware statutes, or if there is no such surplus, out of our net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year. If, however, the capital of our company, computed in accordance with the relevant Delaware statutes, has been diminished by depreciation in the value of our property, or by losses, or otherwise, to an amount less than the aggregate amount of the capital represented by the issued and outstanding stock of all classes having a preference upon the distribution of assets, we are prohibited from declaring and paying out of such net profits any dividends upon any shares of our capital stock until the deficiency in the amount of capital represented by the issued and outstanding stock of all classes having a preference upon the distribution

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of assets shall have been repaired.

Under the terms of both our Series A Convertible Preferred Stock and Series B Convertible Preferred Stock, we cannot pay dividends on our common stock so long as shares of our Series A Convertible Preferred Stock or Series B Convertible Preferred Stock are outstanding or under the terms of our Financing Agreement with Sand Hill Finance, LLC. We do not anticipate that any cash dividends will be declared or paid on our common stock in the foreseeable future.

SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS

The following table sets forth securities authorized for issuance under our 2000 Management and Director Equity Incentive and Compensation Plan and any compensation plan not approved by our stockholders as of September 30, 2005.

| | Number of securities to be issued upon exercise of of outstanding options, warrants and rights (a) ----- | Weighted average exercise price of outstanding options, warrants and rights (b) ----- | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) ----- |
|---|---|---|--|
| Plan category | | | |
| 2000 Management and Director Equity Incentive and Compensation Plan | 1,137,729 | \$4.91 | 34,250 |
| Equity compensation plans not approved by stockholders ... | 0 | 0 | 0 |

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CAPITALIZATION

The following table sets forth our capitalization as of September 30, 2005. This table gives no effect to the possible exercise of outstanding options or common stock purchase warrants or the application of the proceeds therefrom. The table should be read in conjunction with the financial statements and related notes included elsewhere in this prospectus.

| | September 30, 2005 ----- |
|---|-----------------------------|
| Long-term liabilities | \$ 215,625 |
| Stockholders' equity: | |
| Preferred stock, \$.001 par value, 10,000,000 shares authorized, Series A Convertible Preferred Stock, 1,666,667 shares authorized, 1,666,667 shares issued and outstanding | 1,667 |

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| | |
|---|----------------|
| Common stock, \$.001 par value, 1,000,000,000 shares authorized, 6,492,286 shares issued and outstanding | 6,493 |
| Treasury stock, at cost, 162,500 shares | (13,000) |
| Stock subscription receivable | (143,477) |
| Additional paid-in capital | 7,318,831 |
| Accumulated deficit | (6,500,655) |
| | ----- |
| Total stockholders' equity | \$ 669,859 |
| | ----- |
| Total capitalization | \$ 885,484 |
| | ----- |

USE OF PROCEEDS

We will not receive any proceeds upon the sale of shares by the selling security holders. Any proceeds that we receive from the exercise of outstanding warrants will be used by us for general working capital. The actual allocation of proceeds realized from the exercise of these securities will depend upon the amount and timing of such exercises, our operating revenues and cash position at such time and our working capital requirements. There can be no assurances that any of the outstanding warrants will be exercised. Pending utilization of any proceeds from the exercise of warrants, the proceeds will be deposited in interest bearing accounts or invested in money market instruments, government obligations, certificates of deposits or similar short-term investment grade interest bearing investments.

MANAGEMENT'S DISCUSSION AND ANALYSIS
OR PLAN OF OPERATION

OVERVIEW

We provide hosted web-based collaboration solutions that enable organizations to establish Internet, Intranet, and email/collaboration services immediately and with little or no up-front capital investment. Our portal and IceMAIL collaboration software services are available on a monthly or annual subscription basis to small and medium-sized businesses and non-profit

and government organizations. We also provide consulting services to our larger enterprise and government customers including network infrastructure, enterprise email/collaboration, and Internet/Intranet portal implementation and support services. We offer pre-packaged and custom services, using proven best practices to help organizations define their online business objectives and quickly deploy their Internet, Intranet, and email/collaboration systems. Although most of our small to medium-sized business customers purchase and activate our solutions online, our professional services teams work closely with our government, non-profit and larger customers to deploy customized solutions. We also market an array of information technology services and third party computer hardware and software.

Our history and acquisition strategy has been key in our growth as a company. We began as a full service provider of computer systems and professional services to private sector corporations and to the federal government under a General Services Administration (GSA) schedule contract for computer systems and peripherals. Beginning in 2001, we began a series of strategic acquisitions which have resulted in our current business and

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operations, including:

- o in June 2001, we acquired the assets of Learning Stream, Inc., a provider of digital content streaming services, which coincided with the transition of our business model to a focus on e-learning. Learning Stream had developed custom streaming solutions which we believed were more efficient and effective than the solutions we had implemented at that time. We considered the software we acquired to be competitive because it helped remove the complexity and unnecessary cost from the implementation of the streaming technology,
- o in June 2003, we acquired all of the outstanding stock of Interlan Corporation, a provider of data communications and networking solutions for business, government, and education. Interlan provided technical services including presales design and consulting, installation, troubleshooting, and long term maintenance and support contracts,
- o in June 2003, we also acquired all of the outstanding stock of The Seven Corporation, a provider of network engineering services to commercial and government customers throughout the United States,
- o in October 2003, we acquired the software ownership rights and customers of Iplicity, Inc. of Virginia. Iplicity had developed a complete content management software platform based on open source architecture to run in any operating environment. In this transaction we acquired software licenses, source code, potential patents and trademarks, and
- o in May 2004 we acquired substantially all of the assets of DevElements, Inc. of Virginia, a professional IT consultancy firm that designs, develops and implements web-based productivity solutions for the customers. In this transaction we acquired software licenses, source code, potential patents and trademarks, as well as some cash and tangible assets.

We generate revenues from sales of software licenses and provision of software application services, application development and network management services and integrated technology, infrastructure solutions and third party hardware sales. As a result of the growth of our company both through acquisitions and organically, we significantly increased both our revenues and expenses during fiscal 2004. During fiscal 2005 we capitalized on our growth through these acquisitions to organically grow our company and introduce new products. As a result of this growth, and as described elsewhere herein, we anticipate that both revenues and expenses will continue to increase in future periods.

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We believe that the key factors to our continued growth and profitability include the following:

- o the introduction of our IceWEB Vista portal software which was released to general availability during June 2005. IceWEB Vista is a powerful tool for efficient website management, built upon open source architecture

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(.Net) that allows users to quickly, easily and affordably update their Web content and site structure,

- o the launch of IceMAIL, a packaged service that provides a network-hosted groupware, email, calendaring, and collaboration solution utilizing Microsoft Exchange 2003, the most widely used enterprise system available, which was released in December 2005. Customers will be able to leverage the full capabilities of Microsoft Exchange 2003 and Outlook without the initial implementation and maintenance costs associated with such an advanced system. We plan a launch of IceMAIL before the end of fiscal 2005,

- o raising approximately \$4 million of additional working capital to expand our marketing, support our growth and for an acquisition of an additional company in the software services group,

- o hiring additional qualified, technical employees, and

- o improving our internal financial reporting systems and processes.

While we launched the first of our new software offering during June 2005 and our second in December 2005, and the sale of these products are the focus of our business, we face a number of challenges in other areas which we believe are key to our growth, many of which are beyond our control. We have not identified any potential acquisition candidates and do not have any firm commitments for additional working capital as of the date of this prospectus, and we cannot assure you that we will be successful in either undertaking. While we recently hired a Chief Financial Officer and intend to implement upgrades to our internal systems, we face continuing difficulties in locating sufficient qualified technical personnel. Our company is located in the "Tech Corridor" of Northern Virginia and we compete with a number of companies for employees, many of which have been in business longer than we have and which are more attractive to prospective employees. Our inability to accomplish one or more of these key goals may limit our growth in future periods.

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RESULTS OF OPERATIONS

FISCAL YEAR ENDED SEPTEMBER 30, 2005 AS COMPARED TO FISCAL YEAR ENDED SEPTEMBER 30, 2004

The following table provides an overview of the our certain key factors of our result of operations for the fiscal year ended September 30, 2005 as compared to the fiscal year ended September 30, 2004:

| | Fiscal Year Ended | | \$ Change | % Change |
|-------------------------------|-----------------------|-----------------------|----------------|-------------|
| | September 30, 2005 | September 30, 2004 | | |
| Revenues | \$6,809,590 | \$ 6,662,652 | \$ 146,938 | +2.2% |
| Marketing and selling | 56,538 | 125,414 | \$ (68,876) | -5.5% |
| Research and development | 0 | 580,053 | \$ (580,053) | -100% |
| G&A expenses | 1,994,168 | 1,947,392 | \$ 46,776 | +2.4% |
| Total operating expenses | 2,884,566 | 3,656,610 | \$ (772,044) | -21.2% |
| Operating (loss) | (828,252) | (2,009,452) | \$ (1,181,200) | -58.8% |
| Net (loss) | \$ (903,508) | \$ (2,035,443) | \$ (1,131,935) | -55.6% |

Other key indicators:

| | | |
|-------------|-------------|-------------|
| Fiscal 2005 | Fiscal 2004 | % of change |
|-------------|-------------|-------------|

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| | ----- | ----- | ----- |
|---|-------|-------|--------|
| Cost of sales as a percentage of revenues | 69.8% | 75.3% | -5.5% |
| Gross profit margin | 30.2% | 24.7% | +5.5% |
| G&A expenses as a percentage of revenues | 29.3% | 29.3% | +0.1% |
| Total operating expenses as a percentage of revenues | 42.4% | 54.9% | -12.5% |

Revenues

For the year ended September 30, 2005, we reported a modest increase in revenues of \$6,809,590 as compared to revenues of \$6,662,652 for the prior year ended September 30, 2004, an increase of approximately 2.2%.

Cost Of Sales

Our cost of sales consists of products purchased for resale, salaries of technical personnel, third party contractors, hosting and sales commissions. For the year ended September 30, 2005, cost of sales was \$4,753,276, or approximately 69.8% of revenues, compared to \$5,015,494, or approximately 75.3% of revenues, for the year ended September 30, 2004. The decrease in costs of sales as a percentage of revenue and the corresponding increase in our gross profit margin for fiscal 2005 as compared to fiscal 2004 was the result of an increase during the year in commission revenue as a percentage of total revenue compared to infrastructure and hardware revenue.

Total Operating Expenses

Our total operating expenses decreased approximately 21.1% for the year ended September 30, 2005 as compared to the year ended September 30, 2004. These decreases include:

Marketing and Selling. For the year ended September 30, 2005, marketing and selling costs were \$56,538 as compared to \$125,414 for the year ended September 30, 2004, a decrease of \$68,876 or approximately 54.9%. These decreases were the result of a reduction in marketing personnel, trade show events, online web marketing, advertising and print advertising during fiscal 2005.

Research and development. Our research and development expense consists primarily of personnel costs related to the development of the software products. For the year ended September 30, 2005, research and development expenses were \$0 as compared to \$580,053 for the year ended September 30, 2004. The research and development expenses in fiscal 2004 were related to efforts to develop our Vista software and IceMAIL hosting services. Subsequent to September 30, 2005 we have capitalized approximately \$157,000 in research and development expenses related to our IceMAIL and Vista products.

General and administrative expense. For the year ended September 30, 2005, general and administrative expenses were \$1,994,168 as compared to \$1,947,392 for the year ended September 30, 2004, an increase of \$46,776 or approximately 2.4%. These increased general and administrative expenses reflect increases in personnel costs and other fixed expenses resulting from inflation. Like many companies that grow through mergers and acquisition, we have recently experienced attrition in our technical consulting division. This attrition has not presently impacted client delivery as there is skill set overlap in many areas. As we continue to implement our business strategies, we expect general and administrative expenses to potentially decrease as a percentage of sales due to the process efficiencies we have already put in place. At this time, we do

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not anticipate any significant changes in the number of employees through hiring or firing practices, however, any additional acquisitions could result in increased general and administrative expenses.

Depreciation expense. Depreciation expense is provided by use of the straight-line method over the estimated useful lives of the assets. The property and equipment are stated at cost. For the year ended September 30, 2005, depreciation expense was \$51,096 as compared to \$52,716 for the prior year ended September 30, 2004.

Amortization expense. Amortization expense is related to the customer relationships which are intangible assets that we generated through our acquisitions of DevElements, Inc. and Iplicity, Inc. The decrease in amortization expense of \$185,671, or approximately 19.6%, for fiscal 2005 as compared to fiscal 2004 reflects previous amortizations of this intangible asset.

Rental Revenue

During fiscal 2005 and fiscal 2004 we sub-leased excess space at our principal executive offices to third parties. Rental revenue represents revenue from this sub-lease arrangement. Rental revenue for fiscal 2005 decreased \$15,604, or approximately 44.7%, from fiscal 2004 as a result of the termination of the sub-leasing arrangement in mid-fiscal 2005. As a result of our move to other offices we will not have comparable revenue in future periods.

Interest Expense

Interest expense consists primarily of the amounts accrued on the notes payable to John R. Signorello, our CEO, and a third party stockholder as described in Note 5 of the Notes to Consolidated Financial Statements and the interest paid to Comerica Bank on the line of credit as described in Note 6 of the Notes to Consolidated Financial Statements, appearing elsewhere herein. For the year ended September 30, 2005, interest expense was \$94,540 as compared to \$60,879 for the year ended September 30, 2004. This increase of approximately 55.3% is the result of increased borrowings during fiscal 2005.

Income Taxes

Because we incurred net operating losses in the years ended September 30, 2005 and 2004, we paid no federal, state or foreign income taxes in those periods. We have also not recognized any tax benefits for the related tax operating loss carry forwards and may not until we conclude that such benefits will be utilized.

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Overall, our net (loss) was \$(903,508) or \$(0.15) per share for the fiscal year ended September 30, 2005 compared to \$(2,034,443) or \$(0.41) for the year ended September 30, 2004.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity is the ability of a company to generate funds to support its current and future operations, satisfy its obligations and otherwise operate on an ongoing basis. The following table provides certain selected balance sheet comparisons between September 30, 2005 and September 30, 2004:

| September 30, 2005 | September 30, 2004 | \$ of Change | % of Change |
|-----------------------|-----------------------|-----------------|----------------|
| ----- | ----- | ----- | ----- |

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| | | | | |
|--------------------------------|---------------|---------------|--------------|---------|
| Working capital (deficit) | \$ 319,137 | \$(1,049,557) | \$ 1,368,694 | +130.4% |
| Cash | \$ 557,175 | \$ 178,781 | \$ 378,394 | +211.6% |
| Accounts receivable, net | \$ 1,577,460 | \$ 1,062,707 | \$ 514,753 | +48.4% |
| Total current assets | \$ 2,221,916 | \$ 1,241,488 | \$ 980,428 | +79.0% |
| Property and equipment, net .. | \$ 259,852 | \$ 86,251 | \$ 173,601 | +201.3% |
| Intangibles, net | \$ 68,525 | \$ 822,764 | \$ (754,239) | -91.7% |
| Deferred financing costs, net | \$ 180,000 | \$ 0 | \$ 180,000 | +100.0% |
| | ----- | ----- | ----- | |
| Total assets | \$ 2,788,263 | \$ 2,208,473 | \$ 579,790 | +26.3% |
| Accounts payable | \$ 904,910 | \$ 1,233,708 | \$ (328,798) | -26.7% |
| Accrued expenses | \$ 37,488 | \$ 152,577 | \$ (115,089) | -75.4% |
| Advances/notes related party . | \$ 86,001 | \$ 424,461 | \$ (338,460) | -79.7% |
| Preferred stock to be issued . | \$ 408,836 | \$ 0 | \$ 408,836 | +100.0% |
| Total current liabilities | \$ 1,902,779 | \$ 2,291,045 | \$ (388,266) | -16.9% |
| Note payable - related parties | \$ 215,625 | \$ 0 | \$ 215,625 | +100.0% |
| | ----- | ----- | ----- | |
| Total liabilities | \$ 2,118,404 | \$ 2,291,045 | \$ 172,641 | -7.5% |
| Accumulated (deficit) | \$(6,500,655) | \$(4,597,375) | \$ 1,903,280 | +41.4% |
| Stockholders' equity (deficit) | \$ 669,859 | \$ (82,572) | \$ 752,431 | +911.2% |

Net cash used in operating activities was \$920,515 for the year ended, 2005 as compared to net cash provided by operating activities of \$794,861 for the year ended September 30, 2004. The increase in cash used in operations is primarily due to a decrease in accounts payable and accrued expenses.

Net cash used in investing activities for the year ended September 30, 2005 was \$233,244 as compared to net cash provided by investing activities of \$27,454 for the fiscal 2004. During fiscal 2004 we acquired two companies and in connection therewith recognized cash provided by investing activities of \$37,637 which was offset by \$10,183 of property and equipment purchases during fiscal 2004. In fiscal 2005 we purchased equipment and software which represented the cash used in investing activities for the year and we did not have any acquisitions or similar transactions during the year which provided cash from investing activities. Net cash provided by financing activities for fiscal 2005 was \$1,532,133 as compared to \$841,874 for fiscal 2004. The primary reason for the increase is an increase of \$690,259 in proceeds from the sale of equity securities during fiscal 2005 as compared to fiscal 2004.

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At September 30, 2005 we had an accumulated deficit of \$6,500,655 and the report from our independent registered public accounting firm on our audited financial statements at September 30, 2005 contained an explanatory paragraph regarding doubt as to our ability to continue as a going concern as a result of our net losses in operations. We reported a net loss of \$903,508 for fiscal 2005 and there are no assurances that we will report net income in any future periods.

Historically, our revenues have not been sufficient to fund our operations and we have relied on capital provided through the sale of equity securities, a bank line of credit and loans from related parties. At September 30, 2005 we had cash on hand of \$557,175 and working capital of \$319,137. At September 30, 2005 we owed \$461,269 under our line of credit with Comerica Bank, which is reflected as a current liability, and we did not have any ability to borrow any additional sums under this credit facility. Subsequent to September 30, 2005 we entered into a one year receivable factoring agreement with Sand Hill Finance, LLC under which we can sell certain accounts receivable to the lender on a full recourse basis at 80% of the face amount of the receivable up

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to an aggregate of \$1 million. We agreed to pay Sand Hill Finance, LLC an annual commitment fee of \$10,000 and a monthly finance fee of 2% of the average daily balance under the line. We granted Sand Hill Finance, LLC a blanket security interest in our assets and agreed to refrain from certain actions which the line is outstanding. We used availability under this agreement to satisfy our outstanding obligation to Comerica Bank and the remainder of availability under this line will provide us with additional working capital.

While we do not have any working capital commitments, we do not presently have any external sources of working capital other than what may be available under the factoring agreement. Our working capital needs in future periods primarily on the rate at which we can increase our revenues while controlling our expenses and decreasing the use of cash to fund operations. Additional capital may be needed to fund acquisitions of additional companies or assets, although we are not a party to any pending agreements at this time and, accordingly, cannot estimate the amount of capital which may be necessary, if any, for acquisitions.

As long as our cash flow from operations remains insufficient to completely fund operations, we will continue depleting our financial resources and seeking additional capital through equity and/or debt financing. In March 2005 we sold shares of our Series A Convertible Preferred Stock and in December 2005 we sold shares of our Series B Convertible Preferred Stock to the same purchaser. The designations of these shares included a restriction that so long as the shares are outstanding, we cannot sell or issue any common stock, rights to subscribe for shares of common stock or securities which are convertible or exercisable into shares of common stock at an effective purchase price of less than the then conversion value which is presently \$0.60 per share for the Series A Convertible Preferred Stock and \$0.2727 for the Series B Convertible Preferred Stock. Under the terms of the Series B Convertible Preferred Stock transaction we also agreed not to issue and convertible debt or preferred stock. Finally, under the terms of the financing agreement with Sand Hill Finance, LLC we agreed not to incur any additional indebtedness other than trade credit in the ordinary course of business. These covenants may limit our ability to raise capital in future periods. There can be no assurance that acceptable financing can be obtained on suitable terms, if at all. Our ability to continue our existing operations and to continue growth strategy could suffer if we are unable to raise the additional funds on acceptable terms which will have the effect of adversely affecting our ongoing operations and limiting our ability to increase our revenues and maintain profitable operations in the future. If we are unable to secure the necessary additional working capital as needed, we may be forced to curtail some or all of our operations.

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CRITICAL ACCOUNTING POLICIES

Financial Reporting Release No. 60, which was released by the U.S. Securities and Exchange Commission, encourages all companies to include a discussion of critical accounting policies or methods used in the preparation of financial statements. Our consolidated financial statements include a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. Management believes the following critical accounting policies affect the significant judgments and estimates used in the preparation of the financial statements.

Revenue Recognition - revenues are recognized at the time of shipment of the respective products and/or services. Our company includes shipping and handling fees billed to customers as revenues. Costs of sales include outbound freight. Licenses and software are billed as services are rendered on a biweekly schedule.

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Use of Estimates - Management's Discussion and Analysis or Plan of Operations is based upon our unaudited consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, management evaluates these estimates, including those related to allowances for doubtful accounts receivable and the carrying value of inventories and long-lived assets. Management bases these estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis of making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

RECENT CAPITAL RAISING TRANSACTION

On December 28, 2005, we consummated a Preferred Stock Purchase Agreement and related agreements with Barron Partners LP. Under the terms of these agreements we issued Barron Partners LP, an accredited investor, 1,833,334 shares of our Series B Convertible Preferred Stock and Common Stock Purchase Warrants "D", "E" and "F" to purchase an aggregate of 2,250,000 shares of our common stock at exercise prices ranging from \$2.00 to \$9.60 per share, for an aggregate purchase price of \$ 500,000. We are using these proceeds for general working capital. Barron Partners LP had previously purchased shares of our Series A Convertible Preferred Stock in a transaction which closed in March 2005

We received net proceeds of approximately \$408,000 after payment of commissions of \$25,000 and other expenses of the offering. The proceeds were paid to us through the satisfaction of a liability to Barron Partners LP for funds advanced to us in September 2005. We also issued Liberty Company LLC, a broker-dealer, a Common Stock Purchase Warrant "G" exercisable into 25,000 shares of our common stock with an exercise price of \$1.00 per share as additional compensation for its services. The proceeds are being used for general working capital. The transaction was exempt from registration under the Securities Act of 1933 in reliance on an exemption provided by Section 4(2) of that act.

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Under the terms of the Preferred Stock Purchase Agreement, we agreed:

- o that all convertible debt in our company would be cancelled and that for a period of three years from the closing date we will not issue any convertible debt or preferred stock. In addition, we agreed to cause all reset features related to any shares of our outstanding common stock to be cancelled and for a period of three years from the closing date to refrain from entering into any transactions that have reset features,

- o to maintain a majority of independent directors on our Board of Directors, and that these independent directors will make up a majority of the audit and compensation committees of our Board. If at any time we should fail to maintain these independent majority requirements, we are required to pay Barron Partners LP liquidated damages of 24% of the purchase price of the securities (\$120,000) per annum, payable monthly in kind,

- o that if within 24 months from the closing date we consummate the sale of debt or equity securities with a conversion price less than the then effective conversion price of the Series B Convertible Preferred Stock we will

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make a post-closing adjustment in the conversion price of the Series B Convertible Preferred Stock to such lower conversion price,

o that for a period of three years all employment and consulting agreements must have the unanimous consent of the compensation committee of our Board, and any awards other than salary are usual and appropriate for other officers, directors, employees or consultants holding similar positions in similar publicly held-companies,

o that for a period of two years from the closing we will not enter into any new borrowings of more than twice as much as the sum of EBITDA from recurring operations over the past four quarters, subject to certain exceptions,

o that for long as Barron Partners LP holds any of the securities we will not enter into any subsequent financing in which we issue or sell any debt or equity securities with a floating conversion price or containing a reset feature, and

o that we will submit a proposal at our next annual meeting of stockholders to amend our Certificate of Incorporation to require the consent of the holders of a designated percentage of a designated class of our securities to waive or amend the terms of any rights, options and warrants approved by our Board.

Mr. John R. Signorello, our CEO, agreed not to sell any shares of our common stock that he many own in excess of 1% per quarter or at a price of less than \$3.00 per share for a period ending August 30, 2007, and that the earliest any other insiders could sell their shares would be beginning two years from the closing date.

We granted Barron Partners LP a right of first to participate in any subsequent funding we may undertake on a pro rata basis at 94% of the offering price.

We have agreed to file a registration statement with the Securities and Exchange Commission within 30 days to register for resale the shares of common stock issuable upon the possible conversion of the Series B Convertible Preferred Stock and the exercise of the warrants, and to use our best efforts to cause such registration statement to be declared effective within 120 days from the closing date. We have also granted Barron Partners LP demand registration rights covering these securities, as well as piggy-back registration rights for a period of two years from the closing date. We will pay all costs associated with these registration statements and have indemnified Barron Partners LP with respect thereto for any losses or claims related to material misstatements or material omissions by us in the registration statement(s).

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OUR BUSINESS

OVERVIEW

We are a diversified technology company headquartered in Herndon, Virginia, which was founded in 2000 and became public in 2002 through a reverse merger. While our business plan has been in evolution since that time, our focus has consistently remained on enabling governmental organizations and small to medium size businesses to independently manage, create, publish and deliver content easily and affordably. Our products and services are used by organizations in both the public and private sectors with large, dispersed audiences of customers, employees, or other trading or strategic partners. Through internal software development and a series of acquisitions, we have

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developed a suite of robust, scalable content creation, management, publication and delivery tools that can be implemented on any website, as well as e-learning content and customized e-learning portals. Our goal is to make this technology available and affordable and to open up the world of independent web management and publishing to any organization. Complementing these products is our hosted e-mail solution, IceMAIL. We also offer consulting and product support services on a project-by-project basis. In addition to our proprietary software and professional services, we also market an array of information technology services and third party computer hardware and software.

Our solutions are centered on knowledge based support, enabling customers to increase organizational efficiency by converging knowledge based information with easy to manage websites and e-learning portals. Going forward, we intend to leverage our expertise in content management, creation and delivery, and our e-learning portal framework, to develop a Smart Enterprise Suite ("SES") that extends beyond digital content to include dynamic human intelligence for greater information sharing and organizational efficiency across the extended enterprise. According to the Gartner Group, an SES "covers enterprise needs for content management, knowledge management and collaboration, and supports the extended virtual workplace - inside and between enterprises. The SES combines the functionality of portal, collaborative and content management technologies, and delivers these in an integrated suite; provides a broad foundation to support knowledge or information work within an enterprise, or between groups in different enterprises, and may be considered the platform for knowledge management; and focuses on support for unstructured work processes, but through portal-based integration with business applications can provide a comprehensive digital or electronic workplace." Our objective is to provide an affordable SES solution for governmental, association and small to medium size business customers.

OUR PRODUCTS AND SERVICES

Our products and services are designed to provide customers with a comprehensive view of their core business, promote better cross pollination of strategies and objectives between development, sales, marketing and service organizations, and guide strategic planning efforts to meet key corporate objectives of profitability and growth. These products form the basis of our emerging SES. The two key components currently consist of:

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ICEWEB VISTA

This is a powerful tool for efficient website management, built upon open source architecture (.Net) that allows users to quickly, easily and affordably update their Web content and site structure. With IceWEB Vista, users can manage, update, control and publish new content for Web sites anytime and anyplace. Among the many advantages of IceWEB Vista is the ability to easily, quickly and affordably deploy Web content as well as to control who can edit, access and view content. IceWEB Vista eliminates the costs and constraints of utilizing "third party" vendors for website management. With IceWEB Vista organizations can reduce the cost of managing records and documents, and extend the access and power of information to members, customers, or other site users, while maintaining data security. IceWEB Vista empowers users with advanced membership and profile management, a revamped HTML publisher, and more advanced workflow and versioning capabilities. In addition, our mailing list management tool enhances the ability of users to stay in contact with clients or members. IceWEB Vista's single sign-on support enables users to easily access records and documents through a customized interface.

We released the IceWEB Vista portal software solution during the third

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quarter of fiscal 2005. We believe that IceWEB Vista is a major step forward in terms of usability by eliminating several complexities that existed in previous versions of the product. IceWEB Vista unified our earlier offering, IceWEB CMS, and a number of new application modules including HTML Publishing Tool, News Content Management, Advanced Mailing List Manger and Custom Forms Creator to provide one product from the end user's perspective. We believe IceWEB Vista provides the end user with powerful tools to manage not only text but also rich media in a "what you see is what you get" or WYSIWYG environment. IceWEB Vista also provides comprehensive and enterprise wide portal deployment features in a single turnkey solution.

ICEMAIL

In December 2005 we launched IceMAIL, a packaged service that provides a network-hosted groupware, email, calendaring, and collaboration solution utilizing Microsoft Exchange 2003, the most widely used enterprise system available. Customers will be able to leverage the full capabilities of Microsoft Exchange 2003 and Outlook without the initial implementation and maintenance costs associated with such an advanced system. In addition to providing hosted Exchange services, IceMAIL will have a substantial focus on providing wireless PDA/Smart Phone synchronization services that enable our customers to have everything in Outlook/Exchange available while traveling away from their office. IceWEB will be a single-source provider of wireless PDA/Smart Phones, GoodLink or Blackberry software, and the cellular carrier services through reseller arrangements with those companies.

Our goal is to leverage existing technologies from several software and hardware manufacturers and combine them with customized software systems to make ordering and using our Internet hosted applications easy and quick. Most of the solutions we will offer are somewhat common place for large organizations, but cost prohibitive for small and medium sized businesses to manage much less procure the initial technology. We will seek to leverage our expertise in large-scale enterprise systems to build our service offerings that will share these systems across numerous small to medium-sized business customers. We believe that this scale of economy will allow us to offer our services to small to medium-sized business customers at a fraction of the cost would pay if an individual small to medium-sized business customer were to deploy it themselves.

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IceMAIL is based on the advanced Microsoft Exchange 2003 platform which provides industry-leading features such as calendars, group scheduling, contact management, task management, notes, and shareable public folders. Using the latest in network hosting, wireless, and Internet technologies, IceMAIL will be accessible from anywhere on the Internet via Microsoft Outlook 2003 or a web-browser. For the true "road warrior", we will also offer wireless handheld PDA access using a Handspring Treo, RIM Blackberry, Windows PocketPC, or Smart Phone devices.

LEARNINGSTREAM.COM

LearningStream.com is an online business education portal that offers pay-per-view online classes to mid-level managers seeking to update their management and project skills. Additionally, LearningStream.com has a user interface that enables experts and instructional designers to create and publish courses online. The courses have to pass scrutiny and upon acceptance by LearningStream.com staff will be published to the site. We provide the hosting and streaming and shares in the revenue generated by the content providers. Business professionals can choose among many different subjects such as making presentations, managing people and learning software applications from training developers such as Fred Pryor Seminars, CareerTrack and Evelyn Woods.

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CUSTOM SMART ENTERPRISE SOLUTIONS

Through the acquisition of assets of DevElements in May 2004, we increased our capabilities to provide a custom smart enterprise solution, as DevElements has experience developing and deploying complex web-based business solutions in over 27 languages, primarily for Fortune 1000 businesses with offices in multiple countries. By leveraging the core competencies acquired by us through DevElements, we can assist organizations with:

- Custom Application/Software Development: full, life-cycle web development of applications that improve everyday business tasks & processes.
- Portal Integration: deploying, customizing and maintaining portal frameworks, including custom development of applications to assist with single sign-on authentication and extending the framework to meet multiple language needs.
- Collaboration: integration of today's hottest collaboration packages, from embedded awareness in applications to custom "Webinar" reservation management tools.
- Extension of Legacy Systems: extension of well-documented and developed legacy systems to the web for either secured or public access.

STORAGE AND DISTRIBUTION

We offer a competitive level of data security, backup and disaster recovery in order to ensure the integrity of our clients' data. We have redundant production services, a three-tier development cycle, tape backups and redundant connectivity.

CONSULTING SERVICES

Our consulting staff has years of experience in providing custom, rich media solutions. Our consulting services include personalized project management, multimedia development, synchronization of media assets, application design and development, software integration, instructional design, graphic design, foreign language translations and delivery methods

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SUPPORT AND MAINTENANCE SERVICES

We provide engineering and technical support to both government and commercial organizations. These services include everything from security and network analysis to full network technology refreshment and deployment. We also provide support and maintenance to ensure that its solutions are deployed correctly and continue to operate efficiently into the future.

THIRD PARTY HARDWARE

Through open market sales in the private sector and primarily through United States General Services Administration (GSA) Schedule sales to the federal government under GSA Schedules held by certain of our subsidiaries, we sell a broad array of hardware, including large uninterruptible power supplies and other power equipment through our Integrated Power Solutions, Inc. subsidiary.

TECHNOLOGY

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We currently have 20 engineers on staff with expertise in Microsoft.NET, IBM Domino and Java technologies. In addition, we have developed relationships with Sun Microsystems, RSA Security, Cisco Systems, SonicWall, Good Technologies and SurfControl Incorporated, enabling enhanced product and service solutions that combine the expertise of our engineering staff with the product offerings of some of the leaders in the technology space. This is significant for our growing customer base in the integration and customized software and services sector of our business.

Our software is designed for Microsoft's Windows Operating Systems and applications that use Microsoft's SQL 7 database software. The majority of our applications are based on client-server technology. The authoring and content management application software has been developed using a combination of C++, ColdFusion, Javascript, ASP, VBscript, Java and Flash. Since a majority of the processing is done on the server, clients only need a browser to author and manage their web content.

We surmounted a significant product development challenge by leveraging the capabilities of the Microsoft.NET development environment and integrating many of the disparate technologies driving our core software platforms. All of our products utilize their original technology in one form or another. By leveraging the code of existing products, we have been able to decrease product development costs, shorten time to market and realize revenues from new products quickly. This has also provided a significant advantage to our customers, enhancing the stability of new software versions and new product offerings and reducing the effort required to upgrade or deploy our software.

SALES AND MARKETING

We sell our products and services through our direct sales force, online and through strategic and channel partners. Our direct sales process typically includes a demonstration of our product capabilities followed by one or more detailed technical reviews. Our employees utilize our software to generate leads, sales, demos and references. Our websites all run on IceWEB CMS, and our training resides on our intranet education portal.

Our online sales strategy includes generating leads through search engine optimization as well as through pay-per-click venues such as Overture, Google and KnowledgeStorm. Going forward, we intend to market online to web forums, chat rooms and user groups, critical components to "buzz" marketing. Our training classes are also being used as loss leaders to open doors to large

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government and commercial customers. During fiscal 2006 we expect to implement a variety of other online marketing initiatives as well, including event bulletin boards and expert discussions, online surveys and questionnaires to gather valuable feedback and encourage customer communications, focused user groups, referral programs, membership communities and services that revolve around our offerings, and the development and support of customer evangelists that promote, and are promoted by, our products.

Our indirect sales channel strategy is to form additional relationships with systems integrators, value-added resellers and original equipment manufacturers to resell our products and services. We also plan to generate leads from a variety of other sources, such as businesses seeking partners to develop Web-based applications. Because our products are relatively inexpensive, easy to understand, sell and use, they lend themselves to distribution by third parties such as audio/video production companies, business centers and

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hosting/delivery vendors.

We complement our sales initiatives with a variety of marketing programs to build market awareness of our brand name and products, and to attract potential customers. These marketing programs include market research, product and strategy updates with customers and industry analysts, public relations activities, radio and print advertising, direct marketing and relationship marketing programs, webinars, seminars, trade shows and speaking engagements. Our marketing organization also produces marketing materials in support of prospective sales to new customers, including brochures, data sheets, white papers, presentations and demonstrations.

RESEARCH AND DEVELOPMENT

In addition to our focus on subscription-based "software as a service" offerings, we are engaged in a comprehensive research and development plan to integrate our portal and email/collaboration offerings into the next generation of online applications. This next generation of online hosted application services will focus on integrating "traditional email" and portal systems into an integrated Smart Enterprise Suite with both applications running on both Internet/Intranet as well as synchronized wireless/PDA systems. We anticipate that we will launch these product before the end of fiscal 2005. For the fiscal years ended September 30, 2005 and 2004 we spent \$0 and \$580,053, respectively, on research and development.

INTELLECTUAL PROPERTY

Our success depends in part on our ability to protect our intellectual property. The source codes, object codes, and documentation related to our products are all proprietary to us and as to which copyright in favor of our company arose from the date of creation of the products or the date on which the products were assigned to us, whichever is later. We also rely on common law rights to our trademark and service mark "IceWEB" in both block letters and stylized form. To protect our proprietary rights, we rely generally on copyright and trade secret laws, confidentiality agreements with employees and third parties, and agreements with consultants, vendors and customers, although we have not signed such agreements in every case. Despite such protections, a third party could, without authorization, copy or otherwise obtain and use our intellectual property.

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It is also possible that our competitors will adopt product or service names similar to ours, thereby impeding our ability to build brand identity and possibly leading to customer confusion. We can give no assurance that our agreements with employees, consultants and others who participate in development activities will not be breached, or that we will have adequate remedies for any breach, or that our trade secrets will not otherwise become known or independently developed by competitors. There can be no assurance that we will be able to adequately protect our trade secrets. Third parties may assert infringement claims against us or against third parties upon whom we rely and, in the event of an unfavorable ruling on any claim, we may be unable to obtain a license or similar agreement to use technology that we rely upon to conduct our business.

In the future we may pursue copyright protection of our source codes, object codes and documentation as well as the registration of certain of our trademarks and service marks in the United States. In general, there can be no assurance that our efforts to protect our intellectual property rights through copyright, trademark and trade secret laws will be effective to prevent misappropriation of our content. Our failure or inability to protect our

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proprietary rights could materially adversely affect our business, financial condition and results of operations.

COMPETITION

Our competitors include portal vendors, application service providers, software vendors, systems integrators and information technology consulting service providers who offer some or all of the same products as we do to the small to medium sized business and government markets. Our competitors, particularly for larger customers within our target markets, include Plumtree, Vignette, Hummingbird, Websphere, Oracle, SAP and Microsoft's content management system. Our competitive strategy is to undercut the pricing model of our competitors while delivering a higher value to customers and building brand name recognition for our company and our products. We face significant competition from these and other companies, most of which have greater brand recognition, are better capitalized than us and can obtain financing on more favorable terms. We may never be able to successfully compete in our target market.

In addition, there are relatively low barriers to entry into our business. We do not believe our proprietary technology would preclude or inhibit competitors from entering our markets. We anticipate that new entrants will try to develop competing products and services as well as new forums for conducting eCommerce that could be deemed competitors. We believe we may be able to compete successfully by relying on our established infrastructure, marketing strategies, systems and procedures, by continuing to add additional products and services in the future, by periodically revising our methods of doing business and by continuing its expansion into international markets where we believe there is an overall lower level of competition.

EMPLOYEES

As of December 31, 2005, we employed a total of 32 employees, all of whom work full time. We also use the full-time services of 12 consultants in areas of network consulting. We are not a party to any collective bargaining agreements with any unions, and we believe that the overall relations with our employees are satisfactory.

PROPERTY

In November 2005, we entered into a three year lease for approximately 7,900 square feet of office space located in the same building in which our principal executive offices had been located. This new lease provides for annual base rental of approximately \$202,000 which escalates to approximately \$215,000 annually in the third year of the lease term. We are also responsible for our pro-rata share of certain pass through costs. We have the option to renew this lease for one additional five year term and we have a right of first refusal to lease as additional approximately 7,200 square feet of adjoining office space should it become available.

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We also rent 2,000 square feet of office space on a month-to-month basis at 1455 Pennsylvania Avenue, NW, Washington D.C. at a monthly cost of \$2,100.

LEGAL PROCEEDINGS

In October 2005 two related lawsuits have been filed against us in the Circuit Court of Fairfax County, Virginia, captioned Bonnie Edenfield vs. IceWEB, Inc., et al., Chancery No. CH 2005 4303; and Christopher MacDonald vs. IceWEB, Inc., et al., Chancery No. CH 2005 4304. Both suits are brought by

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former shareholders of DevElements, Inc., the assets of which were purchased by us. Ms. Edenfield and Mr. MacDonald were parties to the asset purchase agreement with DevElements. The plaintiffs seek money damages from us in the aggregate amount of \$18,000 for alleged breach of the asset purchase agreement, rights to exercise options for 100,000 shares of our common stock and damages related to stock options. We have filed a response and intend to vigorously defend this litigation as we believe the litigation is without merit.

OUR HISTORY

We were originally formed under the laws of the State of Delaware in February 1969. For many years, we were a wholesaler of custom one, two, three and four-color processed commercial printing, as well as disposable and durable office equipment including stock paper, fax paper, fax and copy machines, computers, file cabinets and safes. We conducted our business throughout the United States of America and Puerto Rico from our headquarters in New York.

In March 1999, we changed the focus of our business and closed a transaction by which we acquired 100% of the outstanding capital stock of North Orlando Sports Promotions, Inc., a privately held Florida corporation. From 1999 until July 2001, we operated a variety of Internet-related services, however, we were unable to generate positive cash flow from these Internet-related businesses.

In May 2001, we executed an Agreement and Plan of Reorganization and Stock Purchase Agreement with Disease S.I., Inc. Under the terms of the agreement, we acquired 100% of the issued and outstanding stock of Disease S.I., Inc. in exchange for 750,000 shares of our common stock. The transaction was accounted for as a reverse acquisition under the purchase method for business combinations. Accordingly, the combination of the two companies was recorded as a recapitalization of Disease S.I., Inc., pursuant to which Disease S.I., Inc. was treated as the continuing entity. Disease S.I., Inc. was a developmental stage biopharmaceutical clinical diagnostics company planning to employ a broad array of technologies to detect, identify and quantify substances in blood or other bodily fluids and tissues. It intended to derive revenues from patent sub-licensing fees, royalties from pharmaceutical sales, appropriate milestone payments and research and development contracts.

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Following completion of the acquisition of Disease S.I., Inc., it became apparent to us that it would be in our best long-term interest that the Internet operations be conducted apart from the biopharmaceutical clinical diagnostics operations. On July 24, 2001, we sold a former officer and director 100% of our subsidiary North Orlando Sports Promotions, Inc., in exchange for the assumption of all liabilities related to North Orlando Sports Promotions, Inc. and its operations estimated at approximately \$112,000, and which included the forgiveness of \$91,500 in accrued compensation. Included in the sale along with the capital stock of North Orlando Sports Promotions, Inc. were fixed assets, rights to several domain names and various contractual rights and obligations.

On November 27, 2001, we acquired 9,050,833 shares of the common stock of Healthspan Sciences, Inc., a privately held California corporation in exchange for 5,000 shares of our common stock in a private transaction exempt from registration under the Securities Act of 1933 in reliance on Section 4(2) of that act. This agreement was rescinded on March 21, 2002. Pursuant to the rescission, Healthspan Sciences, Inc. returned all 5,000 shares of our common stock issued in the exchange and we returned all 9,050,833 shares of Healthspan Sciences, Inc. we had received.

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On March 21, 2002, we executed an Agreement and Plan of Merger with IceWEB Communications, Inc., a Delaware corporation and its stockholders. Founded in 2000, IceWEB Communications, Inc. enabled interactive communications and education on the web. In June 2001, it had acquired the assets in bankruptcy of Learning Stream, Inc., a provider of streaming services. Pursuant to the agreement, each of the 22,720,500 shares of common stock of IceWEB Communications, Inc. issued and outstanding immediately prior to the merger were converted into the right to receive 0.13375 shares of our common stock, for an aggregate of 303,888 shares of common stock. Each of the warrants to purchase an aggregate of 680,125 shares of IceWEB Communications, Inc. common stock issued and outstanding immediately prior to the merger were converted into the right to receive one warrant to purchase 0.13375 shares of our common stock upon exercise of said warrant.

In June 2003, we acquired 100% of the capital stock of Interlan Communications, Inc., a privately held corporation, in exchange for 25,000 shares of our common stock. In June 2003, we also acquired 100% of the capital stock of Seven Corporation in exchange for 37,500 shares of our common stock and cash consideration of \$123,000.

In October 2003, we acquired 19% of the capital stock of Iplicity, Inc. of Virginia, together with substantially all of its assets including software licenses, source code, potential patents and trademarks for a combined stock and cash value of approximately \$632,000 which included the issuance of 191,381 shares of our common stock and cash consideration of \$65,500.

In May 2004, we acquired substantially all of the assets of DevElements, Inc. of Virginia, including software licenses, source code, potential patents and trademarks, cash, hardware, and equipment. As consideration for the purchase of the assets, we paid DevElements \$100,000 and agreed to the assumption of liabilities up to an aggregate of \$150,000. In exchange for the 19% interest in DevElements, we issued to the shareholders of DevElements 187,500 shares of our common stock and options to purchase 187,500 shares of common stock exercisable at a price of \$27.20 per share and expiring May 13, 2009. We issued to the stockholders options to purchase 6,250 shares, which were contingently exercisable upon the satisfaction of certain performance criteria. The performance criteria, which required contracts, task orders and other work assignments involving billing of at least \$840,000 during the six-month period ending November 13, 2004, was not met and the options were cancelled.

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On October 18, 2004, we entered into a non-binding letter of intent to acquire 100% of the issued and outstanding stock of Plan Graphics, Inc. The transaction was subject to approval by the Plan Graphics, Inc. shareholders, and certain terms and conditions, including terms and conditions which are customary to this type of transaction. On April 29, 2005 the letter of intent expired with a definitive agreement having been executed or all conditions precedent to the closing having been completed.

MANAGEMENT

DIRECTORS AND EXECUTIVE OFFICERS

| Name | Age | Positions |
|--------------------|-----|--------------------------------------|
| ---- | --- | ----- |
| John R. Signorello | 39 | Chairman and Chief Executive Officer |
| G. Anthony Munno | 43 | President |
| Brian E. Crooks | 52 | Chief Financial Officer |

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| | | |
|-----------------------|----|----------|
| Harold F. Compton (1) | 57 | Director |
| Raymond Pirtle (2) | 64 | Director |
| Joseph L. Druzak (1) | 53 | Director |
| Jack Bush(1) | 70 | Director |

(1) Member of the Compensation Committee

(2) Member of the Audit Committee

John R. Signorello. Mr. Signorello has served as Chairman of the Board and CEO since March 2000. From 1991 until September 1997, Mr. Signorello served as the Chief Executive Officer of STMS - "Solutions That Make Sense" - a private technology company he founded that specialized in computer networks, systems integration and information technology. In 1996, STMS was ranked the 17th fastest growing technology company in America by The National Technology Council's "The Fast Five Hundred". In September 1997, the company was acquired by Steelcloud (Nasdaq: SCLD), and Mr. Signorello remained as Vice President of Sales and Marketing until November 1998. From 1998 through 2000, Mr. Signorello served as a Director for a publicly traded Internet Venture Fund. Mr. Signorello is an accomplished musician, and serves as a principal in New York City Lights Entertainment. Mr. Signorello received a B.B.A. in Marketing from Radford University in 1989.

G. Anthony Munno. Mr. Munno has served as our President since October 2004. From August 2003 until being elected President, Mr. Munno served as Vice President of Sales and Marketing. Mr. Munno was the founder, President and CEO of Interlan Communications, Inc. a privately held Virginia based data networking and network security company which we acquired in June 2003. From March 1990 to August 1995 Mr. Munno was a Director of Sales for Microcom Incorporated, a publicly traded manufacturer of modems and other wide area networking products. From October 1988 to March 1990, Mr. Munno held the position of Major Business Opportunities, Manager of Systems, and Tests for Government Technology Services Inc. (GTSI), a publicly traded systems provider to government and education. From January 1987 to October 1988, Mr. Munno was employed as a Product Specialist for SMS Data Products Group of Virginia. Prior to starting his civilian career, Mr. Munno was a member of the US Army for seven years where he was awarded the Meritorious Service Medal twice while a member of the US Army Signal Corps. Mr. Munno attended the City College of Chicago.

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Brian E. Crooks. Mr. Crooks as served as our Chief Financial Officer since November 2005. From May 2005 until his appointment as Chief Financial Officer Mr. Crooks has been providing financing and accounting consulting services to our company. Mr. Crooks, a certified public accountant, has been a partner in the Northern Virginia firm of Crooks & Seth P.C. since co-founding the firm in 1982. Mr. Crooks' practice has centered around assisting companies with accounting, tax compliance, financing, tax planning, legal support and management consulting. From December 2002 until April 2004 Mr. Crooks provided various accounting services to our company on a consulting basis. Mr. Crooks holds a B.S. in Accounting from Clarion University.

Harold F. Compton. Mr. Compton has been a member of our Board of Directors since May 2005. Mr. Compton has been a retailer for more than 30 years. Mr. Compton joined CompUSA Inc. in 1994 as Executive Vice President-Operations, becoming Executive Vice President and Chief Operating Officer in 1995, President of CompUSA Stores in 1996 and Chief Executive Officer of CompUSA Inc. in 2000, a position he held until his retirement in 2004. Prior to joining CompUSA, Inc., from 1993 until 1994 he served as President and COO of Central Electric Inc., Executive Vice President Operations and Human Resources, and Director of Stores for HomeBase (1989 to 1993), Senior Vice President

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Operations and Director of Stores for Roses Discount Department Stores (1986 to 1989), and held various management positions including Store Manager, District Manager, Regional Vice President and Zone Vice President for Zayre Corporation from 1965 to 1986. Since 1998 Mr. Compton has been a member of the Board of Directors of Linens 'N Things, Inc., and is a member of its Compensation Committee and Corporate Governance and Nominating Committee of the Board of Directors of that company.

Raymond Pirtle, Jr. Mr. Pirtle has been a member of our Board of Directors since June 2005. Mr. Pirtle is a veteran of the financial services industry, having spent the past three decades in a variety of senior roles in corporate finance, institutional sales, investment banking, and equity research. From 1966 until 1989 he was employed by J.C. Bradford & Co., a large regional investment banking and brokerage, departing as a general partner. From 1989 until 2001 he was a Director and co-head of institutional sales of Equitable Securities Corp., a banking and institutional brokerage firm later known as SunTrust Equitable. In 2001 he was one of the founding partners of Avondale Partners, LLC, an institutional equity research and investment banking firm focusing on small companies generally with a market cap in the range of \$200 million to \$2 billion. Mr. Pirtle presently serves as a member of Avondale Partners' Advisory Board Committee. In March 2005 Mr. Pirtle founded Clairidge Company, LLC, a consulting firm that represents micro-cap to small-cap companies with a public equity valuation under \$200 million or larger companies that are seeking to attract broad attention from institutional portfolio managers, research analysts or investment bankers. Since 1985 Mr. Pirtle has been serving on the board of both public and private companies. He currently serves on the board of Premier Global Services, Inc. (NYSE: PGI), a provider of business communications services and business process solutions that enable enterprise customers to automate and simplify components of their critical business processes and to communicate more effectively with their constituents, and eNucleus, Inc. (OTCBB: ENUI), a provider of supply chain software applications.

Joseph L. Druzak. Mr. Druzak has been a member of our Board of Directors since June 2005. After first joining the company more than 20 years ago, since 1985 Mr. Druzak has served President and CEO of Kreher Steel Company, LLC., a large, privately-held specialty steel distribution company serving such diverse markets as automotive, rail, construction, oil and gas, aerospace and defense.

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Jack Bush. Mr. Bush has been a member of our Board of Directors since August 2005. Mr. Bush has served as the President of Raintree Partners, Inc., a management consulting company, since September 1995. He is also currently Chairman and Director of IdeaForest.com (Joann.com), Vice Chairman and Director of FPE Corporation (Framed Picture Enterprises) and Co-Chairman of Country Sampler stores. From 1995 to 1999 he served as Chairman of Aaron Brothers Holding Company and of Carolina Art & Frame Co. He was a founder, Chief Concept Officer and Director of Artistree Art, Frame & Design Company. During this time he was also a Director of Cyberplay, New York Coffee & Bagels, Bradlees Stores, Stage Stores, Telequip and Jumbo Sports Company. He served on the board of Bradlees during a successful reorganization and served as special assistant to the board of Stage Stores during a successful reorganization. From 1997 to 1999 he served as Chairman, CEO and President of Jumbo Sports Co. From 1991 to August 1995, he was President and Director of Michaels Stores, Inc. and was Chairman of Michaels of Canada. The company grew from 136 to 530 stores and became the largest arts and crafts retailer in the world. Upon leaving the Nasdaq-quoted company, sales reached \$1.5 billion and had 22,000 associates. From 1990 to 1991 he served as Executive Vice President, Director of Operations and Stores for Ames Department Stores. From 1985 to 1990 Mr. Bush was President and Director of

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Roses stores, a Nasdaq-quoted company. During his tenure the company grew to 226 stores with \$1.6 billion in sales and 25,000 associates From 1980 to 1985 He served as Vice President of Zayre Corporation, an NYSE-listed company responsible for 105 stores and \$750 million in sales. From 1958 to 1980 He served in a variety of positions with J.C. Penney Company, an NYSE-listed company. Mr. Bush was a U.S. Air Force Reserve officer and holds a Bachelor of Science from the University of Missouri.

There are no family relationship between any of the executive officers and directors. Directors are elected at our annual meeting of stockholders and hold office for one year or until his or her successor is elected and qualified.

KEY EMPLOYEES

John Younts. Mr. Younts, 38, has served as Vice President Integrated Power Solutions since August 2003. His responsibilities include promotion and local support of mission critical computer room equipment as a manufacturer's representative to local companies with computers, as well as offering maintenance agreements for legacy and new customers. Mr. Younts has 17 years of experience in hardware support equipment business. From 1988 until 2003 Mr. Younts was a Senior Sales Associates with Lee Associates, a provider of infrastructure products and solutions. He was responsible for a nationwide roll out requiring mission critical support equipment for customers including Nextel and Qwest. He was also responsible for building long lasting relationships with his customers as well as the vendors. Mr. Younts' primary focus was on the design, sale and implementation of these critical support systems for MEP firms, end users, electric and general contractors in the Mid-Atlantic Region. Mr. Younts holds a Bachelor degree from Radford University.

James M. Bond. Mr. Bond, 34, has served as our Vice President of Program Services since June 2003. His responsibilities include management of our consulting services practice which is focused on network infrastructure and enterprises messaging services. Mr. Bond is also responsible for developing new services and product offerings. From August 2000 until our acquisition of the company in June 2003, Mr. Bond was President of The Seven Corporation, which is now our consulting services division. Mr. Bond has over 15 years of information technology design and implementation experience. He has been the architect of and has implemented solutions for medium and large corporate and government organizations with some multi-year projects exceeding \$50M. Mr. Bond served as Vice President with Steelcloud from 1997 until 2000 where he ran the Professional Services division with over 50 consulting

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engineers and revenues exceeding \$15M annually. Mr. Bond's earlier work experience includes senior engineering, architecture/design, and project management responsibilities with companies such as Electronic Data Systems (EDS) and Computer Sciences Corporation (CSC). Mr. Bond holds a Bachelor degree from the University of Maryland in Computer Science and is currently pursuing a Master's Degree. He has been a certified engineer for products and companies including Microsoft, Novell, 3Com, NetFRAME, Tricord, and currently serves on the Microsoft Architect's Council for the Mid-Atlantic region.

COMMITTEES OF THE BOARD OF DIRECTORS

Our Board of Directors has created both an Audit Committee and a Compensation Committee.

AUDIT COMMITTEE. The Audit Committee of our Board of Directors was formed to assist the Board of Directors in fulfilling its oversight responsibilities for the integrity of our consolidated financial statements,

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compliance with legal and regulatory requirements, the independent registered public accounting firm's qualifications and independence, and the performance of our internal audit function and independent auditors. The Audit Committee will also prepare the report that SEC rules require be included in our annual proxy statement. The Audit Committee has adopted a charter which sets forth the parameters of its authority. The Audit Committee Charter provides that the Audit Committee is empowered to:

- o Appoint, compensate, and oversee the work of the independent registered public accounting firm employed by our company to conduct the annual audit. This firm will report directly to the audit committee;
- o Resolve any disagreements between management and the auditor regarding financial reporting;
- o Pre-approve all auditing and permitted non-audit services performed by our external audit firm;
- o Retain independent counsel, accountants, or others to advise the committee or assist in the conduct of an investigation;
- o Seek any information it requires from employees - all of whom are directed to cooperate with the committee's requests - or external parties;
- o Meet with our officers, external auditors, or outside counsel, as necessary; and
- o The committee may delegate authority to subcommittees, including the authority to pre-approve all auditing and permitted non-audit services, provided that such decisions are presented to the full committee at its next scheduled meeting.

Each Audit Committee member is required to:

- o satisfy the independence requirements of Section 10A(m)(3) of the Securities Exchange Act of 1934, and all rules and regulations promulgated by the SEC as well as the rules imposed by the stock exchange or other marketplace on which our securities may be listed from time to time, and

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- o meet the definitions of "non-employee director" for purposes of SEC Rule 16b-3 and "outside director" for purposes of Section 162(m) of the Internal Revenue Code.

Each committee member is required to be financially literate and at least one member is to be designated as the "financial expert," as defined by applicable legislation and regulation. No committee member is permitted to simultaneously serve on the audit committees of more than two other public companies. Mr. Pirtle is presently the sole member of our Audit Committee. As we expand our Board of Directors with additional independent directors the number of directors serving on the Audit Committee will also increase.

COMPENSATION COMMITTEE. The Compensation Committee was appointed by the Board to discharge the Board's responsibilities relating to:

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- o compensation of our executives,
- o equity-based compensation plans, including, without limitation, stock option and restricted stock plans, in which officers or employees may participate, and
- o arrangements with executive officers relating to their employment relationships with our company, including employment agreements, severance agreements, supplemental pension or savings arrangements, change in control agreements and restrictive covenants.

The Compensation Committee charter provides that the Compensation Committee has overall responsibility for approving and evaluating executive officer compensation plans, policies and programs of our company, as well as all equity-based compensation plans and policies. In addition, the Compensation Committee oversees, reviews and approves all of our ERISA and other employee benefit plans which we may establish from time to time. The Compensation Committee is also responsible for producing an annual report on executive compensation for inclusion in the our proxy statement and assisting in the preparation of certain information to be included in other periodic reports filed with the SEC.

Each Compensation Committee member is required to:

- o satisfy the independence requirements of Section 10A(m) (3) of the Securities Exchange Act of 1934, and all rules and regulations promulgated by the SEC as well as the rules imposed by the stock exchange or other marketplace on which our securities may be listed from time to time, and
- o meet the definitions of "non-employee director" for purposes of SEC Rule 16b-3 and "outside director" for purposes of Section 162(m) of the Internal Revenue Code.

No committee member is permitted to simultaneously serve on the audit committees of more than two other public companies. Messrs. Compton, Druzak and Bush are the members of our Compensation Committee. As we expand our Board of Directors with additional independent directors the number of directors serving on the Compensation Committee will also increase.

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CODE OF ETHICS

In May 2005, we adopted a Code of Business Conduct and Ethics applicable to our Chief Executive Officer, principal financial and accounting officers and persons performing similar functions. A Code of Business Conduct and Ethics is a written standard designed to deter wrongdoing and to promote:

- o honest and ethical conduct,
- o full, fair, accurate, timely and understandable disclosure in regulatory filings and public statements,
- o compliance with applicable laws, rules and regulations,
- o the prompt reporting violation of the code, and
- o accountability for adherence to the Code.

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A copy of our Code of Business Conduct and Ethics is filed as an exhibit to the registration statement of which this prospectus forms a part, and we will provide a copy, without charge, to any person desiring a copy of the Code of Business Conduct and Ethics, by written request to us at our principal offices.

EXECUTIVE COMPENSATION

Cash Compensation

The following table summarizes all compensation recorded by us in each of the last three fiscal years for our Chief Executive Officer and each other executive officers serving as such whose annual compensation exceeded \$100,000.

| Name and Principal Position | Fiscal Year | Annual Compensation | | | Long-Term Compensation | |
|-----------------------------|-------------|---------------------|------------|--------------------------------|------------------------------|---------------------------------------|
| | | Salary (\$) | Bonus (\$) | Other Annual Compensation (\$) | Restricted Stock Awards (\$) | Securities Underlying Options SAR (#) |
| John R. Signorello .. | 2003 | \$ 5,000 | \$ -0- | \$ -0- | \$ -0- | 75,000 |
| Chief Executive | 2004 | \$ 80,000 | \$ -0- | \$ -0- | \$ -0- | -0- |
| Officer (1) | 2005 | \$ 120,000 | \$ -0- | \$ -0- | \$ -0- | -0- |

(1) In fiscal year 2003, Mr. Signorello was granted options to purchase 75,000 shares at \$3.20 per share, expiring in September 2008.

OPTION/SAR GRANTS IN LAST FISCAL YEAR

The following table sets forth information concerning individual grants of options made during fiscal 2005 to the named executive officers.

| | Number of Shares Underlying Options Granted (#) | % of Total Options Granted to Employees in Fiscal Year | Exercise or Base Price (\$/Sh) | Expiration Date |
|--|---|--|--------------------------------|-----------------|
| | | | | |

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AGGREGATED OPTION/SAR EXERCISES IN LAST FISCAL YEAR AND FISCAL YEAR-END OPTION/SAR VALUES

The following table indicates each exercise of stock options (or tandem SARs) and freestanding SARs during the last fiscal year by each of the named executive officers and the fiscal year end value of unexercised options and SARs.

| Shares Acquired on | Value | Number of Securities Underlying Unexercised Options/SARs at FY End (#) | Value In-the-mon FY |
|--------------------|-------|--|---------------------|
|--------------------|-------|--|---------------------|

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| Name | Exercise (#) | Realized (\$) | Exercisable | Unexercisable | Exercisable |
|-----------------------|--------------|---------------|-------------|---------------|-------------|
| John R. Signorello .. | 25,000 | \$ 0(2) | 104,000 (3) | 12,000 (4) | \$ 0 |

(1) The dollar value of the exercisable and unexercisable options is calculated based upon the difference between the option exercise price and \$0.90 per share, being the last sales price of our common stock on September 30, 2005 as reported on the OTC Bulletin Board.

(1) The exercise price of the options were \$0.80 per share and the fair market value of our common stock on October 15, 2004, the date of exercise, was \$1.04 per share. Accordingly, Mr. Signorello did not realize any value upon the exercise of these options.

(3) Includes options to purchase 50,000 shares of our common stock at an exercise price of \$1.60 per share which expire in February 2007 and options to purchase 54,000 shares of our common stock at an exercise price of \$3.20 per share which expire in September 2008.

(4) Includes options to purchase 21,000 shares of our common stock at an exercise price of \$3.20 per share which expire in September 2008 which had not vested at September 30, 2005.

STOCK OPTION PLAN

In August 2000, our Board of Directors adopted our 2000 Management and Director Equity Incentive and Compensation Plan (the "Plan"). The Plan was approved by our stockholders in August 2001. As amended, we have reserved an aggregate of 1,250,000 shares of common stock for issuance under the Plan. At January 15, 2006 we have granted options to purchase 1,215,750 shares of our common stock under the Plan. Until such time as we have completed an initial public offering, our Board of Directors (or at their discretion a committee of our Board members) administers the Plan including, without limitation, the selection of recipients of awards under the Plan, the granting of stock options, restricted share or performance shares, the determination of the terms and conditions of any such awards, the interpretation of the Plan and any other action they deem appropriate in connection with the administration of the Plan.

The purpose of the Plan is to advance our interests and those of our stockholders by providing a means of attracting and retaining key employees, directors and consultants. In order to serve this purpose, we believe the Plan encourages and enables key employees, directors and consultants to participate in our future prosperity and growth by providing them with incentives and compensation based on our performance, development and financial success. Participants in the Plan may include our officers, directors, other key employees and consultants who have responsibilities affecting our management, development or financial success.

Awards may be made under the Plan in the form of Plan options, shares of our common stock subject to a vesting schedule based upon certain performance objectives ("performance shares") and shares subject to a vesting schedule based on the recipient's continued employment ("restricted shares"). Plan options may either be options qualifying as incentive stock options under Section 422 of the Internal Revenue Code of 1986, as amended or options that do not so qualify. Any incentive stock option granted under our Plan must provide for an exercise price of not less than 100% of the fair market value of the underlying shares on the date of such grant, but the exercise price of any incentive option granted to an eligible employee owning more than 10% of our common stock must be at least 110% of such fair market value as determined on the date of the grant. Only persons who are our officers or other key employees are eligible to receive incentive

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stock options and performance share grants. Any non-qualified stock option granted under our Plan must provide for an exercise price of not less than 50% of the fair market value of the underlying shares on the date of such grant.

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The term of each Plan option and the manner in which it may be exercised is determined by the Board of Directors, provided that no Plan option may be exercisable more than three years after the date of its grant and, in the case of an incentive option granted to an eligible employee owning more than 10% of our common stock, no more than five years after the date of the grant. The exercise price of the stock options may be paid in either:

- o cash, or
- o delivery of unrestricted shares of our common stock having a fair market value on the date of delivery equal to the exercise price, or
- o surrender of shares of our common stock subject to the stock option which has a fair market value equal to the total exercise price at the time of exercise, or
- o a combination of the foregoing methods.

All Plan options are nonassignable and nontransferable, except by will or by the laws of descent and distribution and, during the lifetime of the optionee, may be exercised only by such optionee. At the discretion of the Board of Directors, it may approve the irrevocable transfer, without payment, of non-qualified options to the option holder's spouse, children, grandchildren, nieces or nephews, or to the trustee of a trust for the principal benefit of one or more such persons, or to a partnership whose partners are one or more of such persons. If an optionee's employment is terminated for any reason, other than due to his or her death, disability or termination for cause, or if an optionee is not our employee but is a member of our Board of Directors and his or her service as a director is terminated for any reason, other than due to his or her death or disability, the Plan option granted may be exercised on the earlier of the expiration date or 90 days following the date of termination. If the optionee dies during the term of his or her employment, the Plan option granted to him or her shall lapse to the extent unexercised on the earlier of the expiration date of the Plan option or the date one year following the date of the optionee's death. If the optionee's employment, membership on the Board of Directors or engagement as a consultant terminates by reason of the optionee's retirement, then the Plan option granted may be exercised until the earlier of 90 days following the date of termination or the expiration date. If the optionee is permanently and totally disabled within the meaning of Section 22(c)(3) of the Internal Revenue Code, the Plan option granted to him or her lapses to the extent unexercised on the earlier of the expiration date of the option or one year following the date of such disability.

At the time of the restricted share grant, the Board of Directors may determine the vesting schedule of such shares and that after vesting, such shares may be further restricted as to transferability or be subject to repurchase by us or forfeiture upon the occurrence of certain events. Awards of restricted shares must be accepted by the participant within 30 days of the grant.

At the time of the award of performance shares, the Board of Directors shall establish a range of performance goals to be achieved during the performance period, including, without limitation, earnings, return on capital, or any performance goal approved by our stockholders in accordance with Section

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162(m) of the Internal Revenue Code. Attainment of the highest performance goal for the performance period will earn 100% of the performance shares awarded for the performance period; failure to attain the lowest performance goal will result in the participant earning no performance shares. Attainment of the performance goals will be calculated from our financial statements, excluding changes in federal income tax rates and the effect of non-recurring and extraordinary items. The performance goals may vary for different performance periods and need not be the same for each participant receiving an award during a performance period.

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If the participant's employment by us, membership on our Board of Directors, or engagement by us as a consultant is terminated before the end of any performance period, or upon the participant's death, retirement or disability, the Board of Directors, taking into consideration the performance of such participant and our performance over the performance period, may authorize the issuance to the participant or his or her legal representative or designated beneficiary all or a portion of the performance shares which would have been issued to him or her had the participant's employment, Board membership or consulting engagement continued to the end of the performance period. If the participant's employment, Board membership or consulting engagement terminates before the end of the performance period for any other reason, all performance shares are forfeited.

Notwithstanding the foregoing, but subject to any stockholder approval or other requirements of Section 162(m) of the Internal Revenue Code, the Board of Directors in its discretion and as determined at the time of award of the performance shares, may provide the participant with the option of receiving cash in lieu of the performance shares in an amount determined at the time of award including, without limitation, by one or more of the following methods:

- o the fair market value of the number of shares subject to the performance shares agreement on the date of award, or
- o part or all of any increase in the fair market value since such date, or
- o part or all of any dividends paid or payable on the number of shares subject to the performance share agreement, or
- o any other amounts which in the Board's sole discretion are reasonably related to the achievement of the applicable performance goals, or
- o any combination of the foregoing.

The purchase price for restricted shares or performance shares granted under the Plan shall be set by the Board of Directors but may not be less than par value. Payment of the purchase price for the restricted shares or performance share may be made in either,

- o cash, or
- o by delivery of unrestricted shares of our common stock having a fair market value on the date of such delivery equal to the total purchase price, or
- o a combination of either of these methods.

The restricted stock awards, performance stock awards and stock options

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are subject to accelerated vesting in the event of our change of control. We may, at our option, terminate all unexercised stock options 30 days after a change in control and pay to the participant holding these unexercised options cash in an amount equal to the difference between fair market value and the exercise price of the stock option. If the fair market value is less than the exercise price, we may terminate the options without payment to the holder. The per share purchase price of shares subject to Plan options granted under the Plan or related to performance share awards or restricted share awards may be adjusted in the event of certain changes in our capitalization, but any such adjustment shall not change the total purchase price payable upon the exercise in full of such option or award. No participant in our Plan has any rights as a stockholder until the shares subject to the Plan options or stock awards have been duly issued and delivered to him or her.

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We have an option to purchase any shares of our common stock which have been issued to Plan participants pursuant to restricted stock awards, performance stock awards or stock options if the participant ceases to be our employee, a member of our Board of Directors or a consultant to us for any reason. We must exercise our repurchase right at the time of termination. The purchase price for any shares we repurchase will be equal to the fair market value of the our total stockholders' equity divided by the total outstanding shares of our common stock on the last day of that calendar month, calculated on a fully-diluted basis. If we exercise our repurchase right, we much close the transaction within 20 days from the termination date. At closing, we are entitled to delivery a one-year promissory note as payment for the purchase price or, at our option, we may pay same in cash at closing.

We also have a right of first refusal to meet the offer if the holder of any shares of our common stock awarded or issued pursuant to our Plan desires to sell such shares to a third party.

The Board of Directors may amend, suspend or terminate our Plan at any time, except that no amendment shall be made which:

- o increases the total number of shares subject to the Plan or changes the minimum purchase price therefore (except in either case in the event of adjustments due to changes in our capitalization), or
- o affects outstanding Plan options or any exercise right thereunder, or
- o extends the term of any Plan option beyond 10 years, or
- o extends the termination date of the Plan.

Unless the Plan shall be earlier suspended or terminated, the Plan shall terminate 10 years from the date of the Plan's adoption by our stockholders. Any such termination of our Plan shall not affect the validity of any Plan options previously granted thereunder.

LIMITATION ON LIABILITY AND INDEMNIFICATION MATTERS

As authorized by the Delaware General Corporation Laws, our certificate of incorporation provide that none of our directors shall be personally liable to us or our stockholders for monetary damages for breach of fiduciary duty as a director, except liability for:

- o any breach of the director's duty of loyalty to our company or

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its stockholders;

- o acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law;
- o unlawful payments of dividends or unlawful stock redemptions or repurchases; and
- o any transaction from which the director derived an improper personal benefit.

This provision limits our rights and the rights of our stockholders to recover monetary damages against a director for breach of the fiduciary duty of care except in the situations described above. This provision does not limit our rights or the rights of any stockholder to seek injunctive relief or rescission if a director breaches his duty of care. These provisions will not alter the liability of directors under federal securities laws. Our by-laws require us to indemnify directors and officers against, to the fullest extent permitted by law, liabilities which they may incur under the circumstances described above.

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Our certificate of incorporation further provide for the indemnification of any and all persons who serve as our director, officer, employee or agent to the fullest extent permitted under Delaware law.

Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to our directors, officers and controlling persons according to the foregoing provisions, or otherwise, we have been advised that in the opinion of the SEC such indemnification is against public policy as expressed in the Securities Act of 1933 and is, therefore, unenforceable.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

From time to time we have borrowed funds from Mr. Signorello, our Chairman and CEO, for working capital. In April 2002 we issued Mr. Signorello a demand promissory note in the principal amount of \$150,000. This note bears interest at 12.5% per annum. At March 31, 2005 we owed Mr. Signorello \$93,177. Under the terms of the Preferred Stock Purchase Agreement with Barron Partners, L.P. as described later in this prospectus beginning on page 46 which closed on March 30, 2005 Mr. Signorello was required to convert the principal and interest due under this note into shares of our common stock. In April 2005, Mr. Signorello sold this note to Mr. Robert Druzak, a principal stockholder of our company. In April 2005 we issued 416,667 shares of our common stock in exchange for a \$50,000 subscription receivable to our company and the satisfaction of this note payable. The shares of common stock issued to Mr. Druzak remain restricted until such time as the subscription receivable has been satisfied. At September 30, 2005 this receivable remains outstanding.

Subsequent to this note conversion, from time to time Mr. Signorello has continued to provide funds to us for operating expenses. At September 30, 2005 we owed Mr. Signorello \$86,001, net of repayment of \$86,001 made subsequent to the April 2005 note conversion described above. These advances are short-term and non-interest bearing. We will repay Mr. Signorello this amount as working capital is available to us.

Immediately prior to the closing of the Preferred Stock Purchase Agreement with Barron Partners, L.P. we had other stockholders/employees loans totaling \$227,186 plus accrued interest of approximately \$62,400. Included in this amount was approximately \$77,000 due Mr. James Bond, one of our key employees, which represented the remaining portion of the cash consideration due

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him under the terms of our purchase of the stock of The Seven Corporation as described earlier in this prospectus. This amount was converted by Mr. Bond into 125,000 shares of our common stock in April 2005 in accordance with the terms of the Preferred Stock Purchase Agreement with Barron Partners, L.P.

Also included in this total at March 31, 2005 was a \$150,000 principal amount promissory note bearing interest at the rate of 12.5% per annum due on demand to a stockholder of our company. In May 2005 we issued this stockholder 125,000 shares of common stock as consideration for the extension of the maturity date of the note by 10 years which had been orally agreed to in fiscal 2004. The shares were valued at \$200,000 the fair value at the date of issuance. The note remains outstanding and at September 30, 2005 we owed the stockholder the \$150,000 principal plus accrued interest of approximately \$65,625.

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In 2002, we borrowed \$100,000 from three stockholders. During the fiscal year ended September 30, 2003, these notes were converted to equity at \$0.10 per share, resulting in the issuance of 12,500 shares.

PRINCIPAL STOCKHOLDERS

At January 15, 2006, there were 6,492,286 shares of our common stock issued and outstanding. Our common stock is the only outstanding class of our voting securities. The following table sets forth, as of January 15, 2006, information known to us relating to the beneficial ownership of these shares by:

- o each person who is the beneficial owner of more than 5% of the outstanding shares of common stock;
- o each director;
- o each executive officer; and
- o all executive officers and directors as a group.

Unless otherwise indicated, the address of each beneficial owner in the table set forth below is care of 205 Van Buren, Suite 150, Herndon, Virginia 20170.

We believe that all persons named in the table have sole voting and investment power with respect to all shares of beneficially owned by them. Under securities laws, a person is considered to be the beneficial owner of securities he owns and that can be acquired by him within 60 days from January 15, 2006 upon the exercise of options, warrants, convertible securities or other understandings. We determine a beneficial owner's percentage ownership by assuming that options, warrants or convertible securities that are held by him, but not those held by any other person and which are exercisable within 60 days of January 15, 2006, have been exercised or converted. Unless otherwise noted, the address of each of these principal stockholders is our principal executive offices.

| Name of Beneficial Owner ----- | Amount and Nature of Beneficial Ownership ----- | Percentage of Class ----- |
|--------------------------------------|---|---------------------------------|
| John R. Signorello(1) | 2,339,164 | 35.4% |
| G. Anthony Munno(2) | 122,588 | 1.9% |
| Brian E. Crooks(6) | 95,000 | 1.4% |
| Hal Compton(7) | 8,310 | * |
| Raymond Pirtle(8) | 8,310 | * |

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| | | |
|--|-----------|-------|
| Joseph L. Druzak (3) | 210,126 | 3.2% |
| Jack Bush(9) | 30,000 | * |
| All executive officers and as a group (seven persons) | 2,813,498 | 40.3% |
| Robert Druzak (4) | 506,667 | 7.8% |
| Nite Capital L.P. (5) | 375,000 | 5.7% |

* represents less than 1%

(1) The number of shares beneficially owned by Mr. Signorello includes options to purchase 50,000 shares of our common stock at an exercise price of \$1.60 per share and options to purchase 63,000 shares of our common stock at an exercise price of \$3.20 per share, but excludes options to purchase 12,000 shares of our common stock at an exercise price of \$3.20 per share which have not yet vested.

(2) The number of shares beneficially owned by Mr. Munno includes options to purchase 60,000 shares of our common stock at an exercise price of \$2.16 per share, options to purchase 2,088 shares of our common stock at an exercise price of \$2.40 per share and options to purchase 40,000 shares of our common stock at an exercise price of \$0.65 per share but excludes options to purchase 2,500 shares of common stock at an exercise price of \$2.16 per share which have not yet vested.

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(3) The number of shares beneficially owned by Mr. Druzak includes Series H Common Stock Purchase Warrants exercisable into 50,000 shares of our common stock at an exercise price of \$4.00 per share, Series I Common Stock Purchase Warrants exercisable into 50,000 shares of our common stock at an exercise price of \$8.00 per share and options to purchase 7,500 shares of common stock at an exercise price of \$0.80 per share. The number of shares beneficially owned by Mr. Druzak excludes options to purchase an additional 22,500 shares of common stock at an exercise price of \$0.80 per share which have not yet vested..

(4) The number of shares beneficially owned by Mr. Druzak includes options to purchase 40,000 shares of our common stock at an exercise price of \$0.65 per share. Mr. Robert Druzak is the brother of Mr. Joseph Druzak.

(5) The number of shares beneficially owned by Nite Capital L.P. includes 125,000 shares of our common stock presently outstanding and 250,000 shares of our common stock issuable upon the exercise of common stock purchase warrants with exercise prices ranging from \$4.00 to \$8.00 per share. Mr. Keith Goodman exercises investment and voting rights over the securities held by Nite Capital LP.

(6) The number of shares beneficially owned by Mr. Crooks includes options to purchase 95,000 shares of our common stock at an exercise price of \$0.65 per share but excludes options to purchase 70,000 shares of common stock at \$2.40 per share which have not yet vested.

(7) The number of shares beneficially owned by Mr. Compton includes options to purchase 8,310 shares of our common stock at an exercise price of \$0.80 per share but excludes options to purchase an additional 21,690 shares at \$0.80 per share which have not yet vested.

(8) The number of shares beneficially owned by Mr. Pirtle includes options to purchase 8,310 shares of our common stock at an exercise price of \$0.80 per share but excludes options to purchase an additional 21,690 shares at \$0.80 per share which have not yet vested.

(9) The number of shares beneficially owned by Mr. Bush includes options to

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purchase 30,000 shares of our common stock at an exercise price of \$0.80 per share.

DESCRIPTION OF SECURITIES

Our authorized capital stock consists of 1,000,000,000 shares of common stock, \$.001 par value per share, and 10,000,000 shares of preferred stock, par value \$.001 per share, of which 1,666,667 shares have been designated as Series A Convertible Preferred Stock and 1,833,334 shares have been designated as Series B Convertible Preferred Stock. As of January 15, 2006, there are 6,492,286 shares of common stock, 1,666,667 shares of Series A Convertible Preferred Stock and 1,833,334 shares of Series B Convertible Preferred Stock issued and outstanding. We have not included 437,502 shares of common stock listed as outstanding on our transfer records in the number of shares common shares which are currently issued and outstanding. Although the certificates have not been cancelled, these shares were contributed to our capital by agreement at the time of our reverse merger in March 2002 and may not be voted.

COMMON STOCK

Holders of common stock are entitled to one vote for each share on all matters submitted to a stockholder vote. Holders of common stock do not have cumulative voting rights. Holders of common stock are entitled to share in all dividends that the Board of Directors, in its discretion, declares from legally available funds. In the event of our liquidation, dissolution or winding up, subject to the preferences of any shares of our preferred stock which may then be outstanding, each outstanding share entitles its holder to participate in all assets that remain after payment of liabilities and after providing for each class of stock, if any, having preference over the common stock.

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Holders of common stock have no conversion, preemptive or other subscription rights, and there are no redemption provisions for the common stock. The rights of the holders of common stock are subject to any rights that may be fixed for holders of preferred stock, when and if any preferred stock is authorized and issued. All outstanding shares of common stock are duly authorized, validly issued, fully paid and non-assessable.

PREFERRED STOCK

Our Board of Directors, without further stockholder approval, may issue preferred stock in one or more series from time to time and fix or alter the designations, relative rights, priorities, preferences, qualifications, limitations and restrictions of the shares of each series. The rights, preferences, limitations and restrictions of different series of preferred stock may differ with respect to dividend rates, amounts payable on liquidation, voting rights, conversion rights, redemption provisions, sinking fund provisions and other matters. Our Board of Directors may authorize the issuance of preferred stock, which ranks senior to our common stock for the payment of dividends and the distribution of assets on liquidation. In addition, our Board of Directors can fix limitations and restrictions, if any, upon the payment of dividends on our common stock to be effective while any shares of preferred stock are outstanding.

The rights granted to the holders of any series of preferred stock could adversely affect the voting power of the holders of common stock and issuance of preferred stock may delay, defer or prevent a change in our control.

SERIES A CONVERTIBLE PREFERRED STOCK

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Our Board of Directors has created a series of 1,666,667 shares of preferred stock designated as Series A Convertible Preferred Stock. We sold these shares in a transaction described later in this prospectus under "Selling Security Holders." The designations, rights and preferences of the Series A Convertible Preferred Stock provide:

- o no dividends are payable on the Series A Convertible Preferred Stock. So long as these shares are outstanding, we cannot pay dividends on our common stock nor can we redeem any shares of our common stock,
- o the shares of Series A Convertible Preferred Stock do not have any voting rights, except as may be provided under Delaware law,
- o so long as the shares are outstanding, we cannot change the designations of the Series A Convertible Preferred Stock, create a class of securities that in the instance of payment of dividends or distribution of assets upon our liquidation ranks senior to or pari passu with the Series A Convertible Preferred Stock or increase the number of authorized shares of Series A Convertible Preferred Stock,
- o the shares carry a liquidation preference of \$0.60 per share,
- o each share of Series A Convertible Preferred Stock is convertible at the option of the holder into shares of our common stock, subject to adjustment in the event of stock splits and stock dividends, based upon a conversion value of \$0.60 per share, and

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- o so long as the shares of Series A Convertible Preferred Stock are outstanding, we cannot sell or issue any common stock, rights to subscribe for shares of common stock or securities which are convertible or exercisable into shares of common stock at an effective purchase price of less than the then conversion value.

No conversion of the Series A Convertible Preferred Stock may occur if a conversion would result in the holder, Barron Partners LP, and any of its affiliates beneficially owning more than 4.99% of our outstanding common shares following such conversion. Barron Partners LP may waive this provision upon 61 days prior notice to us, or it immediately terminates in the event of a sale or merger of substantially all of our company or upon an underwritten public offering.

SERIES B CONVERTIBLE PREFERRED STOCK

Our Board of Directors has also created a series of 1,833,334 shares of preferred stock designated as Series B Convertible Preferred Stock. We sold these shares in a transaction described earlier in this prospectus under "Management's Discussion and Analysis or Plan of Operation - Recent Capital Raising Transaction." The designations, rights and preferences of the Series B Convertible Preferred Stock provide:

- o no dividends are payable on the Series B Convertible Preferred Stock. So long as these shares are outstanding, we cannot pay dividends on our common stock nor can we redeem any shares of our common stock,
- o the shares of Series B Convertible Preferred Stock do not have any voting rights, except as may be provided under Delaware law,

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- o so long as the shares are outstanding, we cannot change the designations of the Series B Convertible Preferred Stock, create a class of securities that in the instance of payment of dividends or distribution of assets upon our liquidation ranks senior to or pari passu with the Series B Convertible Preferred Stock or increase the number of authorized shares of Series B Convertible Preferred Stock,
- o the shares carry a liquidation preference of \$0.2727 per share,
- o each share of Series B Convertible Preferred Stock is convertible at the option of the holder into one share of our common stock based upon an initial conversion value of \$0.2727 per share. The conversion ratio is subject to adjustment in the event of stock dividends, stock splits or reclassification of our common stock. The conversion ratio is also subject to adjustment in the event we should sell any shares of our common stock or securities convertible into common stock at an effective price less than the conversion ratio then in effect, in which case the conversion ratio would be reduced to the lesser price. No conversion of the Series B Convertible Preferred Stock may occur if a conversion would result in the holder, Barron Partners LP, and any of its affiliates beneficially owning more than 4.9% of our outstanding common shares following such conversion. Barron Partners LP may waive this provision only with the consent of all of the Series B Preferred Stockholders and the consent of the holders of a majority of our outstanding shares of common stock who are not affiliates,

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- o so long as the Series B Convertible Preferred Stock is outstanding, we have agreed not to issue any rights, options or warrants to holders of our common stock entitling the holders to purchase shares of our common stock at less than the conversion ratio with out the consent of the holders of a majority of the outstanding shares of Series B Convertible Preferred Stock. If we should elect to undertake such an issuance and the Series B holders consent, the conversion ratio would be reduced. Further, if we should make a distribution of any evidence of indebtedness or assets or rights or warrants to subscribe for any security to our common stockholders, the conversion value would be readjusted,
- o the shares of Series B Convertible Preferred Stock automatically convert into shares of our common stock in the event of change of control of our company, and
- o so long as the shares of Series B Convertible Preferred Stock are outstanding, we cannot sell or issue any common stock, rights to subscribe for shares of common stock or securities which are convertible or exercisable into shares of common stock at an effective purchase price of less than the then conversion value of the Series B Convertible Preferred Stock.

COMMON STOCK PURCHASE WARRANTS

At January 15, 2006 we had outstanding an aggregate of 7,765,000 common stock purchase warrants as follows:

WARRANTS ISSUED IN THE SERIES A CONVERTIBLE PREFERRED STOCK TRANSACTION

In connection with the sale of shares of our Series A Convertible

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Preferred Stock in March 2005, we issued the purchaser the following five-year common stock purchase warrants:

- o Common Stock Purchase Warrants "A" to purchase an aggregate of 2,000,000 shares of our common stock at an exercise price of \$2.00 per share,
- o Common Stock Purchase Warrants "B" to purchase an aggregate of 1,250,000 shares of our common stock at an exercise price of \$4.80 per share, and
- o Common Stock Purchase Warrants "C" to purchase an aggregate of 1,250,000 shares of our common stock at an exercise price of \$9.60 per share.

We also issued Liberty Company LLC, a broker dealer which served as finder for us in the transaction, a Common Stock Purchase Warrant "A" to purchase 175,000 shares of our common stock at an exercise price of \$0.70 per share. Other than the exercise price, all other terms of the warrant issued to Liberty Company LLC are identical to the Common Stock Purchase Warrant "A" issued to the purchaser.

The warrants contain a cashless exercise provision which permits the holder, rather than paying the exercise price in cash, to surrender a number of warrants equal to the exercise price of the warrants being exercised. The exercise price of the warrants and the number of shares issuable upon the exercise of the warrants is subject to adjustment in the event of stock splits, stock dividends and reorganizations.

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If we earn between \$.20 and \$.002 per share, on a fully taxed fully diluted basis as reported for the 12 month period ending March 31, 2006 from recurring operations before any non recurring items, the exercise price of the Common Stock Purchase Warrants "A", including the warrant held by the investor and the warrant held by Liberty Company LLC, will be reduced proportionately by 0% if the earnings are \$.20 per share and by 99% if the earnings are \$.002 per share. For example, if we earn \$.15 per share, or 25% below \$.20 per share, then the warrant exercise price will be reduced by 25%. In the event we earn below \$.002 per share, or have a loss, the warrant exercise price will be reduced by 99%. There are no similar provisions which apply to the Common Stock Purchase Warrants "B" or Common Stock Purchase Warrants "C."

In the event we issue any shares, options, warrants, or any instrument convertible into shares or equity in any form below the exercise price of the particular warrant, then the exercise price of the warrant will be reduced proportionately. For example, if we issue shares at \$1.60 per share, or 20% below \$2.00 per share exercise price of the Common Stock Purchase Warrant "A", then the warrant exercise price of that warrant will be reduced by 20%.

No exercise of any warrant can occur if the exercise would result in the holder, Barron Partners LP, and any of its affiliates beneficially owning more than 4.99% of our outstanding common shares following such exercise. Barron Partners LP may waive this provision upon 61 days prior notice to us, or it immediately terminates in the event of a sale or merger of substantially all of our company or upon an underwritten public offering.

WARRANTS ISSUED IN THE SERIES B CONVERTIBLE PREFERRED STOCK TRANSACTION

In connection with the sale of shares of our Series B Convertible Preferred Stock, we issued the purchaser the following common stock purchase

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warrants:

- o Common Stock Purchase Warrants "D" to purchase an aggregate of 1,000,000 shares of our common stock at an exercise price of \$2.00 per share,
- o Common Stock Purchase Warrants "E" to purchase an aggregate of 625,000 shares of our common stock at an exercise price of \$4.80 per share, and
- o Common Stock Purchase Warrants "F" to purchase an aggregate of 625,000 shares of our common stock at an exercise price of \$9.60 per share.

We also issued Liberty Company LLC, a broker dealer which served as finder for us in the transaction, a Common Stock Purchase Warrant "G" to purchase 25,000 shares of our common stock at an exercise price of \$1.00 per share. Other than the exercise price, all other terms of the warrant issued to Liberty Company LLC are identical to the Common Stock Purchase Warrants "E" and "F" issued to the purchaser.

The expiration date of the warrants is five years, or 18 months after effectiveness of a registration statement subsequent to the issuance hereof with such 18 months to be extended by one month for each month or portion of a month during which such registration statement's effectiveness has lapsed or been suspended, whichever is longer. The warrants contain a cashless exercise provision which permits the holder, rather than paying the exercise price in

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cash, to surrender a number of warrants equal to the exercise price of the warrants being exercised. The holder cannot utilize the cashless exercise feature during the first six months of the term or so long as there is an effective registration statement covering the shares of common stock underlying the warrants. The exercise price of the warrants and the number of shares issuable upon the exercise of the warrants is subject to adjustment in the event of stock splits, stock dividends and reorganizations, as well as if we issue common stock or securities convertible into common stock at an effective price less than the then current exercise price of the warrant.

As with the shares of Series B Convertible Preferred Stock, no exercise of these warrants may occur if a conversion would result in the holder, Barron Partners LP, and any of its affiliates beneficially owning more than 4.9% of our outstanding common shares following such exercise. Barron Partners LP may waive this provision only with the consent of all of the Series B Preferred Stockholders and the consent of the holders of a majority of our outstanding shares of common stock who are not affiliates. This limitation, however, immediately terminates as to the warrants in the event of the sale of all or substantially all of our assets or a merger or consolidation in which we are not the surviving entity.

If our common stock trades at or above \$2.85 per share for 20 consecutive trading days, upon notice from us the holder must exercise the Common Stock Purchase Warrant "D" within 45 days, or transfer the warrant to a third party. If the holder elects to so transfer the warrant, the new holder then has an additional 45 days to exercise the Common Stock Purchase Warrant "D". If we have called the warrants and all or any portion of the warrants are not exercised within these respective periods, the unexercised Common Stock Purchase Warrants "D" will terminate.

SERIES H AND SERIES I COMMON STOCK PURCHASE WARRANTS

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In connection with our unit private placement of securities between December 2004 and January 2005, we issued the following common stock purchase warrants to the purchasers:

- o Series H Common Stock Purchase Warrant to purchase an aggregate of 250,000 shares of our common stock at an exercise price of \$4.00 per share expiring on December 31, 2007, and
- o Series I Common Stock Purchase Warrants to purchase an aggregate of 250,000 shares of our common stock at an exercise price of \$8.00 per share expiring on December 31, 2009.

We also issued Cove Partners LLC Series H Common Stock Purchase Warrants to purchase an aggregate of 37,500 shares of our common stock and Series I Common Stock Purchase Warrants to purchase an aggregate of 37,500 shares of our common stock as partial compensation for certain assistance and advisory services to the company, including the structure of financing, strategic planning and business combinations. Cove Partners LLC maintains that it has a right to a greater level of compensation based upon the completion of the private placement. We believe, however, that such claim is without merit.

These warrants contain anti-dilution protection for the holders in the event of reorganization, consolidation or merger. We can call the Series H Common Stock Purchase Warrants at a call price of \$4.00 per underlying common share should our common stock trade at or above \$4.00 per share for 10 consecutive trading days following 15 days' prior written

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notice of our intention to call this warrant. Likewise, we can call the Series I Common Stock Purchase Warrants at a call price of \$8.00 per underlying common share should our common stock trade at or above \$8.00 per share for 10 consecutive trading days following 15 days' prior written notice of our intention to call this warrant. In the event these warrants or warrant series subject to call have not been exercised by written notice within such 15-day notice period, these warrants will cease to exist.

WARRANTS ISSUED IN OUR AUGUST 2001 PRIVATE PLACEMENT

In connection with a private placement of our securities in August 2001, we issued:

- o Series A warrants representing the right to purchase an aggregate of 58,750 shares of our common stock at an exercise price of \$2.40 per share;
- o Series B warrants representing the right to purchase an aggregate of 58,750 shares of our common stock at an exercise price of \$4.80 per share;
- o Series C warrants representing the right to purchase an aggregate of 58,750 shares of our common stock at an exercise price of \$8.00 per share; and
- o Series D warrants representing the right to purchase an aggregate of 58,750 shares of our common stock at an exercise price of \$16.00 per share.

These warrants expire on May 1, 2006. These warrants contain anti-dilution protection for the holders in the event of reorganization,

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consolidation or merger. We can call any of these warrant series or all of the warrants at a call price of \$.01 per underlying share should our common stock trade at or above \$5.00 per share, based on the reported closing bid price of the common stock, for 10 consecutive trading days following 15 days prior written notice of our intention to call the warrants. In the event these warrants or warrant series subject to call have not been exercised by written notice within such 15-day notice period, these warrants will cease to exist.

COMERICA BANK WARRANT

In July 2004, in connection with the granting of a revolving credit line to us we issued Comerica Bank a warrant to purchase 40,000 shares of our common stock at an initial exercise price of \$0.38 per share. The warrant contained anti-dilution protection as described below. As a result of the anti-dilution protection and our subsequent sales of common stock and Series A Convertible Preferred Stock described later in this prospectus under "Selling Security Holders," the number of shares underlying the warrant and the exercise price of the warrant has been adjusted to 5,000 shares with an exercise price of \$2.00 per share.

The warrant is exercisable until July 21, 2011. At the option of the holder, the warrant is convertible into a number of shares of our common stock as determined by dividing the aggregate fair market value of our common stock minus the aggregate exercise price of the warrant by the fair market value of one share of our common stock. In addition, Comerica Bank has right to put the warrant to us at any time on or after July 21, 2006 and we are obligated to pay Comerica Bank \$15,000 upon the exercise of this put.

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The exercise price of the warrant is subject to adjustment in the event we issue or sell shares of our common stock or securities exercisable or convertible into shares of our common stock at a price less than the then effective exercise price as well as in the event of stock splits, stock dividends or recapitalizations.

We granted Comerica Bank registration rights covering the shares of common stock issuable upon the exercise of this warrant. We have included those shares in the registration statement of which this prospectus is a part.

SAND HILL FINANCE, LLC WARRANT

In connection with the Financing Agreement entered into in December 2005 for our accounts receivable factoring arrangement we issued Sand Hill Finance, LLC, the lender, a seven year common stock purchase warrant to purchase 25,000 shares of our common stock at an exercise price of \$1.00 per share. The warrant also contains a cashless exercise provision similar to that which is contained in the Comerica warrant described above. The number of shares issuable upon the exercise of the warrant and the exercise price are subject to adjustment in the event of stock dividends, stock splits and reclassifications.

TRANSFER AGENT

Our transfer agent is Olde Monmouth Stock Transfer Co., Inc., 77 Memorial Parkway, Atlantic Highlands, NJ 07716, and its telephone number is 732-872-2727.

SELLING SECURITY HOLDERS

BACKGROUND OF THE TRANSACTIONS

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This prospectus covers the resale of 7,171,167 shares of our common stock issued or issuable in connection with the following transactions:

UNIT PRIVATE PLACEMENT

Between December 2004 and January 2005, we sold 250,000 units of our securities at a purchase price of \$2.00 per unit to three accredited investors in a private transaction exempt from registration under the Securities Act in reliance on exemptions provided by Section 4(2) and Regulation D of that act. We issued these investors an aggregate of 250,000 shares of our common stock, 250,000 Series H Common Stock Purchase Warrants and 250,000 Series I Common Stock Purchase Warrants. The terms of the warrants are described earlier in this prospectus under "Description of Securities - Series H and Series I Common Stock Purchase Warrants." We received gross proceeds of \$500,000 from this offering. Mr. Joseph Druzak, a member of our Board of Directors since June 2005, was one of the investors in this offering. He was not a member of our Board of Directors at the time of his investment and at the time of his investment there was no agreement or understanding that he would join our board following the investment. Cove Partners LLC, who previously entered into an agreement with the company to provide assistance and advisory services to the company, including the structure of financing, strategic planning and business combinations, introduced the company to two accredited investors and received fees of \$20,000 in cash, 37,500 Series H Common Stock Purchase Warrants and 37,500 Series I Common Stock Purchase Warrants. Cove Partners LLC maintains that it has a right to a greater level of compensation based upon the completion of the private placement. We believe, however, that such claim is without merit.

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We agreed to file a registration statement covering the shares of common stock sold in this offering, including the shares issuable upon the exercise of the warrants, within 120 days from the closing date of the offering. This prospectus is part of that registration statement. We agreed that if we failed to timely file the registration statement, we would be subject to a delayed registration penalty requiring us to issue an additional 1.0% of the total number of shares of our common stock purchased by the investors, including the shares underlying the warrants. Because the registration statement was not filed within 120 days from the closing date of the offering, at June 30, 2005 we are subject to a delayed registration penalty equal to 15,000 shares of our common stock.

SERIES A CONVERTIBLE PREFERRED STOCK TRANSACTION

On March 30, 2005, we entered into a Preferred Stock Purchase Agreement and related agreements with Barron Partners LP. Under the terms of this agreement we sold Barron Partners LP, an accredited investor, 1,666,667 shares of our Series A Convertible Preferred Stock and issued the purchaser the Common Stock Purchase Warrants "A", "B" and "C" to purchase an aggregate of 4,500,000 shares of our common stock at exercise prices ranging from \$2.00 to \$9.60 per share for an aggregate purchase price of \$1,000,000. We received net proceeds of \$900,000 after payment of expenses of \$35,000 and a finder's fee to Liberty Company LLC of \$65,000. We also issued Liberty Company LLC, a broker-dealer, a Common Stock Purchase Warrant "A" exercisable into 175,000 shares of our common stock with an exercise price of \$0.70 per share as additional compensation for its services. We intend to use these proceeds for general working capital and acquisitions. The transaction was exempt from registration under the Securities Act in reliance on an exemption provided by Section 4(2) of that act. The designations, rights and preferences of the Series A Convertible Preferred Stock and terms of the warrants are described earlier in this prospectus under "Description of Securities."

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The Preferred Stock Purchase Agreement provides:

- o we were required to appoint or elect four additional directors, of whom three directors are required to be independent. In addition, the audit and compensation committees of our Board of Directors are to be comprised solely of independent directors. If at any time after the closing our Board of Directors is not comprised of a majority of qualified independent directors, these independent directors do not make up a majority of the members of the audit and compensation committees of the Board of Directors we are required to pay Barron Partners LP liquidated damages of 24% of the purchase price per annum, payable monthly,
- o Messrs. John R. Signorello and James Bond, executive officers of our company, agreed to exchange indebtedness in the principal amount of \$325,000, of which approximately \$170,000 principal amount was then outstanding, into an aggregate of 541,667 shares of our common stock,
- o for period of three years we agreed not to issue any preferred stock, convertible debt or other equity instruments containing reset features. In addition, while the securities issued in the transaction are outstanding, we are prohibited from entering into any financing involving a variable rate feature,
- o Barron Partners LP was given the right of first refusal to participate in any funding transaction by us on a pro rata basis at 94% of the offering price or funding amount received in the transaction,

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- o if we sell notes, shares of our common stock or shares of any class of preferred stock within 24 months from the closing of the offering at an effective price per share of common stock less than the conversion price of the Series A Convertible Preferred Stock then in effect we are required to reduce the conversion price of the Series A Convertible Preferred Stock to this lower price,
- o Mr. Signorello agreed not to sell any shares of our common stock in excess of 1% of our outstanding shares per quarter or at a price less than \$3.00 per share during the two-year period following the closing date. In addition, the remaining officers and directors of our company cannot sell any shares of common stock owned by them for the two year period following the closing date,
- o for a period of two years from the closing date we are prohibited from entering into employment or consulting agreements which provide for any bonus compensation not directly related to increases in our earnings, any car allowances which were not approved by the unanimous vote of our Board of Directors, any anti-dilution or reverse stock split protection, any deferred compensation, any unreasonable compensation or benefit clauses or any termination clauses which exceed one year of salary, unless specifically waived by Barron Partners LP, and
- o for a period of three years from the closing date we agreed not to enter into any new borrowings of more than twice the sum of our EBITDA (earnings before income taxes, depreciation and

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amortization) from recurring operations over the past four quarters, other than short-term borrowings to purchase products to be resold by us.

We agreed to file a registration statement within 30 days of the closing for the common shares underlying the securities sold in this offering and to use our best efforts to cause the registration statement to be declared effective by the SEC within 120 days of the closing date of the transaction. This prospectus is part of that registration statement. We agreed to pay Barron Partners liquidated damages of 36% per annum for each day we did not file this registration statement after the initial 30 day period. As we did not file the registration statement within 30 days from the closing date of the offering, at June 30, 2005 we owed Barron Partners \$36,000 representing the failure to file penalty. In addition, we agreed to pay Barron Partners liquidated damages of 36% per annum for each day this registration statement is not effective beginning on July 30, 2005 through the earlier of the effective date of the registration statement or March 30, 2007. We are unable at this time to predict if we will be subject to the payment of any damages under this provision of our agreement with Barron Partners.

THE SELLING SECURITY HOLDERS

The following table sets forth

- o the name of each selling security holder,
- o the number of shares owned, and
- o the number of shares being registered for resale by each selling security holder.

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The information presented herein is derived from a record list of our stockholders and warrant holders. We may amend or supplement this prospectus from time to time to update the disclosure set forth herein. All of the shares owned by the selling security holders may be offered hereby. Because the selling security holders may sell some or all of the shares owned by them, and because there are currently no agreements, arrangements or understandings with respect to the sale of any of the shares, no estimate can be given as to the number of shares that will be held by the selling security holders upon termination of any offering made hereby. If all the shares offered hereby are sold, the selling security holders will not own any shares after the offering.

| Name of selling security holder | Number of shares owned | Percentage owned before offering | Shares to be offered | Shares to be owned after offering | Percentage owned after offering |
|---------------------------------|------------------------|----------------------------------|-----------------------------|-----------------------------------|---------------------------------|
| Barron Partners LP (1) | 820,373 | 4.9%% | 6,166,667 | 820,373 | 4.9% |
| Barbara Russo (2) | 250,000 | 3.7% | 225,000 | 25,000 | 3.7% |
| Joseph Druzak (3) | 210,126 | 3.2% | 150,000 | 60,126 | 3.2% |
| Nite Capital LP (4) | 375,000 | 5.5% | 375,000 | 0 | n/a |
| Comerica Bank (5) | 5,000 | * | 5,000 | 0 | n/a |
| Liberty Company LLC (6) | 200,000 | 2.6% | 175,000 | 25,000 | 2.6% |
| Cove Partners LLC (7) | 75,000 | * | 75,000 | 0 | n/a |
| | | | ----- 7,171,667 ===== | | |

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* less than 1%

(1) Barron Partners LP holds 1,666,667 shares of our Series A Convertible Preferred Stock which is convertible into 1,666,667 shares of our common stock, 1,833,334 shares of our Series B Convertible Preferred Stock which is convertible into 1,833,334 shares of our common stock and common stock purchase warrants exercisable into 6,750,000 shares of our common stock with exercise prices ranging from \$2.00 to \$9.60 per share. The number of shares offered includes 1,666,667 shares of our common stock issuable upon the conversion of the shares of Series A Convertible Preferred Stock and 4,500,000 shares of common stock issuable upon the exercise of warrants with exercise prices ranging from \$2.00 to \$9.60 per share. Mr. Andrew Barron Worden exercises investment and voting rights over the securities held by Barron Partners LP. Barron Partners LP has contractually agreed that if the number of shares of common stock issuable upon the conversion of the shares of Series A Convertible Preferred Stock and exercise of the related warrants is limited so that Barron Partners LP and any of its affiliates cannot beneficially own more than 4.99% of our outstanding common shares following such exercise or conversion. Barron Partners LP has also contractually agreed that if the number of shares of common stock issuable upon the conversion of the shares of Series B Convertible Preferred Stock and exercise of those related warrants is limited so that Barron Partners LP and any of its affiliates cannot beneficially own more than 4.9% of our outstanding common shares following such exercise or conversion. Barron Partners LP may waive the provision as it relates to the Series A Convertible Preferred Stock and related warrants to purchase 4,500,000 shares of common stock upon 61 days prior notice to us, or it immediately terminates in the event of a sale or merger of substantially all of our company or upon an underwritten public offering. Barron Partners LP may waive this provision as it relates to the Series B Convertible Preferred Stock and related warrants to purchase 2,250,000 shares of common stock only with the consent of the holders of a majority of our issued and outstanding common stock who are not affiliates. As a result of these ownership limitations, at January 15, 2006 Barron Partners LP beneficially owns 820,373 shares of our common stock based upon shares of our Series A Convertible Preferred Stock, Series B Convertible Preferred Stock and warrants which are convertible or exercisable, as the case may be, within 60 days.

(2) The number of shares owned by Mr. Druzak includes 103,126 shares presently outstanding, warrants to purchase 100,000 shares of common stock at exercise prices ranging from \$4.00 to \$8.00 per share and options to purchase 40,000 shares of common stock at an exercise price of \$2.40 per share. The number of shares offered includes 50,000 shares of our common stock presently outstanding and 100,000 shares of our common stock issuable upon the exercise of common stock purchase warrants with exercise prices ranging from \$4.00 to \$8.00 per share.

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(3) The number of shares offered includes 50,000 shares of our common stock presently outstanding and 100,000 shares of our common stock issuable upon the exercise of common stock purchase warrants with exercise prices ranging from \$4.00 to \$8.00 per share. Mr. Druzak has been a member of our Board of Directors since June 2005.

(4) The number of shares offered includes 125,000 shares of our common stock presently outstanding and 250,000 shares of our common stock issuable upon the exercise of common stock purchase warrants with exercise prices ranging from \$4.00 to \$8.00 per share. Mr. Keith Goodman exercises investment and voting rights over the securities held by Nite Capital LP.

(5) The number of shares offered includes 5,000 shares of our common stock issuable upon the exercise of a common stock purchase warrant with an exercise

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price of \$2.00 per share. Mr. Bryan Tom exercises investment and voting rights over the securities held by Comerica Bank. As described earlier in this prospectus under "Description of Securities - Comerica Bank warrant" on page 45, this warrant was issued in connection with the granting of a credit line to us by the bank.

(6) The number of shares owned includes 175,000 shares of our common stock issuable upon the exercise of a common stock purchase warrant with an exercise price of \$0.70 per share and 25,000 shares of common stock issuable upon the exercise of a common stock purchase warrant with an exercise price of \$1.00 per share. The number of shares offered includes 175,000 shares of our common stock issuable upon the exercise of a common stock purchase warrant with an exercise price of \$0.70 per share. Mr. Phil Seifert exercises investment and voting rights over securities held by Liberty Company, LLC.

(7) The number of shares offered includes 37,500 shares of our common stock issuable upon the exercise of common stock purchase warrants with an exercise price of \$4.00 per share and 37,500 shares of our common stock purchase warrants with an exercise price of \$8.00 per share. Mr. Richard A. Mager exercises investment and voting rights over the securities held by Cove Partners LLC.

Liberty Company, LLC is a broker/dealer and a member of the National Association of Securities Dealers, Inc. As described earlier in this section, Liberty Company, LLC received a warrant to purchase 175,000 shares of our common stock as compensation for its services in the ordinary course of its business as a finder in the Series A Convertible Preferred Stock transaction. Liberty Company, LLC also received a warrant to purchase 25,000 shares of our common stock as partial compensation for its services in the ordinary course of its business as a finder in the Series B Convertible Preferred Stock Transaction. To our knowledge, this firm does not have any arrangement with any person to participate in the distribution of such securities. None of the selling security holders has, or within the past three years has had, any position, office or other material relationship with us or any of our predecessors or affiliates, other than as described previously in this section. We are required to pay all fees and expenses incident to the registration of the shares. We have agreed to indemnify the selling security holders against certain losses, claims, damages and liabilities, including liabilities under the Securities Act of 1933. We will not pay selling commissions and expenses associated with any sale by the selling security holders.

PLAN OF DISTRIBUTION

The selling security holders and any of their pledgees, assignees and successors-in-interest may, from time to time, sell any or all of their shares of common stock on any stock exchange, market or trading facility on which the shares are traded or in private transactions. These sales may be at fixed or negotiated prices. The selling security holders may use any one or more of the following methods when selling shares:

- o ordinary brokerage transactions and transactions in which the broker-dealer solicits purchasers;
- o block trades in which the broker-dealer will attempt to sell the shares as agent but may position and resell a portion of the block as principal to facilitate the transaction;

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- o purchases by a broker-dealer as principal and resale by the broker-dealer for its account;

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- o an exchange distribution in accordance with the rules of the applicable exchange;
- o privately negotiated transactions;
- o settlement of short sales;
- o broker-dealers may agree with the selling security holders to sell a specified number of such shares at a stipulated price per share;
- o a combination of any such methods of sale; or
- o any other method permitted pursuant to applicable law.

The selling security holders may also sell shares under Rule 144 under the Securities Act of 1933, if available, rather than under this prospectus.

Broker-dealers engaged by the selling security holders may arrange for other broker-dealers to participate in sales. Broker-dealers may receive commissions or discounts from the selling security holders (or, if any broker-dealer acts as agent for the purchaser of shares, from the purchaser) in amounts to be negotiated. The selling security holders do not expect these commissions and discounts to exceed what is customary in the types of transactions involved.

Broker-dealers may agree to sell a specified number of such shares at a stipulated price per share, and, to the extent such broker-dealer is unable to do so acting as agent for us or a selling stockholder, to purchase as principal any unsold shares at the price required to fulfill the broker-dealer commitment. Broker-dealers who acquire shares as principal may thereafter resell such shares from time to time in transactions, which may involve block transactions and sales to and through other broker-dealers, including transactions of the nature described above, in the over-the-counter markets or otherwise at prices and on terms then prevailing at the time of sale, at prices then related to the then-current market price or in negotiated transactions. In connection with such resales, broker-dealers may pay to or receive from the purchasers of such shares, commissions as described above. In the event that shares are resold to any broker-dealer, as principal, who is acting as an underwriter, we will file a post-effective amendment to the registration statement of which this prospectus forms a part, identifying the broker-dealer(s), providing required information relating to the plan of distribution and filing any agreement(s) with such broker-dealer(s) as an exhibit. The involvement of a broker-dealer as an underwriter in the offering will require prior clearance of the terms of underwriting compensation and arrangements from the Corporate Finance Department of the National Association of Securities Dealers, Inc.

The selling security holder and these broker-dealers and agents and any other participating broker-dealers, or agents may be deemed to be "underwriters" within the meaning of the Securities Act of 1933, in connection with the sales.

The selling security holders may, from time to time, pledge or grant a security interest in some or all of the shares or common stock or warrants owned by them and, if they default in the performance of their secured obligations, the pledgees or secured parties may offer and sell the shares of common stock, from time to time, under this prospectus, or under a supplement to this prospectus under Rule 424 (b) (3) or other applicable provision of the Securities Act of 1933 amending the list of selling security holders to include the pledgee, transferee or other successors-in-interest as selling security holders under this prospectus.

The selling security holders also may transfer the shares of common stock in other circumstances, in which case the transferees, pledgees or other

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successors-in-interest will be the selling beneficial owners for purposes of this prospectus.

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SPECIAL CONSIDERATIONS RELATED TO PENNY STOCK RULES

Shares of our common stock may be subject to rules adopted by the SEC that regulate broker-dealer practices in connection with transactions in "penny stocks". Penny stocks are generally equity securities with a price of less than \$5.00 (other than securities registered on certain national securities exchanges or quoted on the Nasdaq Stock Market, provided that current price and volume information with respect to transactions in those securities is provided by the exchange or system). The penny stock rules require a broker-dealer, prior to a transaction in a penny stock not otherwise exempt from those rules, to deliver a standardized risk disclosure document which contains the following:

- o a description of the nature and level of risk in the market for penny stocks in both public offerings and secondary trading;
- o a description of the broker's or dealer's duties to the customer and of the rights and remedies available to the customer with respect to violation to these duties or other requirements of securities laws;
- o a brief, clear, narrative description of a dealer market, including "bid" and "ask" prices for penny stocks and the significance of the spread between the "bid" and "ask" price;
- o a toll-free telephone number for inquiries on disciplinary actions;
- o definitions of significant terms in the disclosure document or in the conduct of trading in penny stocks; and
- o other information as the SEC may require by rule or regulation.

Prior to effecting any transaction in a penny stock, the broker-dealer also must provide the customer the following:

- o the bid and offer quotations for the penny stock;
- o the compensation of the broker-dealer and its salesperson in the transaction;
- o the number of shares to which such bid and ask prices apply, or other comparable information relating to the depth and liquidity of the market for such stock; and
- o monthly account statements showing the market value of each penny stock held in the customer's account.

In addition, the penny stock rules require that prior to a transaction in a penny stock not otherwise exempt from those rules, the broker-dealer must make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser's written acknowledgment of the receipt of a risk disclosure statement, a written agreement to transactions involving penny stocks, and a signed and dated copy of a written statement. These disclosure requirements may have the effect of reducing the trading activity in the secondary market for a stock that becomes subject to the penny stock rules. Holders of shares of our common stock may have difficulty

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selling those shares because our common stock may be subject to the penny stock rules.

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SHARES ELIGIBLE FOR FUTURE SALE

As of January 15, 2006, we had 6,492,286 shares of common stock issued and outstanding. Of the issued and outstanding shares, approximately 4,755,375 shares of our common stock are "restricted securities." We have included 250,000 shares, which are considered restricted securities in the registration statement of which this prospectus is a part. These shares may be resold by their holders as long as they are covered by a current registration statement or under an available exemption from registration.

In general, Rule 144 permits a stockholder who has owned restricted shares for at least one year, to sell without registration, within a three-month period, up to one percent of our then outstanding common stock. In addition, stockholders other than our officers, directors or 5% or greater stockholders who have owned their shares for at least two years, may sell them without volume limitation or the need for our reports to be current.

We cannot predict the effect, if any, that market sales of common stock or the availability of these shares for sale will have on the market price of the shares from time to time. Nevertheless, the possibility that substantial amounts of common stock may be sold in the public market could adversely affect market prices for the common stock and could damage our ability to raise capital through the sale of our equity securities.

LEGAL MATTERS

The validity of the securities offered by this prospectus will be passed upon for us by Schneider Weinberger & Beilly LLP, 2200 Corporate Boulevard, N.W., Suite 210, Boca Raton, Florida 33431. A partner of the firm is the beneficial owner of 8,125 shares of our common stock.

EXPERTS

Our financial statements as of and for the years ended September 30, 2005 and 2004 included in this prospectus have been audited by Sherb & Co. LLP, independent registered public accounting firm, as indicated in their report with respect thereto, and have been so included in reliance upon the report of such firm given on their authority as experts in accounting and auditing.

ADDITIONAL INFORMATION

We have filed with the SEC the registration statement on Form SB-2 under the Securities Act for the common stock offered by this prospectus. This prospectus, which is a part of the registration statement, does not contain all of the information in the registration statement and the exhibits filed with it, portions of which have been omitted as permitted by SEC rules and regulations. For further information concerning us and the securities offered by this prospectus, we refer to the registration statement and to the exhibits filed with it. Statements contained in this prospectus as to the content of any contract or other document referred to are not necessarily complete. In each instance, we refer you to the copy of the contracts and/or other documents filed as exhibits to the registration statement.

We file annual and special reports and other information with the SEC. Certain of our SEC filings are available over the Internet at the SEC's web site at <http://www.sec.gov>. You may also read and copy any document we file with the

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SEC at its public reference facilities:

Public Reference Room Office
100 F Street, N.E.
Room 1580
Washington, D.C. 20549

You may also obtain copies of the documents at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Callers in the United States can also call 1-202-551-8090 for further information on the operations of the public reference facilities.

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No dealer, sales representative or any other person has been authorized to give any information or to make any representations other than those contained in this prospectus and, if given or made, such information or representation must not be relied upon as having been authorized by the company or any of the underwriters. This prospectus does not constitute an offer of any securities other than those to which it relates or an offer to sell, or a solicitation of any offer to buy, to any person in any jurisdiction where such an offer or solicitation would be unlawful. Neither the delivery of this prospectus nor any sale made hereunder shall, under any circumstances, create an implication that the information set forth herein is correct as of any time subsequent to the date hereof.

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ICEWEB, INC.

PROSPECTUS

_____, 2006

7,171,667 SHARES

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PART II

INFORMATION NOT REQUIRED IN PROSPECTUS

ITEM 24. INDEMNIFICATION OF DIRECTORS AND OFFICERS.

The Delaware General Corporation Law allows us to indemnify each of our officers and directors who are made a party to a proceeding if:

(a) the officer or director conducted himself or herself in good faith;

(b) his or her conduct was in our best interests, or if the conduct was not in an official capacity, that the conduct was not opposed to our best interests; and

(c) in the case of a criminal proceeding, he or she had no reasonable cause to believe that his or her conduct was unlawful. We may not indemnify our officers or directors in connection with a proceeding by or in our right, where the officer or director was adjudged liable to us, or in any other proceeding, where our officer or director are found to have derived an improper personal benefit.

Our by-laws require us to indemnify directors and officers against, to the fullest extent permitted by law, liabilities which they may incur under the circumstances described above.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers or persons controlling the Registrant pursuant to the foregoing provisions, the registrant has been informed that, in the opinion of the Securities and Exchange Commission, such indemnification is against public policy as express in the act and is therefore unenforceable.

ITEM 25. OTHER EXPENSES OF ISSUANCE AND DISTRIBUTION.

The estimated expenses payable by us in connection with the distribution of the securities being registered are as follows:

| | |
|---------------------------------------|-----------|
| SEC Registration and Filing Fee | \$ 3,221 |
| Legal Fees and Expenses* | 35,000 |
| Accounting Fees and Expenses* | 13,500 |
| Financial Printing* | 7,500 |
| Transfer Agent Fees* | 500 |
| Blue Sky Fees and Expenses* | 500 |
| Miscellaneous* | 779 |
| | ----- |
| TOTAL | \$ 61,000 |
| | ===== |

* Estimated

None of the foregoing expenses are being paid by the selling security holders.

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ITEM 26. RECENT SALES OF UNREGISTERED SECURITIES

Following are all issuances of securities by the small business issuer during the past three years which were not registered under the Securities Act of 1933, as amended (the "Securities Act"). In each of these issuances the recipient represented that he was acquiring the shares for investment purposes

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only, and not with a view towards distribution or resale except in compliance with applicable securities laws. No general solicitation or advertising was used in connection with any transaction, and the certificate evidencing the securities that were issued contained a legend restricting their transferability absent registration under the Securities Act or the availability of an applicable exemption therefrom. Unless specifically set forth below, underwriter participated in the transaction and no commissions were paid in connection with the transactions.

Between September 2002 and May 2003, we sold 299,375 units of our securities to 17 accredited investors in a private placement pursuant to exemptions from the registration requirements of the Securities Act available to us under an exemption Section 4(2) and Regulation D of the Securities Act. Each unit consisted of one share of common stock and one common stock purchase warrant. We received gross proceeds of \$239,500.

In August 2003, notes payable totaling \$97,000 plus accrued interest held by two accredited investors were converted to 56,250 shares of our common stock. This issuance was exempt from registration under the Securities Act in reliance on Section 4(2) thereof.

Between June 2003 and April 2004 we sold 593,750 shares of common stock to 14 accredited investors in a private placement exempt from registration under the Securities Act in reliance on an exemption provided by Section 4(2) and Regulation D of that act. We received gross proceeds of \$575,000.

In October 2003, we issued 191,381 shares of our common stock to 12 individuals or entities as consideration for our acquisition of substantially all of the assets of Iplicity, Inc. of Virginia. The recipients were accredited or sophisticated or non-accredited who had such knowledge and experience in business matters that they were capable of evaluating the merits and risks of the prospective investment in our securities. The recipients had access to business and financial information concerning our company. The securities were issued in reliance on an exemption from registration provided by Section 4(2) of the Securities Act.

In May 2004, we acquired substantially all of the assets of DevElements, Inc. of Virginia, including software licenses, source code, potential patents and trademarks, cash, hardware, and equipment. In exchange for the 19% interest in DevElements, we issued to the 20 individuals who were the shareholders of DevElements 187,500 shares of our common stock and options to purchase 187,500 shares of common stock exercisable at a price of \$27.20 per share and expiring May 13, 2009. The recipients were accredited, sophisticated or non-accredited investors who had such knowledge and experience in business matters that they were capable of evaluating the merits and risks of the prospective investment in our securities. The recipients had access to business and financial information concerning our company. The securities were issued in reliance on an exemption from registration provided by Section 4(2) of the Securities Act.

Between December 2004 and January 2005, we sold 250,000 units of our securities at a purchase price of \$2.00 per unit to two accredited investors in a private transaction exempt from registration under the Securities Act in reliance on exemptions provided by Section 4(2) and Regulation D of that act. We issued these investors an aggregate of 250,000 shares of our common stock, 250,000 Series H Common Stock Purchase Warrants and 250,000 Series I Common Stock Purchase Warrants. The terms of the warrants are described earlier in this

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Purchase Warrants." We received gross proceeds of \$500,000 from this offering. Cove Partners LLC, who previously entered into an agreement with the company to provide assistance and advisory services to the company, including the structure of financing, strategic planning and business combinations, introduced the company to two accredited investors and received fees of \$20,000 in cash and common stock purchase warrants to purchase an aggregate of 75,000 shares of our common stock at exercise prices ranging from \$4.00 to \$8.00 per share.

In March 2005, we sold an accredited investor 1,666,667 shares of our Series A Convertible Preferred Stock and issued the purchaser Common Stock Purchase Warrants "A", "B" and "C" to purchase an aggregate of 4,500,000 shares of our common stock at exercise prices ranging from \$2.00 to \$9.60 per share for an aggregate purchase price of \$1,000,000. We received net proceeds of \$900,000 after payment of expenses of \$35,000 and a finder's fee to Liberty Company LLC, a broker dealer, of \$65,000. We also issued Liberty Company LLC a warrant to purchase 175,000 shares of our common stock with an exercise price of \$0.70 per share, the terms of which, other than the exercise price, are identical to the Common Stock Purchase Warrants "A" issued to the investor. We intend to use these proceeds for general working capital and acquisitions. The transaction was exempt from registration under the Securities Act in reliance on an exemption provided by Section 4(2) of that act.

In April 2005 we issued Mr. James Bond, one of our key employees, 125,000 shares of our common stock in satisfaction of \$77,000 owed him which represented the remaining portion of the cash consideration due him under the terms of our purchase of the stock of The Seven Corporation as described earlier in this prospectus. This amount was converted by Mr. Bond in accordance with the terms of the Preferred Stock Purchase Agreement with Barron Partners, L.P. This transaction was exempt from registration under the Securities Act in reliance on an exemption provided by Section 4(2) of that act. The recipient was a sophisticated investor who had such knowledge and experience in business matters that he was capable of evaluating the merits and risks of the prospective investment in our securities. The recipient had access to business and financial information concerning our company.

In April 2005 we also issued 416,667 shares of our common stock to an accredited investor as full payment for amounts due under a promissory note in the principal of \$93,177 and a \$50,000 subscription receivable. This transaction was exempt from registration under the Securities Act in reliance on an exemption provided by Section 4(2) of that act.

In May 2005 we issued a stockholder whom we owe \$150,000 principal plus interest under an unsecured promissory note 125,000 shares of our common stock as consideration for a 10 year extension of the due date of the note. The recipient was an accredited investor and the transaction was exempt from registration under the Securities Act in reliance on an exemption provided by Section 4(2) of that act.

In December 2005, we sold an accredited investor who had previously acquired our Series A Convertible Preferred Stock 1,833,334 shares of our Series B Convertible Preferred Stock and issued the purchaser Common Stock Purchase Warrants "D", "E" and "F" to purchase an aggregate of 2,250,000 shares of our common stock at exercise prices ranging from \$2.00 to \$9.60 per share for an aggregate purchase price of \$500,000. We received net proceeds of \$475,000 after payment of a finder's fee to Liberty Company LLC, a broker dealer, of \$25,000. The proceeds were paid to us through the satisfaction of a liability to the purchaser for funds advanced to us in September 2005. We also issued Liberty Company LLC a warrant to purchase 25,000 shares of our common stock with an exercise price of \$1.00 per share. We intend to use these proceeds for general working capital. The transaction was exempt from registration under the Securities Act in reliance on an exemption provided by Section 4(2) of that act.

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ITEM 27. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

| Exhibit No. | Description of Document |
|-------------|---|
| 2.1 | Agreement and Plan of Reorganization and Stock Purchase Agreement with Disease S.I. Inc.(4) |
| 2.2 | Agreement and Plan of Merger with IceWEB Communications, Inc. (8) |
| 2.3 | Agreement and Plan of Merger with Seven Corporation (9) |
| 3.1 | Certificate of Incorporation (1) |
| 3.2 | Certificate of Amendment to Certificate of Incorporation (1) |
| 3.3 | Certificate of Amendment to Certificate of Incorporation (1) |
| 3.4 | Certificate of Amendment to Certificate of Incorporation (1) |
| 3.5 | Certificate of Amendment to Certificate of Incorporation (2) |
| 3.6 | Certificate of Amendment to Certificate of Incorporation (3) |
| 3.7 | Certificate of Amendment to Certificate of Incorporation (11) |
| 3.8 | Certificate of Designations of Series A Convertible Preferred Stock (12) |
| 3.9 | Certificate of Amendment to Certificate of Incorporation (13) |
| 3.10 | Bylaws (1) |
| 4.1 | Form of Common Stock Purchase Warrant "A" (12) |
| 4.2 | Form of Common Stock Purchase Warrant "B" (12) |
| 4.3 | Form of Common Stock Purchase Warrant "C" (12) |
| 4.4 | Form of Series H Common Stock Purchase Warrant * |
| 4.5 | Form of Series I Common Stock Purchase Warrant * |
| 4.6 | Form of \$0.70 Common Stock Purchase Warrant "A" * |
| 4.7 | Form of Comerica Bank warrant * |
| 4.8 | Form of Common Stock Purchase Warrant "D" (16) |
| 4.9 | Form of Common Stock Purchase Warrant "E" (16) |
| 4.10 | Form of Common Stock Purchase Warrant "F" (16) |
| 4.11 | Form of Sand Hill Finance, LLC Warrant (17) |
| 5.1 | Opinion of Schneider Weinberger & Beilly LLP * |
| 10.1 | Acquisition Agreement with North Orlando Sports Promotions, Inc. (1) |
| 10.2 | Asset Purchase Agreement with Raymond J. Hotaling (5) |
| 10.3 | 2000 Management and Director Equity Incentive and Compensation Plan (6) |
| 10.4 | Stock Purchase Agreement with Health Span Sciences, Inc. (7) |
| 10.5 | Stock Purchase and Exchange Agreement with Interlan Communications (9) |
| 10.6 | Preferred Stock Purchase Agreement dated March 30, 2005 (12) |
| 10.7 | Registration Rights Agreement with Barron Partners LP (12) |
| 10.8 | Asset and Stock Purchase Agreement for iPlicity, Inc.* |
| 10.9 | Asset and Stock Purchase Agreement for DevElements, Inc. of Virginia (15) |
| 10.10 | Form of Loan and Security Agreement with Comerica Bank* |
| 10.11 | Forbearance Agreement* |
| 10.12 | Sublease Agreement for principal executive offices* |
| 10.13 | Demand Promissory Note in the principal amount of \$150,000 to John Signorello* |
| 10.14 | Form of Lease for principal executive offices** |
| 10.15 | Preferred Stock Purchase Agreement for Series B Convertible Preferred Stock (17) |
| 10.16 | Registration Rights Agreement for Series B Convertible Preferred Stock (17) |
| 10.17 | Financing Agreement with Sand Hill Finance, LLC (17) |

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- 14.1 Code of Business Conduct and Ethics*
- 21.1 Subsidiaries of the small business issuer *
- 23.1 Consent of Sherb & Co. LLP **
- 23.2 Consent of Schneider Weinberger & Beilly LLP (contained in such firm's opinion filed as Exhibit 5) *

* previously filed herewith

** filed herewith

- (1) Incorporated by reference to the Form 10-SB, file number 000-27865, filed with on October 28, 1999, as amended.
- (2) Incorporated by reference to the definitive Information Statement on Schedule 14C as filed on June 18, 2001.
- (3) Incorporated by reference to the definitive Information Statement on Schedule 14C as filed on June 26, 2001.
- (4) Incorporated by reference to the Report on Form 8-K as filed on June 6, 2001.
- (5) Incorporated by reference to the Report on Form 8-K as filed on July 26, 2001.
- (6) Incorporated by reference to the definitive Information Statement on Schedule 14C as filed on July 23, 2001.
- (7) Incorporated by reference to the Report on Form 8-K as filed on December 4, 2001.
- (8) Incorporated by reference to the Report on Form 8-K as filed on April 4, 2002.
- (9) Incorporated by reference to the Report on Form 8-K as filed on August 1, 2003.
- (10) Incorporated by reference to the Report on Form 8-K/A as filed on February 20, 2004.
- (11) Incorporated by reference to the definitive Information Statement on Schedule 14C as filed on August 20, 2004.
- (12) Incorporated by reference to the Report on Form 8-K as filed on April 5, 2005.
- (13) Incorporated by reference to the definitive Information Statement on Schedule 14C as filed on April 4, 2005.
- (14) Incorporated by reference to Amendment No. 1 to the Report on Form 8-K/A as filed on February 20, 2004.
- (15) Incorporated by reference to the Report on Form 8-K as filed on July 23, 2004.
- (16) Incorporated by reference to the Annual Report on Form 10-KSB for the fiscal year ended September 30, 2005.
- (17) Incorporated by reference to the Report on Form 8-K as filed on January 30, 2006

ITEM 28. UNDERTAKINGS

The undersigned small business issuer will:

(1) File, during any period in which it offers or sells securities, a post-effective amendment to this registration statement to:

(i) Include any prospectus required by Section 10(a)(3) of the Securities Act;

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(ii) Reflect in the prospectus any facts or events which, individually or together, represent a fundamental change in the information in the registration statement; and notwithstanding the foregoing, any increase or decrease in volume of securities offered (if the total dollar value of securities offered would not exceed that which was registered) and any deviation

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from the low or high end of the estimated maximum offering range may be reflected in the form of prospectus filed with the Commission pursuant to Rule 424(b) if, in the aggregate, the changes in the volume and price represent no more than a 20% change in the maximum aggregate offering price set forth in the "Calculation of Registration Fee" table in the effective registration statement; and

(iii) Include any additional or changed material information on the plan of distribution.

(2) For determining liability under the Securities Act, the small business issuer will treat each post-effective amendment as a new registration statement of the securities offered, and the offering of the securities at that time to be the initial bona fide offering.

(3) File a post-effective amendment to remove from registration any of the securities that remain unsold at the end of the offering.

Insofar as indemnification for liabilities arising under the Securities Act of 1933 (the "Act") may be permitted to directors, officers and controlling persons of the small business issuer pursuant to the foregoing provisions, or otherwise, the small business issuer has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the small business issuer of expenses incurred or paid by a director, officer or controlling person of the small business issuer in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the small business issuer will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Act and will be governed by the final adjudication of such issue.

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SIGNATURES

In accordance with the requirements of the Securities Act of 1933, the registrant certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form SB-2 and authorized this registration statement to be signed on its behalf by the undersigned, thereunto duly authorized, in City of Herndon, State of Virginia on January 30, 2006.

ICEWEB, INC.

By: /s/ John R. Signorello

John R. Signorello, CEO
Principal executive officer

By: /s/ Brian E. Crooks

Brian E. Crooks, CFO
Principal financial and accounting officer

In accordance with the requirements of the Securities Act of 1933, this registration statement was signed by the following persons in the capacities and on the dates stated:

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| Signature ----- | Title ----- | Date ---- |
|---|---|------------------|
| /s/ John R. Signorello ----- John R. Signorello | CEO and director, principal executive officer | January 30, 2006 |
| /s/ * ----- G. Anthony Munno | President | January 30, 2006 |
| /s/ Brian E. Crooks ----- Brian E. Crooks | CFO and principal financial and accounting officer | January 30, 2006 |
| /s/ * ----- Hal Compton | Director | January 30, 2006 |
| /s/ * ----- Raymond J. Pirtle, Jr. | Director | January 30, 2006 |
| /s/ * ----- Joseph Druzak | Director | January 30, 2006 |
| ----- Jack Bush | Director | January 30, 2006 |
| * By: /s/ John R. Signorello ----- John R. Signorello Attorney-in-Fact | | January 30, 2006 |

The foregoing represents a majority of the Board of Directors.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors
IceWEB, Inc.

We have audited the accompanying consolidated balance sheet of IceWEB, Inc. and Subsidiaries as of September 30, 2005 and the related consolidated statements of operations, changes in stockholders' equity and cash flows for the years ended September 30, 2005 and 2004. These consolidated 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 audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by

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management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of IceWEB, Inc. and Subsidiaries, as of September 30, 2005 and the consolidated results of their operations and their cash flows for the years ended September 30, 2005 and 2004, in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 13 to the consolidated financial statements, the Company had net losses in operations of \$903,508 and \$2,035,443 respectively, for the years ended September 30, 2005 and 2004. These matters raise substantial doubt about the company's ability to continue as a going concern. Management's plans in regards to these matters are also described in Note 13. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Sherb & Co., LLP
 Certified Public Accountants

Boca Raton, Florida
 January 12, 2006

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IceWEB, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEET

September 30, 2005

Assets

Current assets:

| | |
|---|------------|
| Cash | \$ 557,175 |
| Accounts receivable, net of allowance for bad debt of \$5,846 | 1,577,460 |
| Prepaid expense | 25,979 |
| Advances | 61,302 |
| | ----- |
| Total current assets | 2,221,916 |

Non-current assets:

| | |
|--|---------|
| Property and equipment, net | 259,852 |
| Goodwill | 41,800 |
| Deposits | 16,170 |
| Customer relationships, net of accumulated amortization of \$1,711,199 . | 68,525 |
| Deferred financing costs, net of accumulated amortization of \$20,000 .. | 180,000 |

 Total Assets

| | |
|--|--------------|
| | \$ 2,788,263 |
|--|--------------|

Liabilities and Stockholders' equity

Current liabilities:

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| | |
|---|--------------|
| Note payable | \$ 461,269 |
| Accounts payable | 904,910 |
| Accrued expenses | 37,488 |
| Deferred revenue | 4,275 |
| Advances from related party | 86,001 |
| Preferred stock to be issued | 408,836 |
| Total current liabilities | 1,902,779 |
| Non-current liabilities | |
| Note payable - related party | 215,625 |
| ----- | |
| Total Liabilities | 2,118,404 |
| ----- | |
| Stockholders' equity: | |
| Preferred stock (par value \$.001; 1,000,000 shares authorized; Series A Convertible Preferred Stock, par value .001, 1,666,667 shares issued and 1,666,667 shares outstanding) | 1,667 |
| Common stock (par value \$.001 1,000,000,000 shares authorized) 6,492,287 issued, and 6,329,787 outstanding | 6,493 |
| Stock subscription receivable | (143,477) |
| Additional paid in capital | 7,318,831 |
| Accumulated deficit | (6,500,655) |
| Treasury Stock, at cost, (162,500 shares) | (13,000) |
| ----- | |
| Total Stockholders' Equity | 669,859 |
| ----- | |
| Total Liabilities and Stockholders' Equity | \$ 2,788,263 |
| ----- | |

See accompanying notes to consolidated financial statements

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IceWEB, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS
For the years ended September 30, 2005 and 2004

| | 2005 | 2004 |
|----------------------------------|--------------|--------------|
| | ----- | |
| Revenue | \$ 6,809,590 | \$ 6,662,652 |
| Cost of sales | 4,753,276 | 5,015,494 |
| ----- | | |
| Gross profit | 2,056,314 | 1,647,158 |
| Operating expenses: | | |
| Marketing and selling | 56,538 | 125,414 |
| Stock compensation expense | - | 2,600 |
| Research and development | - | 580,053 |
| Depreciation expense | 51,096 | 52,716 |
| General and administrative | 1,994,168 | 1,947,392 |
| Amortization expense | 782,764 | 948,435 |

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| | | |
|---|--------------|----------------|
| Total operating expense | 2,884,566 | 3,656,610 |
| Operating loss | (828,252) | (2,009,452) |
| Rental revenue | 19,284 | 34,888 |
| Interest expense | (94,540) | (60,879) |
| Net loss | \$ (903,508) | \$ (2,035,443) |
| Basic and diluted loss per share | \$ (0.15) | \$ (0.40) |
| Weighted average common shares outstanding - basic and diluted | 5,865,935 | 5,049,368 |

See accompanying notes to consolidated financial statements

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IceWEB, Inc. and Subsidiaries
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
For the years ended September 30, 2005 and 2004

| | Common Stock | | Preferred Stock | | Subscription Receivable | Additional Paid-In | Accumulated Deficit | |
|--|--------------|---------|-----------------|--------|----------------------------|-----------------------|------------------------|-----|
| | Shares | Amount | Shares | Amount | | | | |
| Balance at September 30, 2003 | 4,512,610 | \$4,513 | - | - | \$ - | \$2,315,291 | \$(2,561,704) | |
| Sale of common stock | 390,000 | 390 | - | - | - | 413,210 | - | |
| Common stock issued in acquisitions . | 378,881 | 379 | - | - | - | 1,706,109 | - | |
| Common stock issued for the exercise of common stock options | 151,000 | 151 | - | - | (52,000) | 137,160 | - | |
| Common stock issued for settlement ... | 1,250 | 1 | - | - | - | 2,599 | - | |
| Common stock cancelled | (3,750) | (4) | - | - | - | 4 | - | |
| Treasury stock | - | - | - | - | - | - | - | (1) |
| Net loss for the year | - | - | - | - | - | - | (2,035,443) | |
| Balance at | | | | | | | | |

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| | | | | | | | | |
|--|-----------|---------|-----------|---------|--------------|-------------|----------------|-----|
| September 30, 2004 | 5,429,991 | \$5,430 | - | - | \$ (52,000) | \$4,574,373 | \$ (4,597,147) | (1) |
| Preferred A stock issued . for cash | - | - | 1,666,667 | \$1,667 | | 844,169 | | - |
| Preferred A Stock Dividend | - | - | - | - | - | 1,000,000 | (1,000,000) | |
| Common stock issued | 503,129 | 503 | - | - | - | 469,477 | | - |
| Common stock issued in satisfaction of liabilities | 541,667 | 542 | - | - | (91,477) | 403,230 | | - |
| Common stock issued for exercise of common stock options | 17,500 | (18) | - | - | - | 27,582 | | - |
| Net loss for the year | - | - | - | - | - | - | (903,508) | |
| ===== | | | | | | | | |
| Balance at September 30, 2005 | 6,492,287 | \$6,493 | 1,666,667 | 1,667 | \$ (143,477) | \$7,318,831 | \$ (6,500,655) | (1) |
| ===== | | | | | | | | |

See accompanying notes to consolidated financial statements

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IceWEB, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS
For the years ended September 30, 2005 and 2004

| | 2005 | 2004 |
|--|--------------|----------------|
| | ----- | ----- |
| CASH FLOWS FROM OPERATIONS: | | |
| Net Loss | \$ (903,508) | \$ (2,035,443) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Common stock and options issued for settlement | - | 2,600 |
| Depreciation and amortization | 833,860 | 1,001,151 |
| Interest from stock issued for note payable .. | 37,500 | - |
| Changes in operating assets and liabilities: (Increase) decrease in: | | |
| ----- | | |
| Accounts receivable | (514,753) | (672,934) |
| Prepaid expense | (25,979) | 8,056 |
| Advances | (61,302) | - |
| Deposits | - | (3,505) |
| Increase (decrease) in: | | |
| ----- | | |
| Accounts payable | (156,489) | 856,363 |

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| | | |
|---|------------|------------|
| Accrued expense | (115,089) | 43,236 |
| Deferred revenue | (14,755) | 5,615 |
| ----- | ----- | ----- |
| NET CASH USED IN OPERATING ACTIVITIES | (920,515) | (794,861) |
| ----- | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of property and equipment | (224,698) | (10,183) |
| Cash acquired in acquisitions, net | - | 37,637 |
| Increase in Intangibles | (8,526) | - |
| ----- | ----- | ----- |
| NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES | (233,224) | 27,454 |
| ----- | ----- | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| (Payments on) proceeds from line of credit ... | - | 334,269 |
| Payments to related parties | (219,616) | (43,805) |
| Proceeds from Preferred Stock to be issued ... | 408,836 | - |
| Proceeds from related party | - | 65,499 |
| Common stock issued for cash | 469,477 | 413,600 |
| Preferred stock issued for cash | 845,836 | - |
| Exercise of common stock options | 27,600 | 85,311 |
| Purchase of treasury stock | - | (13,000) |
| ----- | ----- | ----- |
| NET CASH PROVIDED BY FINANCING ACTIVITIES | 1,532,133 | 841,874 |
| ----- | ----- | ----- |
| NET INCREASE IN CASH | 378,394 | 74,467 |
| CASH - beginning of year | 178,781 | 104,314 |
| CASH - end of year | \$ 557,175 | \$ 178,781 |

Non-cash investing and financing activities:

| | |
|--|------------|
| Common stock issued for debt and interest..... | \$ 270,000 |
| Common stock issued for subscription receivable..... | \$ 143,177 |
| Cash paid for interest..... | \$ 28,725 |

See accompanying notes to consolidated financial statements

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ICEWEB, INC and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Years ended September 30, 2005 and 2004

NOTE 1 - ORGANIZATION

IceWEB, Inc. began trading publicly in April 2002. In June 2003, the Company added two subsidiaries, acquiring all of the outstanding stock of Interlan Communications Incorporated and The Seven Corporation. Interlan is a full service provider of computer equipment and integration services. The Seven Corporation provides network engineering services. On October 5, 2003, the Company acquired the software ownership rights and customers of Iplicity, Inc.

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of Virginia. Iplicity had developed a complete content management software platform based on open source architecture to run in any operating environment. On May 13, 2004, the Company, through its wholly owned subsidiary Propster, Inc., acquired substantially all of the assets of DevElements, Inc. of Virginia. DevElements is a professional IT consultancy firm that designs, develops and implements web-based productivity solutions for customers. Utilizing resources gained through acquisitions, the company has developed two applications that are now available to the general public, IceWEB Vista which is a website portal development and management application, and IceMAIL which is a hosted Microsoft Exchange application service. In addition to the new application services, IceWEB also continues to provide customers with systems integration, network consulting, and customized software application services.

On October 13, 2004, the Company affected a 10:1 forward split of its common stock. Additionally, the Company amended its Articles of Incorporation to increase its authorized number of shares to 1,000,000,000. All amounts presented in these financial statements have been retroactively restated to give effect to the forward split of the Company's stock.

On April 27, 2005, the Company affected a 1:80 reverse split of its issued and outstanding common stock. All amounts have been retroactively adjusted to reflect this split.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Cash and Cash Equivalents

The Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents.

(b) Accounts Receivable

Accounts Receivable consists of normal trade receivables. The Company recorded a bad debt allowance of \$5,846 for the year ended September 30, 2005. Management performs ongoing evaluations of its accounts receivable and customer base. Management believes that all remaining receivables are fully collectable. Bad debt expense is \$3,127 and \$20,086 for the years ended September 30, 2005 and 2004, respectively.

(c) Revenue Recognition

Generally, revenues from sales of products are recognized when products are shipped unless the Company has obligations remaining under sales or licensing agreements, in which case revenue is either deferred until all obligations are satisfied or recognized ratably over the term of the contract. Revenue from services is recorded each month as it is earned. Commissions earned on third party sales are recorded in the month in which contracts are awarded. Customers are generally billed every two weeks based on the units of production for the project. Each project has an estimated total which is based on the estimated units of production and agreed upon billing rates.

(d) Property and Equipment

Property and equipment are stated at cost, and depreciation is provided by use of the straight-line method over the estimated useful lives of the assets.

(e) Earnings Per Share

The Company computes earnings per share in accordance with Statement of Accounting Standards No. 128, "Earnings per Share ("SFAS No. 128"). Under the provisions of SFAS No. 128, basic earnings per share is computed by dividing the net income (loss) for the period by the weighted average number of common shares

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outstanding during the period. Diluted earnings per share is computed by dividing the net income (loss) for the period by the weighted average number of common and potentially dilutive common shares outstanding during the period.

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Potentially dilutive common shares consist of the common shares issuable upon the exercise of stock options and warrants (using the treasury stock method) and upon the conversion of convertible preferred stock (using the if-converted method). Potentially dilutive common shares are excluded from the calculation if their effect is antidilutive.

(f) Stock Based Compensation

The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations including FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation an interpretation of APB Opinion No. 25" issued in March 2000, to account for its fixed plan stock options. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS No. 123 and SFAS No. 148, "Accounting for Stock-Based compensation," established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic value-based method of accounting described above, and has adopted the disclosure requirements of SFAS No. 123 and SFAS No. 148.

(g) Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the balance sheets and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

(h) Goodwill and Intangible Assets

Goodwill represents the amount by which the purchase price of a business acquired exceeds the fair market value of the net assets acquired under the purchase method of accounting. The Company assesses whether its goodwill and other intangible assets are impaired as required by SFAS No. 142, "Accounting for the Impairment of Long-Lived Assets," based on an evaluation of undiscounted projected cash flows through the remaining amortization period. If impairment exists, the amount of such impairment is calculated based on the estimated fair value of the asset. Customer relationships have been book as intangible assets and amortized over the life of the customer contracts. The Company has amortized these intangible assets in the amount of \$762,764 and \$948,435 respectively, for the year ended September 30, 2005 and 2004. The Company has not recognized any impairment of goodwill during the year ended September 30, 2005 and 2004.

(i) Recent Accounting Pronouncements

In December 2004, the FASB issued SFAS 153 "Exchanges of Non-Monetary Assets" - an amendment of APB Opinion No. 29. This Statement amended APB Opinion 29 to eliminate the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. A non-monetary exchange has commercial substance if the future cash flows of the entity are expected to change

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significantly as a result of the exchange. The adoption of this Standard is not expected to have any material impact on the Company's financial position, results of operations or cash flows.

In December 2004, the FASB issued SFAS 123 (revised 2004) "Share-Based Payment". This Statement requires that the cost resulting from all share-based transactions be recorded in the financial statements. The Statement establishes fair value as the measurement objective in accounting for share-based payment arrangements and requires all entities to apply a fair-value-based measurement in accounting for share-based payment transactions with employees. The Statement also establishes fair value as the measurement objective for transactions in which an entity acquires goods or services from non-employees in share-based payment transactions. The Statement replaces SFAS 123 "Accounting for Stock-Based Compensation" and supersedes APB Opinion No. 25 "Accounting for Stock Issued to Employees". The provisions of this Statement will be effective for the Company beginning with its fiscal year ending in 2007. The Company is currently evaluating the impact this new Standard will have on its financial position, results of operations or cash flows.

(j) Reclassifications

Certain reclassifications have been made to the prior years' financial statements to conform to the current year presentation. These reclassifications had no effect on previously reported results of operations.

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NOTE 3 - PROPERTY AND EQUIPMENT

The major classes of property and equipment are as follows:

| | ESTIMATED USEFUL LIFE | 9/30/2005 |
|--------------------------------|--------------------------|------------|
| Computer equipment | 3 years | \$ 223,369 |
| Computer software | 3 years | 163,314 |
| Furniture and fixtures | 5 years | 30,133 |
| Vista and IceMAIL Software | 3 years | 154,734 |
| Electrical generator equipment | 5 years | 45,000 |
| | | ----- |
| Total property and equipment | | 616,550 |
| Less: accumulated depreciation | | (356,698) |
| | | ----- |
| Property and equipment, net | | \$ 259,852 |
| | | ===== |

Depreciation expense for the years ended September 30, 2005 and 2004 was \$51,096 and \$52,716 respectively.

NOTE 4 - OPERATING LEASES

The Company leases office space in Herndon, VA. Total rental expense for the years ended September 30, 2005 and 2004 was \$152,921 and \$103,037, respectively. The Company also leases facilities for one of its subsidiaries at \$2,100 per month. This lease continues through June 30, 2006.

The Company has lease agreements with Dell Financial, for computer equipment, and one lease with GE Capital for an office copy and fax machine. These leases were entered into by the companies acquired during the year. The total minimum

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lease obligation for the office space and equipment leases combined for the next five fiscal years is as follows:

| Fiscal Year | Amount |
|-------------|------------|
| ----- | ----- |
| 2006 | \$ 45,488 |
| 2007 | \$ 45,488 |
| 2008 | \$ 26,535 |
| 2009 | \$ - |
| 2010 | \$ - |
| | ----- |
| | \$ 117,511 |
| | ===== |

NOTE 5 - RELATED PARTY TRANSACTIONS

A Stockholder has a loan totaling \$150,000 plus accrued interest of approximately \$65,625. Of this amount, \$150,000 bears interest at a rate of 12.5% per annum. The Company has issued the note holder 125,000 shares of common stock in exchange for the individual to extend the maturity date of the note by 10 years to September 30, 2014. The cost associated with these shares has been accounted for as deferred finance charges, and are being amortized over the life of the deferral period. The shares were valued at \$200,000 the fair value at the date of issuance. An employee has a loan totaling \$61,602 payable on demand along with 6% annual interest. This item is shown separately on the balance sheet as employee advances. This employee is not an executive officer of the company.

The Chief Executive Officer of the Company, from time to time, provides advances to the Company for operating expenses. These advances are short-term in nature and non-interest bearing.

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NOTE 6 - NOTE PAYABLE

On July 21, 2004, the Company entered into a Loan and Security agreement with Comerica Bank, to obtain a revolving credit line in the amount of \$500,000. At September 30, 2005, the amount outstanding was \$461,269. The term of the agreement is 364 days from the date of closing. The Company has extended the term of the agreement through December 31, 2005. The terms of the agreement gives Comerica Bank a first position on the Company's assets. In addition this note is collateralized by the assets of the Company. Advances on the credit line bear interest at a variable rate equal to one (1) percentage point above the Prime Rate. The Prime Rate is defined as that most recently announced by Comerica Bank as its "prime rate", whether or not such rate is the lowest available from the Bank. The agreement includes financial covenants for a Quick Ratio of at least 1.00 to 1.00 and Tangible Net Worth of \$390,000 through January 30, 2006. The Tangible Net Worth increases incrementally thereafter.

At September 30, 2005, the Company does meet the financial covenants for Quick Ratio and Tangible Net Worth. The Company did not meet these covenants during the year and on November 18, 2004, the Company executed a Forbearance and Consent agreement with Comerica Bank, which recognizes the default and contains certain forbearances by the Bank from enforcing rights and exercising remedies in connection with the default. This forbearance has been extended to December 31, 2005. On December 23, 2005, the Company entered into a credit facility for \$1,000,000 with Sand Hill Finance which effectively closed the facility with Comerica Bank.

NOTE 7 - CONCENTRATION OF CREDIT RISK

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The Company maintains its cash bank deposits at various financial institutions which, at times, may exceed federally insured limits. Accounts are guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000. At September 30, 2005 the Company had approximately \$522,204 in excess of FDIC insured limits. The Company has not experienced any losses in such accounts.

NOTE 8 - MAJOR CUSTOMERS

Sales to two customers represented approximately 37% and 34% of total sales for the years ended September 30, 2005 and 2004, respectively. As of September 30, 2005 approximately 53% of the Company's accounts receivable were due from these two customers.

NOTE 9 - INCOME TAXES

As of September 30, 2005 the Company had an unused net operating loss carry forward of approximately \$4,881,102 available for use on its future corporate federal tax returns. The Company's evaluation of the tax benefit of its net operating loss carry forward is presented in the following table. The tax amounts have been calculated using the Company's effective income tax rate resulting from the use of graduated rates.

| | 2005 |
|---|--------------|
| | ---- |
| Deferred tax asset: | |
| Tax benefit of net operating loss carry forward | \$ 1,835,294 |
| Less: valuation allowance | (1,835,294) |
| | ----- |
| Total deferred tax asset | \$ - |
| | ===== |

The table below summarizes the differences between the Company's effective tax rate and the statutory federal rate as follows for fiscal 2005:

| | 2005 |
|---|---------|
| | ---- |
| Computed "expected" tax expense (benefit) | (34.0)% |
| State income taxes | (3.6)% |
| Change in valuation allowance | 37.6% |
| Effective tax rate | 0.0% |

The effective tax rate is 34% Federal and 6% Virginia State reduce by 2.4% Federal tax benefit.

Net operating loss carry forward expires between 2021 and 2025. The utilization of the above loss carry forwards, for federal income tax purposes may be subject to limitations resulting from changes in ownership.

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NOTE 10 - STOCKHOLDERS' EQUITY

During the year ended September 30, 2005, the Company sold 503,129 shares of common stock to accredited investors for \$469,477 exempt from registration pursuant to Section 4(2). The investors were sophisticated and had access to the consolidated financial statements of the corporation. The Company issued 541,667 shares of common stock for cash and in exchange for or assumption of liabilities in the total amount of \$403,230. During the year ending September 30, 2004, the Company sold 390,000 shares of common stock for \$413,600.

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During the year ended September 30, 2005, 17,500 shares of common stock were issued in connection with the exercise of stock options.

The Company issued 470,250 stock options to employees under the Company's stock option plan (See Note 12).

During the year ended September 30, 2004, the Company sold 390,000 shares of common stock to accredited investors for \$413,600 exempt from registration pursuant to Section 4(2). The investors were sophisticated and had access to the consolidated financial statements of the corporation. During the year ending September 30, 2003, the Company sold 596,250 shares of common stock for \$422,000.

On October 4, 2003, the Company issued 191,381 shares of common stock as part of the acquisition agreement with Iplicity, Inc (See Note 10).

On May 13, 2004, the Company issued 187,500 shares of common stock as part of the acquisition agreement with DevElements, Inc.

The Company is authorized to issue 10,000,000 shares of Series A Preferred Stock, par value \$.001, with such designations, rights and preferences as may be determined from time to time by the Board of Directors. During the year ended September 30, 2005, the Company sold 1,666,667 shares of preferred stock for \$845,836. There are currently 1,666,667 shares of Series A Preferred Stock issued and outstanding.

NOTE 11 - STOCK OPTION PLAN

During March 2002, the Company adopted the "Management and Director Equity Incentive and Compensation Plan." The maximum number of shares authorized and available under the plan is 1,250,000 shares. Under the terms of the plan, the options expire after 5 years, as long as the employees remain employed with the Company. The following is a summary of option activity for the years ended September 30, 2005:

A summary of the status of the Company's outstanding stock options as of September 30, 2005 and changes during the period ending on that date is as follows:

| | Shares | Weighted Average Exercise Price |
|--|-----------|------------------------------------|
| Outstanding at September 30, 2003 | 487,750 | \$2.75 |
| Granted | 847,000 | 1.21 |
| Exercised | (151,000) | (2.25) |
| Forfeited | (327,619) | (2.01) |
| | 856,131 | \$1.99 |
| Outstanding at September 30, 2004 | | |
| Granted | 470,250 | 1.21 |
| Exercised | - | - |
| Forfeited | (443,902) | (2.01) |
| | 882,479 | \$1.55 |
| Outstanding at September 30, 2005 | | |
| Options exercisable at end of period | 882,479 | \$1.55 |

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Weighted-average fair value of options granted
during the period 470,250 \$1.21

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Common stock warrants

The following information applies to all warrants outstanding at September 30, 2005:

| Range of Exercise Prices | Shares | Warrants Outstanding | | Warrants Exercisable | |
|--------------------------------|-----------|--|--|----------------------|--|
| | | Weighted Average Remaining Contractual Life (Years) | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price |
| \$ 0.70 | 175,000 | 4.5 | \$ 0.70 | 175,000 | \$ 0.70 |
| \$ 2.00 | 2,000,000 | 4.5 | \$ 2.00 | 2,000,000 | \$ 2.00 |
| \$ 4.80 | 1,250,000 | 4.5 | \$ 4.80 | 1,250,000 | \$ 4.80 |
| \$ 9.60 | 1,250,000 | 4.5 | \$ 9.60 | 1,250,000 | \$ 9.60 |
| \$ 4.00 | 250,000 | 2.25 | \$ 4.00 | 250,000 | \$ 4.00 |
| \$ 8.00 | 250,000 | 4.25 | \$ 8.00 | 250,000 | \$ 8.00 |
| \$ 2.40 | 58,750 | 7 months | \$ 2.40 | 58,750 | \$ 2.40 |
| \$ 4.80 | 58,750 | 7 months | \$ 4.80 | 58,750 | \$ 4.80 |
| \$ 8.00 | 58,750 | 7 months | \$ 8.00 | 58,750 | \$ 8.00 |
| \$16.00 | 58,750 | 7 months | \$16.00 | 58,750 | \$16.00 |
| \$ 2.00 | 5,000 | 5.75 | \$ 2.00 | 5,000 | \$ 2.00 |
| \$ 4.00 | 37,500 | 2.25 | \$ 4.00 | 37,500 | \$ 4.00 |
| \$ 8.00 | 37,500 | 4.25 | \$ 8.00 | 37,500 | \$ 8.00 |

The employee option grants provide that the option will be canceled ninety days after an employee leaves employment with the Company.

SFAS No. 123 "Accounting for Stock Based Compensation" ("SFAS 123") and SFAS No. 148 "Accounting for Stock-Based Compensation - Transition and Disclosure" ("SFAS 148") requires the Company to disclose pro forma information regarding option grants made to its employees. SFAS 123 specifies certain valuation techniques that produce estimated compensation charges that are included in the pro forma results below. These amounts have not been reflected in the Company's Statement of Operations, because Accounting Principles Board Opinion 25, "Accounting for Stock Issued to Employees," specifies that no compensation charge arises when the price of the employees' stock options equal the market value of the underlying stock at the grant date, as in the case of options granted to the Company's employees

SFAS No. 123 pro forma results are as follows for the fiscal year periods ended September 30, 2005 and 2004:

| | 2005 | 2004 |
|----------------------------|--------------|--------------|
| | ---- | ---- |
| Actual net loss | \$ 903,508 | \$ 2,035,443 |
| SFAS 123 Compensation Cost | 380,479 | 237,198 |
| | ----- | ----- |
| Pro forma net loss | \$ 1,283,987 | \$ 2,272,641 |
| | ===== | ===== |

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| | | |
|--|-----------|-----------|
| Proforma basic and diluted 2005 net loss per share | \$ (0.22) | \$ (0.08) |
| | ===== | ===== |

Under SFAS 123, the fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The following weighted average assumptions were used:

| | |
|-------------------------|------|
| Risk free interest rate | 4% |
| Expected dividends | 0 |
| Volatility factor | 111% |

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion the existing models do not necessarily provide a reliable single measure of the fair value of the Company's options.

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NOTE 12 - SIGNIFICANT CUMSTOMER INFORMATION AND SEGMENT REPORTING

SFAS No. 131, Disclosure about Segments of an Enterprise and Related Information, establishes standards for the reporting by business enterprises of information about operating segments, products and services, geographic areas, and major customers. The method for determining what information to report is based on the way that management organizes the operating segments with IceWEB for making operational decisions and assessments of financial performance.

IceWEB's chief operating decision-maker is considered to be the chief executive officer (CEO). The CEO reviews financial information presented on a consolidated basis for purposes of making operating decisions and assessing financial performance. The financial information reviewed by the CEO is identical to the information presented in the accompanying consolidated statements of operations. Therefore, IceWEB has determined that it operates in a single operating segment, specifically, web communications services. For the periods ended September 30, 2005 and 2004 all material assets and revenues of IceWEB were in the United States.

NOTE 13 - GOING CONCERN

The Company's auditors stated in their reports on the financial statements of the Company for the years ended September 30, 2004 and 2003 that the Company is dependent on outside financing and has had losses since inception that raise substantial doubt about our ability to continue as a going concern.

For the year ended September 30, 2005, the Company incurred net annual losses of (\$903,508) and used cash in operations of \$920,515. The financial statements do not include any adjustments relating to the recoverability and classification of recorded assets, or the amounts and classification of liabilities that might be necessary in the event the Company cannot continue in existence.

Management has established plans intended to increase the sales of the Company's products and services. Management intends to seek new capital from new equity securities offerings to provide funds needed to increase liquidity, fund growth and implement its business plan; however, no assurance can be given that the Company will be able to raise any additional capital.

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NOTE 14 - CONTINGENCIES

From time to time the Company faces litigation in the ordinary course of business. Currently, we are involved with litigation with two prior employees, which in our opinion will not have a material adverse effect on our financial condition. The two related lawsuits have been filed against the Company in the Circuit Court of Fairfax County, Virginia, captioned Bonnie Edenfield vs. IceWEB, Inc., et al., Chancery No. CH 2005 4303; and Christopher MacDonald vs. IceWEB, Inc., et al., Chancery No. CH 2005 4304. Both suits are brought by former shareholders of DevElements, Inc., the assets of which were purchased by a Company subsidiary. Edenfield and MacDonald were parties to the asset purchase agreement between DevElements and the Company subsidiary. The plaintiffs seek money damages from the Company for alleged breach of the asset purchase agreement, and damages related to stock options. The Company intends to vigorously defend this litigation. The Company believes the litigation is without merit.

NOTE 15 - SUBSEQUENT EVENTS

On December 23, 2005, the Company entered into a credit facility for \$1,000,000 with Sand Hill Finance which effectively closed the facility with Comerica Bank.

On December 28, 2005, the Company consummated the sale of 1,833,333 shares of Series B Convertible Preferred Stock to Barron Partners, L.P. and issued the purchaser common stock purchase warrants to purchase an aggregate of 2,250,000 shares of the Company's common stock for an aggregate purchase price of \$500,000. The purchase price was paid through the satisfaction of a liability to Barron Partners, L.P. for funds advanced to the Company in September 2005.

In the event the Company sells, grants or issues any shares, options, warrants, or any instrument convertible into shares or equity in any form below \$2.00 per share the warrant exercise price shall be reduced proportionately. For example, if the Company sells, grants or issues any shares, options, warrants, or any instrument convertible into shares or equity in any form at \$1.60 per share, or 20% below \$2.00 per share, then the warrant exercise price shall be reduced by 20%. Such reduction shall be made at the time such transaction is made, and shall be cumulative upon any other changes to the exercise of the warrant that may already have been made.

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No exercise of any warrant can occur if the exercise would result in the holder, Barron Partners LP, and any of its affiliates beneficially owning more than 4.9% of our outstanding common shares following such conversion. Barron Partners LP may waive this provision only with the consent of all of the Series B Preferred Stock Holders and the consent of the holders of a majority of the shares of outstanding Common Stock of the Company who are not affiliates.

All of these five-year warrants are exercisable on a cashless basis which means that the holders, rather than paying the exercise price in cash, may surrender a number of warrants equal to the exercise price of the warrants being exercised. The utilization of this cashless exercise feature will deprive us of additional capital which might otherwise be obtained if the warrants did not contain a cashless feature.

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