

E-SMART TECHNOLOGIES INC

Form 10KSB

October 24, 2007

Table of Contents

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**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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**FORM 10-KSB**

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**ANNUAL REPORT UNDER SECTION 13 OR 15(d)**

**OF THE SECURITIES EXCHANGE ACT 1934:**

For the Fiscal Year Ended December 31, 2006

Commission File Number: 0-30717

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**E-SMART TECHNOLOGIES, INC.**

(Name of Small Business Issuer in its Charter)

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**Nevada**  
(State of Incorporation)

**88-0409261**  
(I.R.S. Employer Identification No.)

**526 West 26<sup>th</sup> Street, Suite 710, New York, NY 10001**

(Address of Principal Executive Office, including Zip Code)

**(212) 727-3790**

(Issuer's Telephone Number)

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**Securities registered under Section 12(g) of the Exchange Act:**

**COMMON STOCK, \$.001 PAR VALUE**

(Title of Class)

## Edgar Filing: E-SMART TECHNOLOGIES INC - Form 10KSB

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

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

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

Issuer's revenues for the two years ended December 31, 2006: **\$ -0-**

The aggregate market value of Common Stock held by non-affiliates at September 20, 2007: **\$7,046,197**

Shares of Common Stock, \$.001 par value, outstanding at December 31, 2006: **242,540,441 shares.**

### **DOCUMENTS INCORPORATED BY REFERENCE:**

**No documents are incorporated by reference into this Annual Report.**

**Transitional Small Business Disclosure Format (check one):** Yes  No

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**Table of Contents**

**Table of Contents**

**PART I**

|         |  |    |
|---------|--|----|
| ITEM 1. | <u>Description of Business</u>                             | 3  |
| ITEM 2. | <u>Description of Property</u>                             | 16 |
| ITEM 3. | <u>Legal Proceedings</u>                                   | 16 |
| ITEM 4. | <u>Submission of Matters to a Vote of Security Holders</u> | 17 |

**PART II**

|           |  |    |
|-----------|--|----|
| ITEM 5.   | <u>Market for the Registrant's Common Equity, Related Stockholder Matters and Small Business Issuer Purchases of Equity Securities</u> | 18 |
| ITEM 6.   | <u>Management's Discussion and Analysis or Plan of Operations</u>  | 19 |
| ITEM 7.   | <u>Financial Statements</u>  | 20 |
| ITEM 8.   | <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>  | 32 |
| ITEM 8-A. | <u>Controls and Procedures</u>   | 32 |

**PART III**

|          |  |    |
|----------|--|----|
| ITEM 9.  | <u>Directors, Executive Officers, Promoters and Control Persons; Compliance With Section 16(a) of the Exchange Act</u> | 34 |
| ITEM 10. | <u>Executive Compensation</u>  | 39 |
| ITEM 11. | <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>                  | 41 |
| ITEM 12. | <u>Certain Relationships and Related Transactions</u>  | 43 |
| ITEM 13. | <u>Exhibits and Reports on Form 8K</u>   | 44 |
| ITEM 14. | <u>Principal Accountant Fees and Services</u>  | 45 |
|          | <u>SIGNATURES</u>  | 47 |
|          | <u>EXHIBIT INDEX</u>   | 48 |
|          | CERTIFICATIONS   |    |

## **Table of Contents**

### **Safe Harbor Statement**

Certain statements contained herein constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. We desire to avail ourselves of certain safe harbor provisions of the 1995 Reform Act and are therefore including this special note to enable us to do so. Forward-looking statements included in this Report on Form 10-KSB involve known and unknown risks, uncertainties, and other factors which could cause our actual results, performance (financial or operating) or achievements to differ from our best estimate of future results, performance (financial or operating) or achievements expressed or implied by such forward-looking statements. These risks include, but are not limited to, risks related to recently consummated acquisitions as well as future acquisitions, our ability to increase our revenues and generate income from operations, effects of competition and technological changes, risks related to exposure to personal injury and workers compensation claims, risks that our insurers may not provide adequate coverage, risks associated with compliance with government regulations such as ERISA, state and local employment regulations and dependence upon key personnel.

We believe it is important to communicate our expectations to our investors. There may be events in the future, however, that we are not able to accurately predict or over which we have no control. The risk factors listed below, as well as any cautionary language in this report, provide examples of risks, uncertainties and events that may cause our actual results to differ materially from the expectations we described in our forward-looking statements. Before any investment is made in our securities, be aware that the occurrence of any of the events described in the risk factor section and elsewhere in this report, and other events that we have not predicted or assessed could have a material adverse effect on our ability to transition out of the development stage. In such case, the price of our securities could decline and any investor may lose all or part of the investor's investment.

## **PART I**

### **ITEM 1. DESCRIPTION OF BUSINESS**

#### **Business Overview**

e-Smart Technologies, Inc. (the Registrant or the Company), is engaged in the business of creating, marketing, manufacturing, installing, operating and maintaining biometric identification verification systems which utilize biometric technology to positively authenticate each end user of any networked or local access system while protecting all information residing on or transported by the system. The Company's products are designed to provide assurance that the user is the person that he or she claims to be and has the credentials to access the premises or information being sought.

Pursuant to grants of rights from IVI Smart Technologies, Inc. ( IVI ) we own the exclusive license for certain technologies for the U.S.A. and Asia except China. In addition, and through our wholly owned subsidiary e-Smart Systems, Inc., a Nevada corporation, we own the exclusive license for use in China of the smart card technology and any and all other smart card related assets originally developed or otherwise owned by IVI. This technology is, we believe, the most advanced biometrically protected, multi-application smart card solution currently available.

We have limited operations, and, in accordance with SFAS #7, we are considered a development stage company. We have an administrative office located at 526 West 26<sup>th</sup> Street, Suite 710, New York, NY 10001. Our registered agent in the State of Nevada is The Corporation Service Company and our transfer agent is Holladay Stock Transfer Company of Scottsdale, Arizona. Our common stock trades in the over-the-counter market under the symbol ESMT.PK. Our telephone number is (212) 727-3790.

## **Table of Contents**

### **Industry Overview: The Challenge of Secure Identity Verification**

The business of the Company is focused on the development, manufacturing, marketing and maintaining of proprietary systems which accomplish secure verification of personal identities. Protection and verification of our personal identities is emerging as one of the major critical challenges facing governments and individuals today. The increasing globalization of our personal and financial interactions, and the threats that arise from those interactions, is fueling a growing demand for the means by which to employ verified personal identification systems to enhance our physical and financial security. Identity verification will continue to be a cornerstone of both physical security (airports, border crossings, buildings) and our financial security (merchants, ATMs, etc.). Online, protection and verification of our virtual identities is even more important. We use our virtual identities for online access to almost everything we do. As financial systems increasingly involve online activity, we project our virtual identities to our banks, brokerage accounts, and merchants worldwide. Currently there is no widely-accepted consumer solution for biometric verification of identity, and both the public and private sector are actively seeking a biometric product that will reliably and efficiently satisfy increasing demand. At e-Smart, we believe that we offer the most advanced product and biometric technology currently available to accomplish this critical function of identity verification and meet the needs of this expanding market.

### **The e-Smart Solution:**

#### **The Super Smart Card**

During 2006, e-Smart continued the development and refinement of its core technology, its state-of-the-art Super Smart Card and Biometric Verification System (BVS<sup>®</sup>) designed to accomplish immediate, local recognition of a person's fingerprint. One of the key attributes of the Company's design, which we believe makes it unique from all other smart cards and systems, is its Match-on-Card capability: our product design features an on-board biometric matching engine which enables the card to perform identification verification without reference to any external database.

Our product design combines that Match-on-Card capability with an on-board digital fingerprint sensor, which is water-proof, ESD proof, scratch-proof and can detect liveness. While others in the industry also use fingerprints for personal identification, those other products and systems require a controlled environment for a fragile sensor, considerable electrical power, a remote database (subject to hacking), and a powerful computer to execute the comparison. In contrast, e-Smart has designed a rugged, low-power system that executes a fingerprint match entirely internally, in less than one second. This system can be embedded inside a credit card format, integrated into official documents such as passports, or packaged in any number of configurations for an almost unlimited variety of applications. This system is designed for demanding consumer applications such as a card form that will be flexible, waterproof, tamperproof, resistant to shock and mechanical and magnetic damage. There are a number of patents pending to protect this unique technology.

The e-Smart product is also dual interface, i.e., it will work either in conjunction with a reader that requires physical contact with the card to supply power and transfer data, or with a reader that does not require physical contact, as power and data are transferred to each card through an electro-magnetic field generated by such a card reader.

## **Table of Contents**

Other attributes and competitive advantages of the Super Smart Card design, which have been discussed at length in prior filings, include the following:

*Unique Sensor On-Card.* A key component of the Super Smart Card design is its fingerprint sensor. The Super Smart Card will contain a thin (.33 mm thin), low power consumption sensor that will be durable enough to be embedded in a smart card and yet not effected by static electricity, the elements or the condition (wet, dry, hot, cold) of the user's skin. Fingerprint Imaging will occur in 3D based on micro-pressure variations across the sensor surface caused by the ridges and valleys existing in one's fingerprint. Only the fingerprint of the registered user will activate the card. The system will prevent unauthorized use of any card or card application by requiring the authorized cardholder's fingerprint to activate the microprocessor inside and to initiate any transaction or to access any information.

*Fraud-proof, counterfeit-proof and hack-proof.* We believe that the physical characteristics of each Super Smart Card will cause tampering to permanently disable it and destroy any information contained therein. We also believe based on technical innovations contained within each Super Smart Card that counterfeit cards will not work on the system thereby rendering any fake cards useless;

*Hardware Based, Software Enhanced, Multi-Application System.* One card can contain multiple, independent and secure applications. For example, the technology will permit/deny access (physical and/or logical), identify precise location and/or movement of personnel and/or watch list parties while at the same time operating other secure applications, each completely and securely isolated one from the other;

*The Zero/Zero System.* e-Smart is continuing to develop its Zero False Acceptance Zero False Reject system which is believed by us to be unique in the field of biometrics. In the normal course, when setting a biometric system, the closer to theoretical zero false acceptances you set your matching system for, the further you get from zero false rejections. Based on our internal studies, our Zero/Zero System, using a patent pending technique that combines human factors with mechanical factors, reduces the false reject rate to approximately 0.5% on the first use and less than 0.2% after the third to fifth use of the system by each new user. This reduction in the false rejection rate is particularly significant when dealing with high volume transport such as border crossings and airports.

We believe that we are the first, and currently the only company offering a commercially available dual ISO 7816 (contact) and ISO 14443 B (wireless) compatible smart card with a fingerprint sensor onboard, biometric matching engine onboard and a multi-application processor for deployment today.

### **The Biometric Identification Verification System**

Our products are designed to operate on a common platform which we refer to as the Biometric Identification Verification Security System ( BVS2 ). The BVS2 platform, which is based on pending patent application and proprietary technology, consists of the Super Smart Card, readers, operational software and a communication technology that ensures that the transmission of data throughout the system is secure and reliable.

To ensure the security of all information transmitted through the system, we have continued the development and refinement of means by which to encrypt and protect all data from unauthorized access. Our solution, referred to as Presto-Chango, is designed to cause information to become indecipherable if there is any attempt to access or transport data without verification of identity and authorization.

BVS2 transactions are routed through the BVS2 Universal Gateway subsystem which is designed to accomplish translation of and access to diverse database systems.

## **Table of Contents**

### **Card Readers**

The card reader is the means by which the Super Smart Card communicates with the BVS2 platform. We intent to offer an array of readers including a handheld wireless device, an interface module compatible with most standard PDAs and notebooks.

### **Our Strategy**

Key elements of our strategy include:

*Enhance Technological Position.* We intend to continue to invest in research and development in order to enhance our technological position, develop new technologies, extend the functionality of our products and services, and offer innovative products to our customers.

*Expand Domestic Market Presence.* We are continuing marketing efforts focused on the security needs of the United States. In particular, we have targeted various agencies within the Department of Homeland Security, including but not limited to the Bureau of Immigration and Customs Enforcement and the Transportation Security Administration. We intend to continue our marketing efforts to these and other agencies both on a direct basis and on a partnering basis with major U.S. domestic systems integrators in line with these agencies' current policy of awarding virtually all major contracts to established system integrators such as Accenture, EDS, SAIC and Titan.

*Expand Global Market Presence.* The global market for biometric identification cards is already substantial and growing rapidly, increasing by over 50% annually in some segments. The Company has focused on specific regions where it can demonstrate substantial results and earn a significant market share, particularly South Korea. Building on its proven marketing and management talent in that region, the Company is expanding its physical operations in South Korea to include an engineering and development facility, and transferring personnel and technology to South Korea to intensify its focus on that market.

The South Korean market offers three distinct advantages: (1) excellent partners for manufacturing and production, (2), talented technical workforce who are trained and experienced in smart card technologies, and (3) a large population of consumers with the highest adoption rate for new technology of any country in the entire world. Both the South Korean government and South Korean consumers actively support and promote adoption of new technology. The South Korean national legislature has passed a law requiring that all financial services cards issued in South Korea after 2007 have smart card capability as well as a magnetic strip. Further, this legislation requires that the banks assume 100% of any financial loss from stolen or lost credit cards. As a result, card issuers in South Korea are eager to test and adopt new solutions such as the Super Smart Card offered by e-Smart.

At the consumer level, South Koreans adopt new technologies very quickly. With a population of 47 million people, the country supports over 150 million financial services cards, over three cards for every person in the entire country. Seoul and other major cities use AFC (automatic fare collection) systems for the mass transit systems that operate wirelessly, using the 14443b ISO standard. The city government of Seoul is driving this payment system to be extended to taxis, schools, libraries, and other public services. In summary, at every level from the national government to municipalities to individual consumers, South Korea is in the vanguard in initiating and adopting cashless financial service solutions. These solutions will require secure personal identification, such as the Super Smart Card offered by e-Smart Technologies.

The Company has established manufacturing partnerships with several South Korean production companies, each a world leader in its specific niche. The Company is also in the process of retaining additional engineers and developers with experience in wireless communications, payment systems, hardware miniaturization, and electronic packaging. The team is continuing its efforts to develop and refine its software and conform its hardware to high-volume, low-cost manufacture and operation.

## **Table of Contents**

The Company seeks, through its South Korean subsidiary, to focus on particular contracts to accomplish these high-volume applications, with high-visibility. These include applications for access control (both government and commercial) as well as financial services applications in South Korea. The Company has previously disclosed contracts in the South Korean market and will disclose further developments as appropriate.

### **Marketing and Distribution**

We intend to continue to market our products directly, through our Homeland Defense, Inc. affiliate (inactive to date), and through e-Smart Korea. We are also continuing to develop strategic relationships with systems integrators and others. Our sales and marketing efforts will be directed from our offices in Seoul, South Korea, New York and Washington, DC.

### **Proprietary Technologies**

The Company has continued to develop and refine its extensive portfolio of intellectual property through its relationship with IVI which filed 4 new patent applications in 2006. Because the market for its technology is global, IVI also files its patents under the Patent Cooperation Treaty.

e-Smart is currently the owner of three technology licenses from IVI Smart and IVI has agreed to issue new licenses to e-Smart relating to all refinements of the technology, all biometric and smart card related technologies, and/or all technology derivative of the existing technologies. Each license is granted pursuant to an Exclusive Use and Distribution Agreement (collectively the License Agreements), which grant to the Company exclusive rights to use and exploit the technology in particular territories. Those licenses cover all of Asia and the United States of America. The rights to technology granted to the Company include all smart card, biometric and related assets of the licensor including the Super Smart Card, the BVS2 platform and all relevant components thereof. The License Agreements require that all inventions and improvements developed by e-Smart be assigned to the licensor with a license to use granted back to the Company on the same terms and conditions as the technology was granted in the original license. IVI and e-Smart are jointly responsible to protect and defend the technology in the event of challenge or dispute in a covered territory.

### **Competition**

While we believe that there is no product that can directly compete with the Super Smart Card and the BVS2, there are numerous products and competitors in the smart card and smart card operating system arena. We must, therefore, anticipate competition in sales of our products, systems and technologies from other providers of microprocessor-based smart card technologies. We expect competition to intensify as, and if, we become successful in our deployment plans and our competitors commit greater resources to the development of biometrically empowered contactless microprocessor-based smart cards. Some of the larger chip manufacturers that operate in the smart card market, including Atmel, STM, Infineon and Philips Semiconductors, have announced that they are developing contactless microprocessor-based smart cards. However, we know of no card planned or otherwise that has the sophistication and features of the Super Smart Card.

We also compete with contactless ASIC-based technologies developed primarily by Philips Semiconductors, which comply with ISO 14443 and which are used by some of the largest manufacturers of smart cards, including Gemplus, Giesecke & Devrient, and Sony's contactless ASIC based technology. Further, we also compete with contact-based products such as microprocessor-based contact cards, ASIC-based contact cards, memory chip cards and magnetic strip cards.

We believe that all of these cards offer inferior functionality compared to our dual interface, biometrically powered, contactless microprocessor-based smart cards. Nevertheless, some of our potential customers have in the past, and may in the future, consider these alternatives sufficient for their needs.



## **Table of Contents**

### **Employees**

As of December 31, 2006, the Company maintained an aggregate of 12 full time employees. Our Chief Executive Officer, President and Chief Financial Officer, Mary A. Grace, maintains a home in Washington D.C. but travels more than 95% of the time on our behalf. Our Chief Technical Officer, Tamio Saito, maintains a residence in San Jose, CA and in South Korea where he oversees our research and engineering, and also travels extensively in connection with his responsibilities within the Company. Two employees work in the New York office and oversee administrative aspects of marketing, managerial and financial functions.

The Managing Director of e-Smart Korea is Richard Kun In Kim. The Company maintains an office in South Korea where it conducts its engineering and research function since June 2007.

None of our employees is a party to a collective bargaining agreement.

### **Recent Developments:**

#### **Termination of Consulting Relationship**

Effective June 2006, the Company's consulting relationships with Wayne Drizin and Associated Business Group were terminated. The Company thereafter commenced an investigation into the activities of Mr. Drizin and Associated Business Group. As reflected in prior filings, Mr. Drizin had been a key consultant to the Company and so the Company immediately took steps to ensure that his departure would not affect the operations of the Company. Those steps included the identification and retention of another consultant who, in 2007, joined the Company as its Chief Operating Officer.

Based on the results of its investigation regarding Mr. Drizin and other consultants, the Company filed a civil action on or about September 11, 2006 in the Northern District of California against former consultants including Wayne Drizin for misappropriation of property of the Company. Discovery has not been completed and the action is continuing.

#### **Additional Patents Filed**

In 2006, IVI filed new patents related to developments in its biometric technology, and is in the process of filing additional patents relating to further refinements of the technology. IVI has licensed the use of that technology to the Company.

#### **Letter of Intent and Agreement with MYBi, Inc.**

The Strategic Alliance Agreement with MYBi, remains in force and effect and the Company is continuing to take the requisite steps relating to the contractual conditions set forth in that agreement. The Company anticipates that it will commence manufacture and delivery of product pursuant to that agreement during 2007.

#### **Shareholders Authorize Increase in Common Shares and Board Recommendations**

During July 2006, a majority of the Company's shareholders consented to the reappointment of Mary A. Grace, Elliot Cole, and Tom Volpe to the Board of Directors and the election of Charles R. Black and Gary Messina to fill the two board appointments which expired in July 2006. Shareholders also approved an amendment to our Certificate of Incorporation which increased the number of authorized shares of Common and Preferred Stock, both of which have a par value of \$.001, from 200,000,000 to 500,000,000.

Shareholders of record at the close of business on May 15, 2006 were entitled to notice of this action by written consent. Because the actions had already been approved by holders of a majority of the outstanding shares of our voting stock, no proxies were solicited. The increase in authorized shares became effective on or about July 15, 2006.

## **Table of Contents**

### **Plan of Reorganization and Recapitalization.**

Pending resolution of issues associated with negotiation of long term financing, the Company has continued to delay full implementation of its Planned Reorganization and Recapitalization (the "Planned Reorganization"). That comprehensive reorganization, previously approved by the shareholders and the Board, is intended to further the goals of receipt of permanent financing, movement to a national securities exchange, and maximizing of shareholder value, includes the following terms and conditions: IVI will grant continuing access and licenses to existing and after developed biometric and smart card related technologies; IVI will forgive indebtedness previously incurred by the Company; IVI will forgive the obligation of the Company to issue additional shares in relation to further financing provided in 2006 and additional shares for additional technology licenses, IVI will surrender its current common stock holdings of the Company; in exchange for that forgiveness of indebtedness, issuance of additional stock for loans in 2006, and surrender of its existing holdings, IVI will receive Preferred Series A shares with 70% voting control of the Company. The Company anticipates that the Planned Reorganization will be implemented during 2007, to the extent that it remains consistent with the Company's efforts to procure long term financing and enhance shareholder value.

### **Risk Factors**

The following risks with respect to the Company's proposed business and its financial condition should be carefully considered. These risks and uncertainties are not the only ones facing us. Other risks and uncertainties that have not been predicted or assessed by us may also adversely affect us. Some of the information in this report contains forward-looking statements that involve substantial risks and uncertainties. These statements can be identified by forward-looking words such as may, will, expect, anticipate, believe, intend, estimate, and continue similar words. Statements that contain these words should be carefully read for the following reasons:

The statements may disclose our future expectations;

The statements may contain projections of our future earnings or our future financial condition; and

The statements may state other forward-looking information.

#### **Risks Related to Our Business**

*We have no history of revenue from operations and we have only minimal assets.*

As of the date of this report, we have yet to generate any revenue from operations. Our assets are comprised principally of the contracts we have signed and our licenses of the smart card intellectual property from IVI Smart. In all likelihood, we will continue to incur pre-operating expenses without corresponding revenues for some time in the foreseeable future. This may result in continuing increases in our net operating loss until we can generate cash flow from operations. There can be no assurance that we will be successful in developing our proposed operations or that we will ever become profitable.

*We are undercapitalized and may be unable to continue our business unless we raise additional money.*

We have limited working capital unless and until additional funding is obtained or until delivery on our contracts. At this point, we remain dependent upon proceeds derived from private securities offerings. We will need to obtain additional financing in order to implement all the material aspects of our business plan. There can be no assurance that additional financing will be available to us on acceptable terms, if at all. If we continue to raise funds by issuing additional equity securities, further dilution to existing equity holders will necessarily result. Accordingly, we are subject to all of the risks inherent in starting a new business enterprise including the potential loss of all monies invested.

## **Table of Contents**

*We may not be able to operate successfully if we are unable to hire qualified additional personnel.*

We continue to seek additional qualified management with the expertise we believe we require for success. Our success may largely be dependent on the personal efforts and abilities of our management and our ability to attract and retain qualified key personnel in the future. Except for Tamio Saito, our Chief Technical Officer, none of our management team has ever operated a smart card business or has any experience with the manufacture and marketing of smart card products. In addition to performing their regular duties, our management must currently devote a significant amount of time to devising strategies to finance and execute our business model.

*We are presently highly dependent upon three people.*

Our ultimate success or failure will depend to a large extent on the services and efforts of our executive and operating officer, Mary A. Grace, Tamio Saito, Chief inventor of our BVS2 and Super Smart Card technology, and the Managing Director of e-Smart Korea, Richard In Kun Kim. The loss of the services of any one or more of these key persons, especially during the period prior to the installation and successful operation of our first biometric card and BVS2 based products and related technologies system, will have a material adverse effect on the continued economic viability of our Company. Since we believe that Mr. Saito is the individual best able to continue to refine, to present and to customize the use of our system and oversee its installation, and that Ms. Grace and Mr. Kim are essential managers, the untimely demise, unavailability or disability of one or more of these four persons, would leave us without the ability to pursue, procure and fulfill contracting opportunities or possibly even to continue our business.

*We have no Key Man Insurance.*

Presently, we do not maintain any key man life insurance. The lack of key man coverage and the lack of other such insurance may have a material adverse effect upon our business in the event of the untimely loss of any of our key employees.

*We have no director's and officer's liability insurance*

The employment of other qualified officers and directors may be contingent upon our acquiring a policy of directors and officers liability insurance in an amount reasonably satisfactory to such nominees. Our failure to acquire such a policy may prevent us from attracting the services of other qualified officers and directors.

*We have a history of losses and may not achieve profitability in the foreseeable future.*

We have incurred losses in each year since our inception. Our losses resulted primarily from expenses we incurred in research and development, selling and marketing, as well as general and administrative expenses. We have never had any revenue. We expect to continue to incur operating losses in future periods as we invest in the expansion of our global operations and continue to enhance our research and development capabilities and expand our relationship with contract manufacturers.

*If the market for smart cards in general, and for biometric, multi-application-based smart cards in particular, does not grow as we expect, we may not succeed in selling our products.*

The success of our products depends on commercial enterprises, governmental authorities and other potential card issuers adopting biometric multi-application based smart card technologies. Other card technologies, such as magnetic strips or bar codes, are widely used and could be viewed by potential customers as more cost effective alternatives to our products. Additionally, potential customers in developed countries such as the United States may already have installed systems that are based on technologies different than ours and may therefore be less willing to incur the capital expenditure required to install or upgrade to a biometric multi-application-based smart card system. As a result, we cannot provide any assurance that there will be significant market opportunities for smart card systems. If demand for biometric multi-application-based smart card products such as ours does not develop or develops more slowly than we anticipate, we may have fewer opportunities for growth than we expect.

## **Table of Contents**

*If we fail to develop new products or adapt our existing products for use in new markets, our revenue growth may be impeded and we may incur significant losses.*

To date, we have not implemented any advanced Super Smart Card and BVS2 System. We are continuing to develop our technology for use as an identification and payment card, for use by governmental authorities, banks and commercial enterprises. We have not yet received revenues from sales of these products. We are devoting significant resources to developing and marketing these and other products and adapting our existing products for use in new markets. If we fail to develop markets for our products we will not generate revenues and will continue to incur significant losses.

*Our inability to maintain our current, and establish new, strategic relationships could impair our revenue growth.*

In accordance with our business model, we plan and have entered into strategic relationships in order to facilitate or accelerate our penetration into new markets. The termination of any of our strategic relationships or our failure to develop additional relationships in the future may limit our ability to develop markets or to sell particular products, and thereby impair our revenue growth.

*We face intense competition. If we are unable to compete successfully, our business prospects will be impaired.*

We face intense competition from developers of contact and contactless microprocessor-based technologies and products, developers of contactless products that use other types of technologies that are not microprocessor-based, and non-smart card technologies. We compete on a range of competitive factors including price, compatibility with the products of other manufacturers, and the ability to support new industry standards and introduce new reliable technologies. Many of our competitors, such as Phillips Semiconductors, a division of Phillips Electronics N.V., and Infineon Technologies AG, have greater market recognition, larger customer bases, and substantially greater financial, technical, marketing, distribution, and other resources than we possess. As a result, they may be able to introduce new products, respond to customer requirements and adapt to evolving industry standards more quickly than we can. The announcement of new or enhanced products may cause customers to delay or alter their purchasing decisions in anticipation of such products, and new products developed by our competitors may render our products obsolete or achieve greater market acceptance than our products.

*If there is a sustained increase in demand for components, availability might be limited and prices might increase.*

Our products require components including microprocessors and other silicon based chips, the availability of which may be limited. The microprocessor industry periodically experiences increased demand and limited availability due to production capacity constraints. Increased demand for, or limited availability of, microprocessors could substantially increase the cost of producing our products. In addition, as a result of a shortage, we may be forced to delay shipments of our products, or devote additional resources to maintaining higher levels of microprocessor inventory. Consequently, we may experience substantial period-to-period fluctuations in our cost of revenues and, therefore, in our future results of operations.

*Our products have long development cycles and we may expend significant resources in relation to a specific project without realizing any revenues.*

The projects which will involve use of our product will be complex and will require that we customize our products to our customers' needs and specifications. We will be required to undergo evaluation, testing, implementation and acceptance procedures of the customized products with the customer. Only after successful completion of these procedures will customers place orders for our products in commercial quantities, if any. We, therefore, cannot provide an assurance that contracts that we enter into will result in commercial sales. As a result, we may expend financial, management and other resources to develop customer relationships before we become capable of recognizing revenues, if any.

## **Table of Contents**

*We are dependent on a small number of suppliers for critical components, delays or discontinuance of the supply of components may hamper our ability to produce our products on a timely basis and cause short-term adverse effects.*

The components we use in our products, including microprocessors and cards, are supplied by third party suppliers and manufacturers. Many of these suppliers are our sole suppliers. Although we are now in the process of securing additional sources of supply, in the meantime, we may experience short-term adverse effects due to delayed shipments that will delay the supply of our products to our customers, and that may result in cancellation of orders for our products. In addition, we do not generally have long term supply contracts under which our suppliers are committed to supply us with components at a fixed price. Suppliers could increase component prices significantly without warning or could discontinue the manufacture or supply of components used in our products. We may not be able to develop alternative sources for product components if, and as, required in the future. Even if we are able to identify any alternative source of supply, we may need to modify our products to be compatible with other components, which may cause delays in product shipments, increase manufacturing costs and increase product prices.

Because some of our suppliers are located in Europe and the Far East, we may experience logistical problems in our supply chain, including long lead times for receipt of products or components and shipping delays.

*If we fail to hire, train and retain qualified research and development personnel, our ability to enhance our existing products, develop new products and compete successfully may be materially and adversely affected.*

Our success depends, in part, upon our ability to hire, train and retain qualified research and development personnel. Individuals who have expertise in research and development in our industry are scarce. Competition for such personnel is intense in the electronics industry, particularly in the United States, and therefore hiring, training and retaining such personnel is both time consuming and expensive. If we fail to hire, train and retain employees with skills in research and development, we may not be able to enhance our existing products or develop new products.

*Our ability to compete depends on our continuing right to use, and our ability to protect, our intellectual property rights.*

Our technology is licensed from IVI Smart (see *Proprietary Technologies* ). Our success and ability to compete depends in large part on using our licensed intellectual property and proprietary rights to protect the technology we use and the products we make. We rely on a combination of patent, trademark, copyright and trade secret law, as well as confidentiality agreements and other contractual relationships with our employees, customers, affiliates, distributors and others.

Our licensor currently has patents pending in the United States, Europe, Japan and elsewhere that have not yet resulted in granted patents. We cannot be certain that patents will be issued with respect to any of these pending or future patent applications or that the scope of any future patents that are issued to our licensor will provide us with adequate protection for our technology and products. Others may challenge these patents or registered trademarks. We do not know whether any of them will be upheld as valid or will be enforceable against alleged infringers and thus we do not know whether they will enable us to prevent or hinder the development of competing products or technologies. Moreover, patents provide legal protection only in the countries where they are registered and the extent of the protection granted by patents varies from country to country.

The measures we have taken to protect our technology and products may not be sufficient to prevent their misappropriation by third parties or independent development by others of similar technologies or products. Competitors may also develop competing technology by designing around our patents and will then be able to manufacture and sell products which compete directly with ours. In that case, our business and operating results would be harmed. Substantially all of our employees are subject to non-compete agreements but there is no assurance that employees will not breach such agreements, necessitating costly and protracted litigation.

## Table of Contents

In order to protect our technology and products and enforce our patents and other proprietary rights, we may need to initiate litigation against third parties or defend opposition proceedings before the European Patent Office or prosecute interference proceedings before the U.S. Patent and Trademark Office. These legal and administrative proceedings could be expensive and occupy significant management time and resources.

Furthermore, a successful opposition to our patent in any jurisdiction could provide a basis for our competitors to claim that our patents in other jurisdictions covering this technology are invalid.

*Our products may infringe the intellectual property rights of others.*

It is not possible to know with certainty whether the manufacture and sale of our products will infringe patents or other intellectual property rights owned by third parties. There may, for example, be patent applications pending at the moment, which if granted, may cover products that we have just developed or are developing. In certain other jurisdictions there is no publication of the subject matter of patents until the patents are issued. Third parties may from time to time claim that our current or future products infringe their patent or other intellectual property rights. In addition, if third parties claim that our customers are violating their intellectual property rights, our customers may seek indemnification from us, which could be costly, or may terminate their relationships with us. Any intellectual property claim could involve time-consuming and disruptive litigation and, if determined adversely to us, could prevent us from making or selling our products, and subject us to substantial monetary damages or require us to seek licenses.

Intellectual property rights litigation is complex and costly, and we cannot be sure of the outcome of any such litigation. Even if we prevail, the cost of such litigation could harm our results of operations. In addition, such litigation is time consuming and could divert our management's attention and resources away from our business. If we do not prevail in any litigation, in addition to any damages we might have to pay, we might be required to discontinue the use of certain processes, cease the manufacture, use and sale of infringing products and solutions, expend significant resources to develop non-infringing technology or obtain licenses on unfavorable terms. Licenses may not be available to us on acceptable terms or at all. In addition, some licenses are non-exclusive and, therefore, our competitors may have access to the same technology licensed to us. If we fail to obtain a required license or cannot design around any third party patents or otherwise avoid infringements, we may be unable to sell some of our products.

*We are susceptible to changes in international markets and difficulties with international operations could harm our business.*

Our ability to penetrate any market, whether domestic or international, is dependent, in part, on political and economic factors that we have no control over. In addition, there are certain inherent risks in international operations which include:

Changes in regulatory requirements and standards;

Required licenses, tariffs and other trade barriers;

Difficulties in enforcing intellectual property rights across, or having to litigate disputes in, various jurisdictions;

Difficulties in staffing and managing international operations;

Potentially adverse tax consequences; and

The burden of complying with a wide variety of complex laws and treaties in various jurisdictions.

General political instability



## Table of Contents

If we are unable to manage the risks associated with our focus on international sales, our business may be harmed.

*We may have to adapt our products in order to integrate them into our customers' systems or if new government regulations or industry standards are adopted or current regulations or standards are changed.*

Some of our products are subject to mandatory government regulation in the countries in which they are used. For example, card readers that are used in the United States require certification of compliance with regulations of the Federal Communications Commission and in Europe of compliance with regulations of the European Telecommunications Standards Institute regarding emission limits of radio frequency devices. In addition, governmental certification for the systems into which our products are integrated may be required. The International Standards Organization is in the process of approving industry standards regulating the transfer of data between contactless smart cards and readers. If there is a change to government regulations or industry standards, we may have to make significant modifications to our products and, as a result, could incur significant costs and may be unable to deploy our products in a timely manner.

In addition, prior to purchasing our products, some customers may require us to receive certification that our products can be integrated successfully into their systems or comply with applicable regulations. Receipt of these certifications may not occur in a timely manner or at all. In some cases, in order for our products, or for the system into which they are integrated, to be certified, we may have to make significant product modifications. Failure to become so certified could render us unable to deploy our products in a timely manner or at all.

*Our products may contain defects that we find only after deployment, which could harm our reputation, result in loss of customers and revenues and subject us to product liability claims.*

Our products are highly technical and deployed as part of large and complex projects. Any defects in our products could result in:

Harm to our reputation;

Loss of, or delay in, revenues;

Loss of customers and market share;

Failure to attract new customers or achieve market acceptance for our products; and

Unexpected expenses to remedy errors.

In addition, we could be exposed to potential product liability claims. Currently we maintain no product liability insurance. We intend to seek product liability insurance prior to the distribution of our products. However, we cannot provide any assurances that we can obtain this insurance in an amount that will be sufficient to cover any successful product liability claim or at an acceptable cost. If we self insure or if there is any product liability claim in excess of our insurance coverage, any related payments would have to be made out of our cash reserves, and this would harm our business. Furthermore, the assertion of product liability claims, regardless of the merits underlying the claim, could result in substantial costs to us, divert management's attention away from our operations and damage our reputation and business.

*Nevada Law Permits the Limitation on Directors' Liability.*

Pursuant to our Certificate of Incorporation and under Nevada law, our directors are not liable to us or our stockholders for monetary damages for breach of fiduciary duty, except for liability in connection with a breach of the duty of loyalty, for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, for dividend payments or stock repurchases illegal under Nevada law or any transaction in which a director has derived an improper personal benefit.





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**Table of Contents**

**Risks Related to Our Common Shares**

*We are controlled by IVI*

During 2006, IVI continued to provide financing to the Company and to take steps to enhance and protect the value of the intellectual property which is licensed to the Company. During 2006, IVI also continued to own a substantial percentage of the outstanding shares of Common Stock, with percentages ranging from 68% at January 1, 2006 to 18% at December 31, 2006. Pursuant to the Planned Reorganization, previously discussed, IVI will forgive the Company's indebtedness and the Company's obligation to issue additional stock for loans in 2006, and will surrender its stock holdings in exchange for Preferred Series A stock which possesses 70% voting control of the Company. Accordingly, this entity effectively has had and will continue to have the ability to control the outcome of all matters requiring stockholder approval, including, but not limited to, the election and removal of directors, and any merger, consolidation or sale of all, or substantially all, of our assets.

*Our share price has fluctuated in the past and may continue to fluctuate in the future.*

The market price of our shares in the over-the-counter market has experienced significant volatility and may continue to fluctuate significantly. The market price of our shares may be significantly affected by factors such as the announcements of agreements, new products or product enhancements by us or our competitors and technological innovations by us or our competitors. In addition, while we cannot assure you that any securities analysts will initiate or maintain research coverage of our Company and our shares, any statements or changes in estimates by analysts initiating or covering our shares or relating to the smart card industry could result in an immediate and adverse effect on the market price of our shares. Further, we cannot predict the effect, if any, that market sales of shares or the availability of shares for sale will have on the market price of the shares prevailing from time to time. Sales of a substantial number of shares or the perception that such sales could occur following the filing of this report, could have a material adverse effect on the market price of our shares.

Trading in shares of companies, such as the registrant, listed on the Pink Sheets in general and trading in shares of technology companies in particular have been subject to extreme price and volume fluctuations that have been unrelated or disproportionate to operating or other performance. We anticipate the filing of a Form 211 to initiate trading of our common stock on the OTC Bulletin Board. However, until this application is filed and approved, of which there can be no assurance, no market maker is presently publishing bid and asked quotations in our common stock.

*If our shares continue to be considered a Penny Stock, any investment in our shares will continue to be considered a high-risk investment and continue to be subject to restrictions on marketability.*

Since the bid price of our shares continues to be below \$5.00, our common shares are deemed to be penny stock for the purposes of the Exchange Act. Brokers effecting transactions in a penny stock are subject to additional customer disclosure and record keeping obligations. The additional obligations include disclosure of the risks associated with low price stocks, stock quote information and broker compensation. In addition, brokers making transactions in penny stocks are subject to additional sales practice requirements under the Exchange Act. These additional requirements include making inquiries into the suitability of penny stock investments for each customer or obtaining the prior written agreement of the customer for the penny stock purchase. Because of these additional obligations, some brokers will not effect transactions in our securities.

*Our share price could be adversely affected by future sales of our shares.*

As of December 31, 2005, we had 200,000,000 shares of common stock issued and outstanding. In July 2006, we filed a Certificate of Amendment to our Articles of Incorporation authorized by the consent of a majority of our stockholders increasing the number of authorized shares of our common stock from 200 million to 500 million. The market price of our shares could drop as a result of sales of substantial amounts of our shares in the public market. This factor could also make it more difficult to raise additional funds through future private offerings of our shares or other securities.

## **Table of Contents**

*We do not anticipate paying cash dividends in the foreseeable future.*

We have paid no dividends on our common stock since our inception and presently intend to continue to retain all earnings, if any, for use in our business. Investors who anticipate the need for either immediate or future income by way of cash dividends from their investment should refrain from investing in our securities.

*Our shareholders could experience dilution of their ownership interest if we issue more shares that are purchased by third parties.*

Under Nevada law, shareholders in public companies such as the registrant do not have preemptive rights. This means that our shareholders do not have the legal right to purchase shares in a new issue before they are offered to third parties. In addition, our board of directors may approve the issuance of shares in many instances without shareholder approval. As a result, our shareholders could experience dilution of their ownership interest if we decide to raise additional funds by issuing more shares and these shares are purchased by third parties.

## **Available Information**

We intend to file Annual Reports on Form 10-KSB on a timely basis for all subsequent years. In addition, we file Quarterly Reports on Form 10Q-SB, Current Reports on Form 8-K, amendments to these reports, and other information with the SEC. The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1800-SEC-0330. The SEC maintains an Internet site ([www.sec.gov](http://www.sec.gov)) that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC.

## **ITEM 2. DESCRIPTION OF PROPERTY**

We maintain an office at 526 West 26<sup>th</sup> Street, Suite 710, New York, NY 10001 at a monthly rental of \$3,000 per month on a month-to-month basis without the benefit of a written lease. Our office facilities in New York are adequate for the purposes for which they are intended and provide sufficient capacity to accommodate our short-term needs.

Through June 2007 the Company maintained a sublease of office and laboratory space in San Jose, after which all operations of the Company with the exception of the New York office were moved to South Korea. The Company also continues to lease approximately 2,750 square feet of executive office space in Seoul, South Korea from a non-affiliated landlord, at a monthly rental of \$5,300 through October 2007.

We believe that our rental expense is equal or better than we could have negotiated at arms length with a non-affiliated landlord for similarly situated space. Our space is adequate for our current needs and being utilized to approximately 100% of its capacity.

## **ITEM 3. LEGAL PROCEEDINGS**

Effective June 2006, the Company's consulting relationship with Wayne Drizin and Associated Business Group were terminated. The Company thereafter commenced an investigation into the activities of Mr. Drizin and Associated Business Group. On or about September 11, 2006, the Company filed a civil action in the Northern District of California against former consultants including Wayne Drizin for misappropriation of property of the Company. Discovery in that proceeding has not yet taken place and the action is continuing.

The Company's public filings are subject to review by the Securities and Exchange Commission and, from time to time, the SEC forwards to the Company letters commenting on prior filings. During 2006, the Company received such letters and has responded to each. Further, in response to such a comment letter, the Company filed a Form 10-KSB/A for the year ended December 31, 2005 and, to the extent that such letters of comment were applicable to future filings, the Company has incorporated suggested improvements and or clarifications in its presentation within its reports.

**Table of Contents**

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

The Company did not conduct a meeting of stockholders during 2006. However, and as disclosed in Item 1, on October 14, 2005, the Plan of Reorganization (the Plan ) was approved by the written consent of 126,590,052 of the 200,000,000 common shares of our Company that were outstanding on that date.

Further, the increase in the number of authorized shares was approved by shareholder vote in July 2006.

**Table of Contents****PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES****Market Information**

Since late 1997, our common stock, our only class of trading equity securities, has been traded in the over-the-counter market on the Pink Sheets under the symbol ESMT.PK. The following table sets forth the range of high and low bid price information for the common stock for each fiscal quarter for the past two fiscal years as reported by the Pink Sheets LLC. High and low bid quotations represent prices between dealers without adjustment for retail mark-ups, markdowns or commissions, and may not necessarily represent actual transactions.

|                               | HIGH BID | LOW BID |
|-------------------------------|----------|---------|
| Year Ended December 31, 2006: |          |         |
| Fourth Quarter                | \$ .09   | \$ .04  |
| Third Quarter                 | .23      | .05     |
| Second Quarter                | .31      | .05     |
| First Quarter                 | .11      | .04     |
| Year Ended December 31, 2005: |          |         |
| Fourth Quarter                | .19      | .06     |
| Third Quarter                 | .23      | .12     |
| Second Quarter                | .45      | .20     |
| First Quarter                 | .78      | .52     |

Since our shares began trading in the over-the-counter market in the Pink Sheets, the prices for our shares have fluctuated widely. There may be many factors that explain these variations. We believe that such factors include (a) the demand for our common stock, (b) the number of shares of our common stock available for sale, (c) developments in the smart card industry, and (d) changes in the performance of the stock market in general, among others.

In recent years, the stock market has experienced extreme price and volume fluctuations that have had a substantial effect on the market prices for many small and emerging growth companies such as our Company, which may be unrelated to the operating performances of the specific companies. Some companies that have experienced volatility in the market price of their stock have been the targets of securities class action litigation. If we became the target of securities class action litigation, it could result in substantial costs and a diversion of management's attention and resources and have an adverse effect on our ability to implement our business plan. In addition, holders of shares of our common stock could suffer substantial losses as a result of fluctuations and declines in the market price of our common stock.

The trading of shares of our common stock is subject to limitations set forth in Rule 15g-1 through 15g-9 of the Exchange Act. This rule imposes sales practice requirements on broker-dealers who sell so-called "penny stocks" to persons other than established customers, accredited investors or institutional investors. For any transaction involving a penny stock, unless exempt, the rules require that a broker or dealer: (a) approve a person's account for transactions in penny stocks; and (b) receive from the investor a written agreement to the transaction, setting forth the identity and quantity of the penny stock to be purchased. In order to approve a person's account for transactions in penny stocks, the broker or dealer must: (i) obtain financial information and investment experience and objectives of the person; and (ii) make a reasonable determination that the transactions in penny stocks are suitable for that the person and that person has sufficient knowledge and experience in financial matters to be capable of evaluating the risks of transactions in penny stocks. The broker or dealer must also deliver, prior to any transaction in a penny stock, a disclosure schedule relating to the penny stock market, which, in highlight form, sets forth the basis on which the broker or dealer made the suitability determination; and explains that the broker or dealer received a signed, written agreement from the investor prior to the transaction. Disclosure

**Table of Contents**

also has to be made about the risks of investing in penny stocks in both public offerings and in secondary trading, and about commissions payable to both the broker-dealer and the registered representative, current quotations for the securities and the rights and remedies available to an investor in cases of fraud in penny stock transactions. Finally, monthly statements have to be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks.

**Holders**

As of December 31, 2006, the approximate number of holders of record of shares of our common stock, \$.001 par value per share, our only class of trading securities, was believed by management to be as follows:

| Title of Class                 | Number of<br>Record Holders |
|--------------------------------|-----------------------------|
| Common Stock, \$.001 par value | 345                         |

We believe there are numerous shareholders whose securities are held in street name with various brokerage houses. The exact number of shareholders is unknown to us.

**Dividends**

To the best of management’s knowledge and belief, we have never paid a dividend; and no dividends are expected to be paid at least until we achieve a full year of profitable operations. Until then, earnings, if any, will be retained and used to finance the development and expansion of our business.

**ITEM 6. MANAGEMENT’S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION**

During 2006, the Company focused on its core technology, continuing to conduct research to enhance its product in areas including sensor technology and multiprocessor applications, and taking appropriate steps to ensure full protection of that technology for the value of the Company’s shareholders. Management also continued to pursue capital liquidity opportunities which will enable the Company to commence large scale production of its Super Smart Cards. At this point, our primary source of funds remains private placements of our equity securities and loans to the Company. We expect that this dependence will continue until the Company finalizes broader financing or our first system starts to generate sufficient income to cover our operating costs.

As of the date of this Report, we expect this dependence to continue at least through the third quarter of 2007. There can be no assurance that we will continue to be able to rely upon these sources of funds.

In 2007, the Company intends to continue marketing and research and development efforts, and expects to implement our first systems during the next 12 months, demonstrating the viability of our Super Smart Card and BVS2 based products and related technologies. The Company’s resources will be devoted initially to fulfillment of the MyBi contract which will utilize the established operations of e-Smart Korea while also providing a high visibility platform for demonstration of the operational capabilities of the product. The Company’s other contractual opportunities, including contracts previously disclosed in Kyrgyzstan and the People’s Republic of China will also be pursued as financial and operational resources permit.

Our ability to maintain what we believe to be the state-of-the-art quality of our Super Smart Card and BVS2 system and related technologies is dependent upon our ability to continue to improve our products functionality and durability and reduce their cost of manufacture. In addition, we are constantly trying to find and develop new products that enhance the functionality of our BVS2 platform. This research and development is expected to continue during 2006, and is expected to continue to be dependent upon funds from subscribers. Accordingly, it is subject to the same risks enumerated in the preceding paragraph.

**Table of Contents**

The Company will continue to expend funds in connection with our research and development activities. Our planned 2007 budget is approximately \$2,000,000 for these costs, but could change depending on a number of factors, including our rate of accomplishment.

During 2007, we intend to continue our efforts to fill a number of key management, marketing and technology positions commensurate with our intended growth and expanded operations.

**Off-Balance Sheet Arrangements**

During the fiscal year ended December 31, 2006, we had no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

**Forward Looking Statements:**

This discussion includes Forward-Looking Statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. Any statements that express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, using words or phrases such as expects or does not expect, is expected, anticipates or does not anticipate, plans, estimates or intends, or stating that certain actions, events or results may, could, would, might, or should be taken, occur or be achieved) are not statements of historical fact and may be considered forward looking statements. Such statements are included, among other places in this Form 10-KSB, in the sections entitled Management's Discussion and Analysis, and Description of Business. Forward-looking statements are based on expectations, estimates and projections at the time the statements are made that involve a number of risks and uncertainties which could cause actual results or events to differ materially from those presently anticipated. Although the Registrant believes that the expectations reflected in such forward-looking statements are reasonable, the Registrant can give no assurance that such expectations will prove to have been correct.

**ITEM 7. FINANCIAL STATEMENTS**

|  | <b>Page</b> |
|--|-------------|
| <u>Report of Independent Registered Accounting Firm</u>  | 21          |
| Consolidated Financial Statements  | 22          |
| <u>Balance Sheets as of December 31, 2006 and 2005</u>   | 23          |
| <u>Statements of Operations for the Years Ended December 31, 2006 and for the Period January 1, 2001 (inception of development period) through December 31, 2006</u> | 24          |
| <u>Statements of Shareholders' Equity (Deficiency) for the Period from January 1, 2001 (inception of development period) through December 31, 2006</u>               | 25          |
| <u>Statements of Cash Flows for the Years Ended December 31, 2006 and for the Period January 1, 2001 (inception of development period) through December 31, 2006</u> | 26          |
| <u>Notes to Consolidated Financial Statements</u>  |             |

**Table of Contents**

Report of Independent Registered Accounting Firm

To the Board of Directors and Stockholders of

e-Smart Technologies, Inc. (a development stage company)

We have audited the accompanying consolidated balance sheet of e-Smart Technologies, Inc. and subsidiaries (a development stage company) as of December 31, 2006 and December 31, 2005, and the related consolidated statements of operations, shareholders' equity (deficiency), and cash flows for the years then ended. The period from January 1, 2001 (inception of development period) through December 31, 2006 has been included in the accompanying financial statements in conformity with the requirements for reporting upon a development stage company. However, we have only audited the period from January 1, 2005 through December 31, 2006. The period from January 1, 2001 (inception of development period) through December 31, 2004 has not been examined by us. 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 audit. The consolidated financial statements of e-Smart Technologies, Inc. (a development stage company) as of December 31, 2004, were audited by other auditors whose report dated March 31, 2005, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with standards established by 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 management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of e-Smart Technologies, Inc. and subsidiaries (a development stage company) as of December 31, 2006 and December 31, 2005, and the results of their operations and their cash flows for the respective years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, the Company commenced its development stage on January 1, 2001. Realization of a major portion of the assets in the accompanying consolidated balance sheets is dependent upon the Company's ability to meet its future financing requirements, and the success of future operations. These factors raise substantial doubt about the Company's ability to continue as a going concern.

Horowitz & Ullmann, P.C.

New York, NY

October 18, 2007



**Table of Contents****e-Smart Technologies, Inc. and Subsidiaries****(a Development Stage Company)****Consolidated Balance Sheets**

|  | December 31, |              |
|--|--------------|--------------|
|  | 2006         | 2005         |
| <b>Assets</b>  |              |              |
| Current Assets   |              |              |
| Cash   | \$ 49,845    | \$ 164,584   |
| Prepaid expenses   | 7,558        | 2,692        |
| Total Current Assets   | 57,403       | 167,276      |
| Equipment, net   | 41,446       | 44,701       |
| License of Smart Card Technology, net of amortization  | 92,860       | 99,290       |
| Officers' advances   | 11,549       | 51,674       |
| Lease deposit  | 79,713       | 73,484       |
| Total Assets   | 282,971      | 436,425      |
| <b>Liabilities and Shareholders' Equity (Deficiency)</b>   |              |              |
| Current Liabilities  |              |              |
| Current portion of notes payable   | 509,927      | 509,927      |
| Accounts payable   | 1,286,904    | 640,197      |
| Accrued officer's compensation   | 544,285      | 371,060      |
| Accrued expenses   | 76,660       | 170,932      |
| Total Current Liabilities  | 2,417,776    | 1,692,116    |
| Note payable - long-term   | 1,946,394    | 2,274,722    |
| Total Liabilities  | 4,364,170    | 3,966,838    |
| Shareholders' Equity (Deficiency)  |              |              |
| Preferred Stock, \$0.001 par value, 10 million shares authorized, -0- issued and outstanding   |              |              |
| Common Stock, \$0.001 par value, 490 million shares authorized, 242,540,441 and 200,000,000 shares issued and outstanding in 2006 and 2005, respectively | 242,540      | 200,000      |
| Additional paid-in capital   | 70,954,225   | 63,777,497   |
| Deficit accumulated during the development stage   | (75,277,964) | (67,507,910) |
| Total Shareholders' Equity (Deficiency)  | (4,081,199)  | (3,530,413)  |
| Total Liabilities and Shareholders' Equity (Deficiency)  | \$ 282,971   | \$ 436,425   |

See notes to consolidated financial statements.

**Table of Contents****e-Smart Technologies, Inc. and Subsidiaries****(a Development Stage Company)****Consolidated Statements of Operations**

|  | Year Ended December 31, |                | January 1, 2001 |
|--|-------------------------|----------------|-----------------|
|  | 2006                    | 2005           | (inception of   |
|  |                         |                | development     |
|  |                         |                | period)         |
|  |                         |                | to December 31, |
|  |                         |                | 2006            |
| Revenue  | \$                      | \$             | \$              |
| Operating Expenses                                   |                         |                |                 |
| Research and development                             | 583,575                 | 927,620        | 15,150,309      |
| Selling, general and administrative                  | 7,007,715               | 3,824,120      | 59,767,838      |
| Interest expense                                     | 176,264                 | 111,018        | 351,017         |
| Total Operating Expenses                             | 7,767,554               | 4,862,758      | 75,269,164      |
| Loss before provision for income taxes               | (7,767,554)             | (4,862,758)    | (75,269,164)    |
| Provision for Income Taxes                           | 2,500                   | 2,550          | 8,800           |
| Net Loss   | \$ (7,770,054)          | \$ (4,865,308) | \$ (75,277,964) |
| Loss Per Share                                       | \$ (0.04)               | \$ (0.03)      | \$ (0.47)       |
| Weighted Average Number of Common Shares Outstanding | 217,380,939             | 187,565,362    | 162,075,228     |

See notes to consolidated financial statements.

**Table of Contents****e-Smart Technologies, Inc. and Subsidiaries****(a Development Stage Company)****Consolidated Statements of Shareholders Equity (Deficiency)**

|   | Common Stock       |                   | Additional<br>Paid-In<br>Capital | Retained<br>Earnings<br>(Deficit) | Total                 |
|---|--------------------|-------------------|----------------------------------|-----------------------------------|-----------------------|
|   | Shares             | Amount            |                                  |                                   |                       |
| Balance, January 1, 2001(Inception of Development Period) | 501,000            | \$ 501            | \$ 3,075                         | \$ (2,944)                        | \$ 632                |
| Issuance of shares for services                           | 16,016,200         | 16,016            | 119,640                          |                                   | 135,656               |
| Issuance of shares for licensed technology                | 128,600,000        | 128,600           |                                  |                                   | 128,600               |
| Net (loss)  |                    |                   |                                  | (142,636)                         | (142,636)             |
| <b>Balance, December 31, 2001</b>                         | <b>145,117,200</b> | <b>145,117</b>    | <b>122,715</b>                   | <b>(145,580)</b>                  | <b>122,252</b>        |
| Issuance of shares for cash                               | 7,903,967          | 7,904             | 1,031,221                        |                                   | 1,039,125             |
| Issuance of shares for services                           | 750,826            | 751               | 84,843                           |                                   | 85,594                |
| Issuance of stock options for services                    |                    |                   | 21,476,000                       |                                   | 21,476,000            |
| Net income (loss)   |                    |                   |                                  | (22,961,160)                      | (22,961,160)          |
| <b>Balance, December 31, 2002</b>                         | <b>153,771,993</b> | <b>153,772</b>    | <b>22,714,779</b>                | <b>(23,106,740)</b>               | <b>(238,189)</b>      |
| Issuance of shares for cash                               | 16,497,519         | 16,498            | 2,531,854                        |                                   | 2,548,352             |
| Issuance of shares for services                           | 437,500            | 437               | 80,813                           |                                   | 81,250                |
| Issuance of stock options for services                    |                    |                   | 34,170,000                       |                                   | 34,170,000            |
| Net income (loss)   |                    |                   |                                  | (36,771,607)                      | (36,771,607)          |
| <b>Balance, December 31, 2003</b>                         | <b>170,707,012</b> | <b>170,707</b>    | <b>59,497,446</b>                | <b>(59,878,347)</b>               | <b>(210,194)</b>      |
| Issuance of shares for cash                               | 2,828,932          | 2,829             | 1,556,355                        |                                   | 1,559,184             |
| Net income (loss)   |                    |                   |                                  | (2,764,255)                       | (2,764,255)           |
| <b>Balance, December 31, 2004</b>                         | <b>173,535,944</b> | <b>173,536</b>    | <b>61,053,801</b>                | <b>(62,642,602)</b>               | <b>(1,415,265)</b>    |
| Issuance of shares for cash                               | 26,464,056         | 26,464            | 2,723,696                        |                                   | 2,750,160             |
| Net income (loss)   |                    |                   |                                  | (4,865,308)                       | (4,865,308)           |
| <b>Balance, December 31, 2005</b>                         | <b>200,000,000</b> | <b>200,000</b>    | <b>63,777,497</b>                | <b>(67,507,910)</b>               | <b>(3,530,413)</b>    |
| Issuance of shares for cash                               | 20,990,441         | 20,990            | 4,150,278                        |                                   | 4,171,268             |
| Issuance of shares for services                           | 21,550,000         | 21,550            | 3,026,450                        |                                   | 3,048,000             |
| Net income (loss)   |                    |                   |                                  | (7,770,054)                       | (7,770,054)           |
| <b>Balance, December 31, 2006</b>                         | <b>242,540,441</b> | <b>\$ 242,540</b> | <b>\$ 70,954,225</b>             | <b>\$ (75,277,964)</b>            | <b>\$ (4,081,199)</b> |

See notes to consolidated financial statements.

**Table of Contents****e-Smart Technologies, Inc. and Subsidiaries****(a Development Stage Company)****Consolidated Statements of Cash Flows**

|   | <b>Year Ended December 31,</b> |                    | <b>January 1, 2001</b>      |
|---|--------------------------------|--------------------|-----------------------------|
|   | <b>2006</b>                    | <b>2005</b>        | <b>(inception of</b>        |
|   |                                |                    | <b>development period)</b>  |
|   |                                |                    | <b>to December 31, 2006</b> |
| <b>Cash Flows From Operating Activities</b>                                 |                                |                    |                             |
| Net Loss  | \$ (7,770,054)                 | \$ (4,865,308)     | \$ (75,277,964)             |
| Adjustments to reconcile net loss to net cash used in operating activities: |                                |                    |                             |
| Issuance of stock options for services                                      |                                |                    | 55,646,000                  |
| Issuance of common stock for services                                       | 3,048,000                      |                    | 3,350,500                   |
| Depreciation expense  | 17,654                         | 23,566             | 41,696                      |
| Amortization expense  | 6,430                          | 6,430              | 35,740                      |
| Bad debt expense  |                                | 312,505            | 312,505                     |
| Changes in Assets and Liabilities:  |                                |                    |                             |
| (Increase) decrease in prepaid expenses                                     | (4,866)                        | 39,669             | (7,558)                     |
| (Increase) decrease in officers' advances                                   | 40,125                         | (51,674)           | (11,549)                    |
| (Increase) in deposits  | (6,229)                        | (15,345)           | (79,713)                    |
| Increase in accounts payable  | 646,707                        | 267,937            | 1,286,904                   |
| Increase in accrued expenses  | 351,193                        | 257,215            | 893,185                     |
| <b>Net Cash Used in Operating Activities</b>                                | <b>(3,671,040)</b>             | <b>(4,025,001)</b> | <b>(13,810,254)</b>         |
| <b>Cash Flows From Investing Activities</b>                                 |                                |                    |                             |
| Cash used for intangible assets   |                                |                    | (128,600)                   |
| Acquisition of equipment  | (14,399)                       | (25,749)           | (83,142)                    |
| Advances to (repayments from) Biosensor, LLC                                |                                | 11,995             | (312,505)                   |
| <b>Net Cash Used in Investing Activities</b>                                | <b>(14,399)</b>                | <b>(13,754)</b>    | <b>(524,247)</b>            |
| <b>Cash Flows From Financing Activities</b>                                 |                                |                    |                             |
| Proceeds from borrowings - other  |                                |                    | 117,500                     |
| Repayments of borrowings - other  |                                | (70,000)           | (70,000)                    |
| Proceeds from common stock issuances  |                                | 2,094,754          | 7,373,591                   |
| Proceeds from borrowings - related party                                    | 3,570,700                      | 2,135,728          | 7,150,828                   |
| Proceeds from related party advances  |                                |                    | 12,427                      |
| Repayment of borrowings - related party                                     |                                |                    | (200,000)                   |
| <b>Net Cash Provided by Financing Activities</b>                            | <b>3,570,700</b>               | <b>4,160,482</b>   | <b>14,384,346</b>           |
| <b>Net Increase in Cash</b>   | <b>(114,739)</b>               | <b>121,727</b>     | <b>49,845</b>               |
| Cash at Beginning of Year   | 164,584                        | 42,857             |                             |
| <b>Cash at End of Year</b>  | <b>\$ 49,845</b>               | <b>\$ 164,584</b>  | <b>\$ 49,845</b>            |
| <b>Supplemental Disclosures of Cash Flow Information</b>                    |                                |                    |                             |
| Cash paid during the year for:  |                                |                    |                             |
| Interest  | \$                             | \$ 5,000           | \$ 68,735                   |
| Income taxes  |                                | 150                | 3,900                       |

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### Supplemental Non-Cash Investing Activities

|   |              |    |    |            |
|---|--------------|----|----|------------|
| Issuance of common stock for services                             | \$ 3,048,000 | \$ | \$ | 3,350,500  |
| Issuance of common stock in repayment of related party borrowings | 4,171,268    |    |    | 4,171,268  |
| Issuance of stock options for services                            |              |    |    | 55,646,000 |

See notes to consolidated financial statements.

## **Table of Contents**

### **e-Smart Technologies, Inc. and Subsidiaries**

#### **(a Development Stage Company)**

### **Notes to Consolidated Financial Statements**

## **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### **Nature of Organization**

e-Smart Technologies, Inc. (the Company) is a Nevada corporation organized in July 1997 under the name of Boppers Holdings, Inc. ( Boppers ). The Company changed its name to e-Smart Technologies, Inc. on December 22, 2000.

On October 20, 2000, Boppers, Boppers Acquisition Corp., a then newly-formed Nevada Corporation and wholly owned subsidiary of Boppers ( BAC ), and e-Smart Systems, Inc., a Nevada corporation ( e-Smart Systems ) and wholly owned subsidiary of InterMarket Ventures, Inc., a Utah corporation ( Intermarket ), entered into an Agreement and Plan of Merger (the Merger Agreement ).

Pursuant to the Plan of Merger, Boppers' management resigned and the Registrant's present management took control. The Company's name was changed from Boppers Holdings, Inc. to e-Smart Technologies, Inc., effective December 22, 2000.

The Company was inactive until the commencement of its development stage on January 1, 2001. The Company and its subsidiaries are engaged in the business of creating, marketing, manufacturing, installing, operating and maintaining proprietary systems that are designed to positively authenticate each and every end user of any networked or local access system while protecting all information residing on or transported by the system in a manner that generates transaction fees.

### **Principles of Consolidation**

The consolidated financial statements include the accounts of e-Smart Technologies, Inc. and its wholly owned subsidiaries, e-Smart Systems, Inc., a heretofore inactive Nevada corporation, and e-Smart Korea, Inc., a South Korean corporation that commenced operations on January 1, 2004. All significant inter-company balances and transactions have been eliminated in consolidation.

### **Basis of Financial Statement Presentation**

The financial statements of the Company have been prepared assuming the Company will continue as a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. We have never been profitable and incurred substantial losses from operations of \$(7,770,054) and \$(4,865,308) for the years ended December 31, 2006 and 2005, respectively and \$(75,277,964) for the period January 1, 2001 (inception of development period) through December 31, 2006. Furthermore, the Company has negative working capital amounting to \$(2,360,373) and \$(1,524,840) at December 31, 2006 and 2005, respectively. The Company expects that losses from operations will continue through 2007 and anticipates that it will require additional financing in 2007, which may not be readily available. The Company is dependent upon the efforts of its management to raise proceeds from continued debt or equity placement to sustain the research and development and ultimate commercialization of their respective interests in the Super Smart Card™ technology. The Company's ability to continue to receive new investment proceeds is uncertain. The financial statements do not include any adjustments that might be necessary in the event that the Company cannot continue in existence.

### **Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles 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 financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

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## **Table of Contents**

### **Net Loss Per Share**

Loss per share, in accordance with the provisions of Financial Accounting Standards Board No. 128, *Earnings per Share*, is computed by dividing the net loss by the weighted average number of common shares outstanding during the period. Any common stock equivalents outstanding during the period would have had an anti-dilutive effect.

### **Research and Development Costs**

Research and development costs are charged to operations as incurred and amounted to \$583,575 and \$927,620 in 2006 and 2005, respectively, and \$15,150,309 from January 1, 2001 (inception of development period) through December 31, 2006.

### **License Costs**

Effective January 1, 2001 the Company acquired certain technology licenses. The technology was licensed from IVI Smart Technologies, Inc. ( *IVI* ), a related party, for an aggregate of 128,600,000 common shares of the Company valued at \$0.001 per share or \$128,600 as the total agreed upon consideration, which sum approximates the Licensor's allocable but not historical costs. The cost of the license is being amortized over its twenty-year term on a straight line basis. Amortization expense amounted to \$6,430 and \$6,430 for the years ended December 31, 2006 and 2005, respectively, and \$35,740 for the period January 1, 2001 (inception of development period) through December 31, 2006.

### **Shares Issued for Services**

The Company has adopted Statement of Financial Accounting Standard (SFAS) No. 123(R), *Share-Based Payment*. This Statement requires a public entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award (with limited exceptions). That cost will be recognized over the period during which an employee is required to provide service in exchange for the award the requisite service period (usually the vesting period). No compensation cost is recognized for equity instruments for which employees do not render the requisite service. This 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 Company recognized compensation costs of \$3,048,000 in 2006 in exchange for shares issued for services rendered by employees and non-employees. The Company did not recognize any compensation costs in 2005. The Company recognized compensation costs of \$3,350,500 for the period January 1, 2001 (inception of development period) through December 31, 2006 in exchange for shares issued for services rendered by employees and non-employees.

The Company did not issue stock options and did not recognize compensation costs in exchange for stock options for services rendered by employees and non-employees in 2006 or 2005. The Company recognized compensation costs of \$55,646,000 for the period January 1, 2001 (inception of development period) through December 31, 2006, in exchange for stock options issued for services rendered by employees and non-employees. The compensation costs recognized by the Company in exchange for stock options issued were measured using the grant-date fair value. The grant-date fair value was estimated using an option-pricing model adjusted for unique characteristics of those stock options. All stock options issued by the Company have expired by term or mutual agreement prior to December 31, 2006.

The Company did not have any outstanding awards of equity or liability awards as of December 31, 2006.

### **Equipment and Depreciation**

The cost of equipment is depreciated for financial reporting purposes on a straight-line basis over the estimated useful lives of the assets: 3-8 years for equipment. Repairs and maintenance expenditures which do not extend the useful lives of the related assets are expensed as incurred.

### **Income Taxes**

In accordance with the provisions of Financial Accounting Standards No. 109, *Accounting for Income Taxes* ( SFAS No. 109 ), deferred taxes are recognized for operating losses that are available to offset future taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. The Company incurred net operating losses for financial-reporting and tax-reporting purposes. Accordingly, the benefit from income taxes has been offset by a valuation allowance against the related deferred tax asset.

### **Foreign Currency Translation**

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The functional currency for the foreign operations of e-Smart Korea, Inc. is the local currency. The translation of foreign currencies into U.S. dollars is performed for the 2006 and 2005 balance sheet accounts using exchange rates in effect at the respective balance sheet date and for revenue and expense accounts, using a weighted average exchange rate during the respective calendar year.



**Table of Contents****Fair Value of Financial Instruments**

Cash, related party receivable, accrued expenses and notes payable are subject to fair value adjustments.

The carrying amount approximates fair value because of the short term maturity of these instruments.

**Limitations**

Fair value estimates are made at a specific point in time, based on relevant information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

**Reclassification**

Certain prior year amounts disclosed in the financial statements and notes thereto have been reclassified to conform to current year presentation.

**2. CONCENTRATIONS OF CREDIT RISK**

The Company maintains cash balances in financial institutions which are insured by the Federal Deposit Insurance Corporation up to \$100,000. Balances in these accounts may, at times, exceed the federally insured limits.

**3. DEPOSITS**

Deposits represent monies delivered as security under the leasing agreements for the office premises and automobile in South Korea.

**4. EQUIPMENT AND DEPRECIATION**

Equipment at cost, less accumulated depreciation consists of the following:

|  | As of December 31, |                  |
|--|--------------------|------------------|
|  | 2006               | 2005             |
| Equipment                                      | \$ 83,142          | \$ 68,743        |
| Less accumulated depreciation and amortization | (41,696)           | (24,042)         |
| <b>Total</b>                                   | <b>\$ 41,446</b>   | <b>\$ 44,701</b> |

Depreciation expense charged to operations was \$17,654, \$23,566, and \$41,696 in 2006, 2005, and for the period January 1, 2001 (inception of development period) through December 31, 2006, respectively.

**5. NOTES PAYABLE**

Notes payable consist of the following:

|  | 2006       | 2005       |
|--|------------|------------|
| 5% demand note due Intermarket Ventures, Inc., a related party       | \$ 450,000 | \$ 450,000 |
| 6% note term due Intermarket Ventures, Inc, a related party          | 1,946,394  | 2,274,722  |
| Non-interest bearing demand note due Associated Business Group, Inc. | 12,427     | 12,427     |
| Non-interest bearing demand notes - other                            | 47,500     | 47,500     |

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|                      |              |              |
|----------------------|--------------|--------------|
| Total                | 2,456,321    | 2,784,649    |
| Less current portion | (509,927)    | (509,927)    |
| Long-term portion    | \$ 1,946,394 | \$ 2,274,722 |

**Table of Contents****6. ACCRUED EXPENSES**

Accrued expenses are as follows:

|                 | 2006             | 2005              |
|-----------------|------------------|-------------------|
| Interest        | \$ 68,818        | \$ 164,782        |
| Franchise taxes | 7,842            | 6,150             |
| <b>Total</b>    | <b>\$ 76,660</b> | <b>\$ 170,932</b> |

**7. INCOME TAXES**

The income tax provision is comprised of the following:

|                                     | Year Ended December 31, |                 | January 1, 2001<br>(inception of<br>development period)<br>to December 31, |
|-------------------------------------|-------------------------|-----------------|--|
|                                     | 2006                    | 2005            | 2006   |
| Federal current provision           | \$                      | \$              | \$   |
| State and foreign current provision | 2,500                   | 2,550           | 8,800  |
| <b>Total income taxes</b>           | <b>\$ 2,500</b>         | <b>\$ 2,550</b> | <b>\$ 8,800</b>  |

The Company's total deferred tax asset and valuation allowance are as follows:

|   | 2006         | 2005         |
|---|--------------|--------------|
| Total deferred tax asset, current       | \$ 6,100,000 | \$ 3,550,000 |
| Less valuation allowance                | (6,100,000)  | (3,550,000)  |
| <b>Net deferred tax assets, current</b> | <b>\$</b>    | <b>\$</b>    |

The differences between income tax benefits in the financial statements and the tax benefit computed at the U.S. Federal statutory rate of 34% at December 31, 2006 and 2005 are as follows:

|                           | 2006     | 2005     |
|---------------------------|----------|----------|
| Tax benefit               | 34%      | 34%      |
| Valuation allowance       | (34)     | (34)     |
| <b>Effective tax rate</b> | <b>%</b> | <b>%</b> |

At December 31, 2006, the Company had available approximately \$18,000,000 of net operating losses to carry forward which may be used to reduce future federal taxable income through December 31, 2026.

**8. ISSUANCE OF COMMON STOCK AND STOCK OPTIONS**

During 2006, the Company issued 166,790,441 shares of its common stock to various individuals and related affiliates prior to receiving approval of the Board of Directors. Subsequent to the balance sheet date, the Board ratified 20,990,441 shares issued to Intermarket and affiliates in reduction of the Company's indebtedness thereto, 21,550,000 shares issued to officers, directors, consultants as compensation for services rendered, and cancelled 124,250,000 shares issued to related parties during 2006, pending further review. The number of shares reflected as issued and outstanding in the accompanying financial statements do not include shares issued during 2006, that were cancelled subsequent to December 31, 2006.

**Table of Contents**

At December 31, 2006, of the Company's 500,000,000 authorized shares, \$.001 par value, there were 242,540,441 shares issued and all previously existing options to purchase shares had either expired by term or mutual agreement. Additionally, all pre-existing warrants to purchase shares expired without being exercised. No new options or warrants were granted in 2006 and 2005. A summary of the stock option activity for years ended December 31, 2006 and 2005 is set forth below:

|  | Number of<br>Options | Weighted<br>Average<br>Exercise<br>Price |
|--|----------------------|--|
| Options in thousands                                     |                      |  |
| Options outstanding at January 1, 2005                   | 93,050,000           | \$ 0.61                                  |
| Granted  |                      |  |
| Exercised  |                      |  |
| Expired  |                      |  |
| Options outstanding and exercisable at December 31, 2005 | 93,050,000           | 0.61                                     |
| Granted  |                      |  |
| Exercised  |                      |  |
| Expired (by term or mutual agreement)                    | (93,050,000)         | (0.61)                                   |
| Options outstanding and exercisable at December 31, 2006 |                      | \$                                       |

**9. RELATED PARTY TRANSACTIONS**

The Company is the owner of three technology licenses. Each license has been granted pursuant to an Exclusive Use and Distribution Agreement, each of which grants the Company exclusivity to the technology covered in a particular territory. The three territories covered are the People's Republic of China, the remainder of Asia and the United States of America. The licenses, which have a term of twenty years, commencing January 1, 2001, were granted to the Company by IVI. IVI, together with its parent, Intermarket Ventures, Inc. (Intermarket), owns a 17.99% interest in the Company's common stock at December 31, 2006. [gs 1]

At December 31, 2006 and 2005, the Company was indebted to Intermarket in the amount of \$2,396,394 and \$2,724,722, respectively, plus accrued interest. These obligations are unsecured and bear interest at 6%. Of the above amounts owed, \$450,000 is due on demand, and the remaining balance, \$1,946,394 and \$2,274,722 at December 31, 2006 and 2005, respectively, is due on December 31, 2008. Pursuant to the Planned Reorganization, the foregoing obligations to Intermarket will be forgiven by IVI as one of the terms of its receipt of preferred shares.

On November 15, 2003 the Company entered into a Compensation and Settlement Agreement with Mary A. Grace, its President and Chief Executive Officer. Pursuant to this agreement the Company agreed to pay Ms. Grace a salary of \$250,000 per year for a five year term. At December 31, 2006 and 2005, the financial statements of the Company include a liability for Ms. Grace's accrued compensation of \$544,285 and \$371,060 respectively. Ms. Grace has agreed to accept payment in shares for such amounts due her. Further, in settlement of certain indebtedness of the Company to Ms. Grace, the Company has agreed to pay an amount equal to fifty percent (50%) of any net profit earned by the Company in any year during the term of this agreement until such time as Ms. Grace has received aggregate payments of \$450,000.

The Company maintains an office at 526 West 26<sup>th</sup> Street, Suite 710, New York, NY 10001 which it rents from a company owned by Ms. Grace's son for \$3,000 per month on a month-to-month basis. Based upon the office's size and location, the rental approximates market value.

## **Table of Contents**

We have sublicensed the rights to market the technology to state and federal agencies to the Company's forty-five percent (45%) affiliate, Homeland Defense, Inc. ( HDI ). The remaining fifty-five percent (55%) interest in HDI is owned by our President and Chief Executive Officer. During the 12 months ended December 31, 2006, neither our Company nor any related interests made investments in HDI.

### **10. DEPENDENCE UPON CONTROL PERSONS**

Intermarket, together with its two principal stockholders (the Company's President and Chief Executive Officer Mary A. Grace and its Chief Technology Officer Tamio Saito), continue to own a substantial percentage of the common stock of the Company and will continue to have the ability to materially influence the direction of the Company, its efforts in raising the additional capital critical to its success, and the strategies employed in commercialization of the licensed technology. In addition, the Planned Reorganization will include the receipt by IVI of Preferred Series A shares which possess 70% voting control of the Company.

### **11. RECENT ACCOUNTING PRONOUNCEMENTS**

#### **Impact of recently issued accounting standards**

In December, 2004, FASB issued Statement No. 123-R, Share Based Payment ( SFAS 123-R ) which is a revision of SFAS 123. SFAS 123-R superseded APB Opinion No. 25, Accounting for Stock Issued to Employees and its related guidance. Generally the approach to accounting for share based payments in SFAS 123-R is similar to the approach described in SFAS 123; however, SFAS 123-R requires all share based payments to employees, including grants of employee stock options, be recognized in the financial statements based on their fair values (pro forma disclosure is no longer an alternative to financial statement recognition). SFAS 123-R is effective for financial statements at both interim and annual periods beginning after January 1, 2006.

In May 2005, the FASB issued Statement No. 154, Accounting Changes and Error Corrections A Replacement of APB No. 20 and FASB Statement No. 3 ( SFAS 154 ). SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections, and is effective for fiscal years beginning after December 15, 2005. The adoption of SFAS 154 is not expected to have a material effect on the Company's consolidated results of operations of financial position.

**Table of Contents**

**12. COMMITMENTS**

The MYBi Agreement Pursuant thereto, we are required to: (i) supply MYBI with a designated number of terminals and Super Smart Cards necessary to meet consumer demand; (ii) purchase 9% of MYBI s issued and outstanding shares at a negotiated price; (iii) purchase a senior convertible debenture and warrant from MYBi (collectively the Debenture ) with a conversion price that allows us to purchase a minimum of 10.1 percent of MYBi at a designated price; and (iv) create, operate, and service an Operations Center in South Korea necessary to process the Super Smart Cards and any other type of non-cash payments other than Automated Fare Collections and other traditional MYBi e-purse transactions. The Debenture: (i) provides us with at least one permanent seat on MYBi s Board of Directors; (ii) requires MYBi to hire a manager designated by us as a full time employee for harmonious coordination; (iii) provide us with specified veto rights with respect to major decisions; and (iv) contains customary assurances with respect to management and business plans as well as customary covenants. The Company is continuing its efforts to raise the capital associated with the closing conditions of the Strategic Alliance Agreement.

**ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.**

None.

**ITEM 8-A. CONTROLS AND PROCEDURES**

**Limitations on the Effectiveness of Controls**

Our management does not expect that our disclosure controls or internal controls over financial reporting will prevent all errors or all instances of fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system s objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our Company have been detected.

These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Because of the inherent limitation of a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

**Changes in Internal Controls over Financial Reporting.**

There were no significant changes in our internal control over financial reporting that could significantly affect these controls during fiscal year ended December 31, 2006. As of December 31, 2006, we had not identified any significant deficiency or materials weaknesses in our internal controls, and therefore there were no corrective actions taken.

**Table of Contents**

Evaluation of Disclosure Controls and Procedures.

As of December 31, 2006, the Company's Chief Executive Officer and Chief Financial Officer carried out an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)). Based upon this evaluation, the CEO and CFO concluded that as of December 31, 2006, the Company's disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed by the Company is recorded, processed and summarized.

While management concluded that its controls and procedures are effective to ensure that information is accumulated and communicated to management to allow timely decisions regarding disclosures, management also acknowledges that the Company has not retained securities counsel and has not been able to ensure that its reports were filed within the time periods specified by the Commission. Management concluded that the issues regarding reporting related not to the accuracy of the reported data but to the delays in filing which flowed from issues associated with allocation and availability of resources, both financial and staff. The Company has therefore taken additional steps to retain additional administrative staff, has retained an acting Chief Financial Officer, and is seeking to ensure the availability of the funds necessary for timely submission of all periodic filings.

Section 404

We are continuing the process of documenting and evaluating our internal control procedures in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act which will apply to us beginning with our fiscal year 2007. Section 404 will require an annual report by our management on the effectiveness of our internal controls over financial reporting and for our independent registered public accounting firm to attest to management's evaluation report.



**Table of Contents****PART III****ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT****Directors and Executive Officers**

The following table sets forth: (1) names and ages of all persons who presently are and who have been selected as our directors; (2) all positions and offices with us held by each such person; (3) the term or office of each person named as a director; and (4) any period during which he or she has served as such:

| Name             | Duration          | Position and Office  | Age and          |
|------------------|-------------------|--|------------------|
|                  | and Date of       |  | Director         |
|                  | Expiration of     | with our Company   | Since            |
|                  | Present Term      |  |                  |
| Mary A. Grace    | One year 12/31/07 | President, Chief Executive Officer, Chief Financial Officer and Director | 59 - March 2001  |
| Charles R. Black | One year 12/31/07 | Director   | 55 - July 2006   |
| Gary Messina     | One year 12/31/07 | Director   | 54 - July 2006   |
| Thomas J. Volpe  | One year 12/31/07 | Director   | 71 - April 2005  |
| Elliot H. Cole   | One year 12/31/07 | Director   | 74 - April 2005  |
| Tamio Saito      | One year 12/31/07 | Senior Exec Vice President, and Chief Technical Officer                  | 53- October 2003 |

There is no understanding or arrangement between any directors or any other person or persons pursuant to which such individual, was or is to be, selected as one of our directors or as a nominee.

**Employment Agreements**

During the period covered by this Report, we entered into employment agreements with the following officers: None.

**Business Experience**

The following is a brief account of the experience of each of our directors and executive officers:

*Mary A. Grace* has been one of our directors since March 2001, and has also served as our President, Chief Executive Officer and Chief Financial Officer since that date. Between April 2001 and October 2000, Ms. Grace has served in the same capacities for IVI -Smart Technologies, Inc., a privately owned Delaware corporation and our parent. Between December 1997 and the current date, Ms. Grace served as Chairman, President and Chief Executive Officer of Intermarket Ventures, Inc., a publicly owned Utah corporation and parent of IVI-Smart Technologies, Inc. From July 1996, until its acquisition in November 1996, Ms. Grace served as the founder and a director of China Hi Tech American Telecommunications Ltd., a corporation engaged in international telecommunications. Between 1995 and 1996, Ms. Grace was one of the founders and an executive officer of Asia American Tele-Communications Corporation, a corporation engaged in telephony infrastructure development in Sichuan Province of the Peoples Republic of China. This company was sold to Metromedia Asia Corporation, a subsidiary of Metromedia International Group, Inc., in 1997. Between 1993 and 1995, Ms. Grace was a founding partner and director of Asian Infrastructure Development Co., Ltd. and Solution Technologies, Ltd., corporations that became engaged in infrastructure development in the Peoples Republic of China.



## Table of Contents

*Thomas J. Volpe* was elected to our Board of Directors on April 7, 2005 having previously served as our Advisory Board Chairman. Mr. Volpe until recently was Senior Vice President, Financial Operations, of The Interpublic Group of Companies, Inc., Vice President and Treasurer of Colgate-Palmolive Company and a Principal of Deloitte, Haskins & Sells. At Interpublic, Mr. Volpe was responsible for the worldwide treasury management of this \$7 billion company, including financial analysis, budgeting, approval of all investments, and the financing of mergers and acquisitions worldwide. He performed corporate controller functions, and conducted comprehensive strategic analyses and plans for the successful integration of acquired companies into the parent company. Mr. Volpe was in charge of Interpublic's global enterprise Y2K security risk analysis, as well as the implementation and coordination of the Y2K security protection needed throughout the company's operations in 160 countries. During his tenure at Colgate, Mr. Volpe maintained domestic and international banking relationships, negotiated unique global credit and financing arrangements, supervised an investment portfolio of \$500 million, restructured \$750 million of pension assets, and designed an international risk program constituting captive insurance operations including safety, security and loss prevention.

*Elliot H. Cole* was elected to our Board of Directors on April 7, 2005 having previously served as a member of our Advisory Board. Mr. Cole is senior counsel with the firm of Patton Boggs, LLP (Washington, DC), Mr. Cole has practiced corporate law in the nation's capitol for over 40 years, more than 30 of those years as a partner at Patton Boggs. Patton Boggs, through nearly four decades of practice, has established a reputation for cutting-edge advocacy by working closely with the US Congress and regulatory agencies in Washington. Patton Boggs, for example, has participated in the formation of every major multilateral trade agreement considered by Congress. The firm is a leader in merging public policy expertise getting results in both Washington and throughout the world. The firm is led by partners with extensive backgrounds in government service and with strong ties to both major political parties in order to be effective on Capitol Hill. In addition, Mr. Cole's expertise includes the representation of early-stage companies. As a counselor of start-ups through mezzanine and later-stage financing, he assists with bringing along to maturity companies in a wide range of businesses. His broad-based contacts with financiers and investors have provided capital and management assistance to a number of firm's clients over the years. Mr. Cole serves on the boards of numerous business, community and social organizations, and has been a trustee of his alma mater, Boston University, for over 20 years.

*Tamio Saito* has been one of our directors since October 2003, and will serve only until the election of the next director to our board. Mr. Saito also served and continues to serve as our Chief Technical Officer, since inception. Mr. Saito is also the Chief Technical Officer of our parent, Intermarket Ventures, Inc., and its affiliates. Mr. Saito joined the group with over 21 years of experience at Toshiba where he served in various positions, including Marketing Manager in the Semiconductor Division, Group Leader and Senior Research Scientist in the R&D Center as well as Manager of Technology for the Computer Division. Mr. Saito was the leading inventor at Toshiba with over 400 inventions and 50 US patents. Mr. Saito's inventions include, among other things: the Smart Card, the Thermal Printer, the 3-D Display, the 5th generation CT Scanner, the 3-D CT Scanner, the Image Sensor, Amorphous Silicon TFT/Sensor devices, Poly-Silicon TFT devices, the Digital Camera, Ti etching, Plasma Deposition Equipment, Switching Regulator, and Liquid Cooling System. Mr. Saito pioneered Sub-Nano-Second Signal Propagation, reflection theory and Fractal-Entropy interconnection theory in MPU, Memory, PCB and computers and he performed groundbreaking R&D work in high-end supercomputer technology including high speed circuitry analysis and Gallium Arsenic cross talk analysis and in semiconductor R&D work including simultaneous noise analysis. Mr. Saito has published over 50 papers at IEEE and other conferences and has published over 24 industrial professional books. Mr. Saito has a degree in Physics from Tohoku University in Japan.

*Charles R. Black.* Mr. Black is best known as one of America's leading Republican political strategists and has served as senior advisor to Presidents Reagan and Bush. He also served as a principal public spokesman for President Bush in the 1992 presidential campaign. During 1990, Mr. Black served as chief spokesman for the Republican National Committee and in 2000 Mr. Black also served on President George W. Bush's campaign as a volunteer political advisor and surrogate spokesman. An attorney with more than twenty-five years of experience in government, public affairs and politics, Mr. Black has managed the successful elections of more than ten members of the U.S. Senate and more than a dozen members of Congress. Mr. Black serves as the principal legislative and public affairs advisor to several

## **Table of Contents**

Fortune 500 companies and trade associations. He currently serves as Co-Chairman of the Civitas Group, LLC., a unique multi-disciplinary security consulting firm. The leadership team at Civitas is an impressive gathering of top security experts, including Robert H. Swindell, who spent nearly two decades with Lehman Brothers as head of its U.S. Technology Banking; David Howe, a former Special Assistant to President George W. Bush and the Senior Director for Emergency Preparedness and Response at the Homeland Security Council at the White House; Penrose "Parney" Albright, former Secretary of Homeland Security for Science and Technology; Richard A. Falkenrath is the former Deputy Assistant to the President and Deputy Homeland Security Advisor and also served as Special Assistant to the President and Senior Director for Policy and Plans within the Office of Homeland Security and Warren Rudman, former U.S. Senator from New Hampshire who served as Chairman of the President's Foreign Intelligence Advisory Board under President Clinton and was Co-Chair of the U.S. Commission on National Security.

*Gary S. Messina.* Mr. Messina has nearly three decades of public & private information technology infrastructure experience and expertise. His background includes multi-agency and industry experience in the design, development and deployment of technology strategies and policies with extensive knowledge of Information Technology Infrastructure, e-Commerce, start-up and expansion and the seamless integration of emerging technologies. Currently, Gary S. Messina is a Corporate Director for L-3 Communications Headquarters Operations. He is responsible for Homeland Security and Defense Operations domestically and internationally, which involves all of L-3 Communications. Prior to joining L-3, Washington Operations, Gary was the Strategic Development Executive for Titan Corporation which was acquired by L-3 Communications in September 2005. This position, at the vice-president level, was created to develop holistic business concepts and long-term strategies for Titan both national and internationally. He participated in mergers and acquisitions, congressional affairs and senior management. Gary was responsible for systems and approaches supporting the Department of Homeland Security and other large-scale government agencies and programs. Before he moved to the private sector, Gary was the Chief Information Officer for the Bureau of Citizenship and Immigration Services within the newly formed Department of Homeland Security where he retired in June 2004. During his tenure in the Federal Government he was a key player in the integration of former Immigration and Naturalization Service operations into the DHS environment. Gary has served under five U.S. Presidents, and six INS Commissioners. He was instrumental in leading change during his 27-year career with the Immigration and Naturalization Service. His expertise within the Agency spanned numerous programs, organizational changes, and administrations. Gary demonstrated a unique combination of management and policy experience in immigration affairs, counter-terrorism, Information Technology and organizational analysis. In his tenure with legacy INS and prior to his retirement, he served as Acting, Executive Associate Commissioner, Deputy Associate Commissioner, Assistant Commissioner, and Director of Research & Development, where he developed innovative technologies for counter-terrorism and counter intrusion programs within the agency.

## **Directorships**

Each of our directors has indicated to us that he is not presently a director in any other company with a class of securities registered pursuant to Section 12 of the Exchange Act or subject to the requirements of Section 15(d) of such act or any investment company registered under the Investment Company Act of 1940.

## **Advisory Board**

We have formed an advisory board to aid, assist and advise our Board of Directors regarding the smart card industry, technological developments, and related matters. The committee is currently made up of four members. No member of the Advisory Board is presently receiving any monetary compensation from us. However, and as indicated herein under Item 10, Executive Compensation, we have granted options to members of the Advisory Board under the 2003 Long Term Plan. The following is a brief summary of the experience of the members of the Advisory Board.

**Table of Contents**

*Eugene P. Beard* recently retired as Vice Chairman, Finance and Operations, of The Interpublic Group of Companies, Inc., a worldwide advertising and marketing communications group with 400 offices in 120 countries, over 50,000 employees and revenues of more than \$6 billion. A former Interpublic Group board member, and Chairman of its Finance Committee, Mr. Beard's retirement is effective at the end of 2003. Mr. Beard also serves on the boards of directors of Brown Brothers Harriman; Bessemer Trust Company; Mattel & Company and the Mattel Foundation; as well as MARC USA. As a member of the Advisory Council for Ethics and the Professions at Harvard's John F. Kennedy School of Government, Mr. Beard established the Beard Graduate and Faculty Fellowship programs for Ethics in the Professions. He also founded the Beard Center for Leadership and Ethics in Business at Pittsburgh's Duquesne University. Mr. Beard has been featured as an expert commentator and profiled in a number of media outlets, including Global Finance's CFO Superstars, Investor Relations, Treasury Magazine, Forbes, Corporate Finance, Institutional Investor and Business Week. He has also appeared on CNBC News and PBS's Nightly Business Report.

*Ronald E. Blaylock* is the founder, Chairman and Chief Executive Officer of Blaylock & Partners, L.P, a New York City based financial service firm offering institutions expertise in equity sales and trading, asset management, equity research, fixed income sales and trading, and investment banking. The firm also has offices in San Francisco, Austin, Chicago and Atlanta. Mr. Blaylock, who earned his MBA at the New York University Stern School of Business, held senior management positions with Paine Webber Group and CitiGroup before launching Blaylock & Partners in 1993. In his 20-year career on Wall Street, Mr. Blaylock has worked with a diverse range of corporate clients and institutional investors. As CEO of Blaylock & Partners, his leadership resulted in a number of unique industry achievements including being listed as the Corporate Capital Raiser of the Year by Corporate Finance Magazine in 1999. In 2003, Black Enterprise Magazine listed the firm in the top women/minority investment banks. In addition, the firm was ranked among the top 20 investment banking firms in the United States for underwriting investment grade debt for 1999, 2000 and 2001. Blaylock also has a strong presence in the equity markets having been a co-manager of the four largest U.S. IPOs to date. Blaylock & Partners is also well regarded for its experience and highly ranked research analysts. Mr. Blaylock earned his BS at Georgetown University where he was a member of the first NCAA Final Four basketball team. He serves on the Board for the National Association of Basketball Coaches, the New York University Board of Trustees, and serves on the board of the American General Life Insurance Company of New York, Radio One, and W.R. Berkley. His other charitable board work includes the American Ballet Theatre, the Inner-City Scholarship Fund, and Prep for Prep.

*John J. DeLucca* is currently Executive Vice President and CFO of the REL Consultancy Group, a private international consulting company. Previously, he served as Executive Vice President, Finance and Administration, and CFO of Coty Inc., where he was responsible for all global finance and administration operations, including accounting, strategic planning, corporate development, all treasury, audit and control functions, legal information technology systems, tax and administration. Prior to that he served as RJR Nabisco, Inc.'s Senior Vice President and Treasurer where he was responsible for all corporate finance and treasury activities, including capital markets, banking, derivatives/swaps, foreign exchange, risk management, pension fund management and cash management. Prior thereto, he served as Managing Director and CFO of Hascoe & Associates, President and CFO of the Lexington Group and Sr. VP, Finance and Managing Director of The Trump Group. Mr. DeLucca is a member of the boards of directors and serves as Chairman of the Audit Committees of the Elliott Company, Horizon Natural Resources and ITC Deltacom. He is also currently on the board of directors of Enzo Biochem, Inc and formerly a member of the boards of directors and Chairman of the Audit Committee of Edison Controls Corporation. Former directorships include Kash n Karry (sold to Food Lion); Nature's Food Centers (sold to General Nutrition Centers); Emperor Clock Company; and RKO Century Warner Theaters (sold to Cinema Odeon). Mr. DeLucca is active as a guest speaker/lecturer for many financial institutions, including Merrill Lynch, Bank of America, Deutsche Bank, Sumitomo Bank, Ltd., Banque Paribas, Canadian Imperial Bank of Commerce, Pace University, Standard & Poor's and NYU Stern School of Business.

## **Table of Contents**

### **Family Relationships**

No family relationship exists between any of our directors or executive offices.

### **Involvement in Certain Legal Proceedings**

Except as indicated above, no event listed in Sub-paragraphs (1) through (4) of Subparagraph (d) of Item 401 of Regulation S-B, has occurred with respect to any of our present executive officers or directors or any nominee for director during the past five years which is material to an evaluation of the ability or integrity of such director or officer.

### **Compliance with Section 16(a) of the Exchange Act**

Section 16(a) of the Exchange Act, as amended, requires our executive officers and directors and persons who own more than 10% of a registered class of our equity securities, to file with the SEC initial statements of beneficial ownership, reports of changes in ownership and annual reports concerning their ownership, of common stock and other of our equity securities on Forms 3, 4, and 5, respectively. Executive officers, directors and greater than 10% shareholders are required by SEC regulations to furnish us with copies of all Section 16(a) reports they file. To the best of our knowledge, none of the executive officers or directors of the Company have filed any documents under Section 16(a).

### **Audit Committee Financial Expert**

Mr. Thomas Volpe, a director and former Chairman of our Advisory Board, has agreed to serve as our Audit Committee Financial Expert.

### **Code of Ethics**

We have a Code of Ethics that applies to our principal executive officer, principal financial officer, principal accounting officer, controller and/or persons performing similar functions.

**Table of Contents****ITEM 10. EXECUTIVE COMPENSATION****Aggregate Compensation Covered**

During fiscal years 2004, 2005 and 2006, the aggregate compensation paid to, accrued or set aside for any of our executive officers or directors was \$250,000, \$250,000, and \$306,000, respectively.

**Summary Compensation Table**

| Name and Position  | Year | Annual Compensation      |         |       | Long Term Compensation |         |                        |                          |
|--|------|--------------------------|---------|-------|------------------------|---------|------------------------|--------------------------|
|  |      | Salary                   | Bonuses | Other | Stock Awards           | Options | LTIP                   | Payments Other           |
| Mary A. Grace,<br>President, CEO, CFO<br>and Director since<br>2001                  | 2004 | \$250,000 <sup>(1)</sup> |         |       |                        |         |                        |                          |
|  | 2005 | 250,000 <sup>(1)</sup>   |         |       |                        |         | \$                     |                          |
|  | 2006 | 250,000 <sup>(1)</sup>   |         |       |                        |         |                        |                          |
| Tamio Saito, Executive VP,<br>Chief Technology Officer,<br>and Director through 2006 | 2004 |                          |         |       |                        |         |                        |                          |
|  | 2005 |                          |         |       |                        |         |                        |                          |
|  | 2006 |                          |         |       |                        |         |                        |                          |
| Charles B. Black<br>Director since July<br>2006                                      | 2004 | 56,000                   |         |       |                        |         |                        |                          |
|  | 2005 | N/A                      |         |       |                        |         |                        |                          |
|  | 2006 | N/A                      |         |       |                        |         |                        |                          |
| Gary Messina, Director<br>since July 7, 2006   | 2004 |                          |         |       |                        |         | 450,000 <sup>(2)</sup> |                          |
|  | 2005 |                          |         |       |                        |         |                        |                          |
|  | 2006 |                          |         |       |                        |         |                        |                          |
| Thomas J. Volpe, Director<br>since April 7, 2005                                     | 2004 |                          |         |       |                        |         | 450,000 <sup>(2)</sup> |                          |
|  | 2005 |                          |         |       |                        |         |                        |                          |
|  | 2006 |                          |         |       |                        |         |                        |                          |
| Elliott H. Cole, Director<br>since April 7, 2005                                     | 2004 |                          |         |       |                        |         | 450,000 <sup>(2)</sup> |                          |
|  | 2005 |                          |         |       |                        |         |                        |                          |
|  | 2006 |                          |         |       |                        |         |                        |                          |
| Totals   | 2004 | \$250,000                |         |       |                        |         | \$                     |                          |
|  | 2005 | 250,000                  |         |       |                        |         |                        |                          |
|  | 2006 | 306,000                  |         |       |                        |         |                        | 1,800,000 <sup>(2)</sup> |

- (1) Does not include a settlement payment of \$450,000 referenced in a November 15, 2003, written Compensation Settlement Agreement with Mary A. Grace, our President, Chief Executive Officer and Chief Financial Officer. Pursuant to this agreement, we agreed to pay Ms. Grace a salary of \$250,000 per





## **Table of Contents**

year commencing on January 1, 2004. In consideration for Ms. Grace's release of our obligation to accrue her former salary of \$250,000 per year, net of approximately \$300,000 of expenses paid on Ms. Grace's behalf during the three years ending December 31, 2003, we agreed to pay to Ms. Grace a preferred distribution of 50% of future profits limited to \$450,000. In addition, and in consideration for our return to Ms. Grace of certain of her marketable securities, Ms. Grace released us from any prior obligations under a contemplated agreement to purchase such securities. Finally, we agreed that the approximate \$300,000 in expenses we paid on Ms. Grace's behalf would be deemed to be a loan and deductible only from the amount she is entitled to receive under the Compensation Settlement Agreement up to a maximum of \$100,000 per year, commencing in the first year following the year in which we first receive sufficient income from operations.

- (2) Represents the grant on July 13, 2006, of 2,500,000 common shares to each of the outside directors at \$.18 per share (100% of market value date of grant), which grants were ratified by the board during July 2007.

### **Option/SAR Grant Table**

During the fiscal year ended December 31, 2006, no options were granted to any of our officers, directors or advisory board members.

### **Aggregate Option/SAR Exercises and Fiscal Year-End Option/SAR Value Table**

During the fiscal year ended December 31, 2006, no stock options or freestanding SARs were exercised.

### **Long-Term Incentive Plans Awards in Last Two Fiscal Years**

None.

### **Warrants**

During the fiscal year ended December 31, 2006, no warrants to purchase shares of our common stock were issued or exercised.

### **Compensation of Directors and Advisors**

During the fiscal year ended December 31, 2006, each of the Company's four outside directors and three members of its advisory board received 2,500,000 and 500,000 common shares, respectively, for their services. The aggregate market value of the foregoing shares, based upon their date of issue, was \$1,890,000. The share issuances were ratified by the board in July 2007. The Company has agreed to implement a share compensation plan during 2007.

### **Employment Contracts and Termination of Employment, and Change in Control Arrangements**

Except for our President, Mary A. Grace, none of our executive officers was employed pursuant to the terms of an employment agreement with us.

**Table of Contents****ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Set forth below are the number of shares of our Common Stock, \$.001 par value per share, owned beneficially, or known by us to be owned beneficially, by any holder of more than 5% of any class of such security at December 31, 2006:

| Name and Address of<br>Beneficial Owner  | Amount<br>and<br>Nature of<br>Beneficial<br>Ownership | Percentage of Class |
|--|---|---------------------|
| IVI Smart Technologies, Inc.<br>526 West 26 <sup>th</sup> Street<br>Suite 710<br>New York, NY 10001<br>Mary A. Grace | 43,635,516 <sup>(1)</sup>                             | 17.99%              |
| 526 West 26 <sup>th</sup> Street<br>Suite 710<br>New York, NY 10001<br>Tamio Saito                                   | 10,250,000 <sup>(2)(3)(4)(7)</sup>                    | 4.23%               |
| 526 West 26 <sup>th</sup> Street<br>Suite 710<br>New York, NY 10001  | 2,500,000 <sup>(5)(6)(7)</sup>                        | 1.03%               |

<sup>(1)</sup> Includes 3,635,516 shares owned of record by Intermarket, which owns 37.5% of the outstanding shares of IVI. Intermarket is controlled by Mary A. Grace, and Tamio Saito.

<sup>(2)</sup> Does not include options to acquire an aggregate of 31,575,000 shares of our common stock granted on February 13, 2002 and December 1, 2003 which were cancelled simultaneously with the June 1, 2006 shareholders' approval of the Planned Reorganization.

<sup>(3)</sup> Does not include: (i) an aggregate of 13,090,655 shares of our common stock which may be attributable to Ms. Grace by virtue of her 30% equity ownership of Intermarket, which shares are inclusive of the shares of our stock owned by IVI.

<sup>(4)</sup> Does not include: (i) an aggregate of 4,050,000 shares owned of record by James Michael Phelan; or (ii) an aggregate of 4,175,000 shares owned of record by John Daniel Phelan, each adult sons of Mary Grace, neither of whom reside with her; (iii) an aggregate of 300,000 shares owned by Michele, Steven and Virginia Grace, family of Mary Grace, none of whom reside with her; or (iv) an aggregate of 950,000 shares owned of record by David N. Phelan, Ms. Grace's former spouse from whom she has been divorced since 1975. Ms. Grace disclaims beneficial ownership of the shares owned by her former husband and her adult children and her family.

<sup>(5)</sup>

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Does not include options to acquire an aggregate of 20,000,000 shares of our common stock granted on February 13, 2002 and December 1, 2003 which were cancelled simultaneously with the June 1, 2006 shareholders' approval of the Planned Reorganization.

- <sup>(6)</sup> Does not include: (I) an aggregate of 4,363,551 shares of our common stock which may be attributable to Mr. Saito by virtue of his 10% ownership of Intermarket; which shares are inclusive of the shares of our stock owned by IVI.
- <sup>(7)</sup> Does not include the receipt by management of common stock, which was agreed to in 2006, but finalized in 2007.

**Table of Contents****Security Ownership of Management**

Set forth below are the number of shares of our Common Stock, \$.001 par value per share, owned beneficially by each of our executive officers and directors and by all of our executive officers and directors as a group at December 31, 2006:

| Name and Address<br>of Beneficial Owner  | Amount and<br>Nature of<br>Beneficial<br>Ownership | Percentage of<br>Class |
|--|--|------------------------|
| Mary A. Grace<br>526 West 26 <sup>th</sup> Street, #710<br>New York, NY 10001    | 10,250,000 <sup>(1)(2)(3)(8)</sup>                 | 4.23%                  |
| Tamio Saito<br>526 West 26 <sup>th</sup> Street #710<br>New York, NY 10001       | 2,500,000 <sup>(4)(5)(6)(8)</sup>                  | 1.03%                  |
| Charles B. Black<br>526 West 26 <sup>th</sup> Street, #710<br>New York, NY 10001 | 2,500,000 <sup>(8)</sup>                           | 1.03%                  |
| Gary Messina<br>526 West 26 <sup>th</sup> Street, #710<br>New York, NY 10001     | 2,500,000 <sup>(8)</sup>                           | 1.03%                  |
| Thomas J. Volpe<br>526 West 26 <sup>th</sup> Street, #710<br>New York, NY 10001  | 2,500,000 <sup>(8)</sup>                           | 1.03 %                 |
| Elliott H. Cole<br>526 West 26 <sup>th</sup> Street, #710<br>New York, NY 10001  | 2,500,000 <sup>(8)</sup>                           | 1.03 %                 |
| All officers and directors as a group of five persons                            | 22,750,000 <sup>(7)(8)</sup>                       | 9.38%                  |

<sup>(1)</sup> Does not include: (i) an aggregate of 4,050,000 shares owned of record by James Michael Phelan; or (ii) an aggregate of 4,175,000 shares owned of record by John Daniel Phelan, each adult sons of Mary Grace, neither of whom reside with her; (iii) an aggregate of 300,000 shares owned by Michele, Steven and Virginia Grace, family of Mary Grace, none of whom reside with her; or (iv) an aggregate of 950,000 shares owned of record by David N. Phelan, Ms. Grace's former spouse from whom she has been divorced since 1975. Ms. Grace disclaims beneficial ownership of the shares owned by her former husband and her adult children and her family.

<sup>(2)</sup> Does not include options to acquire an aggregate of 31,575,000 shares of our common stock granted on February 13, 2002 and December 1, 2003 which were cancelled simultaneously with the June 1, 2006 shareholders' approval of the Planned Reorganization.

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- <sup>(3)</sup> Does not include: (i) an aggregate of 13,090,655 shares of our common stock which may be attributable to Ms. Grace by virtue of her 30% equity ownership of Intermarket, which shares are inclusive of the shares of our stock owned by IVI.

**Table of Contents**

- (4) Does not include options to acquire an aggregate of 20,000,000 shares of our common stock granted on February 13, 2002 and December 1, 2003 which were cancelled simultaneously with the June 1, 2006 shareholders' approval of the Planned Reorganization.
- (6) Does not include: (i) an aggregate of 4,363,551 shares of our common stock which may be attributable to Mr. Saito by virtue of his 10% ownership of Intermarket, which shares are inclusive of the shares of our stock owned by IVI.
- (7) Does not include options granted to management and a co-inventor of our Super Smart Card technology to acquire an aggregate of 83,000,000 shares of our common stock granted on February 13, 2002 and December 1, 2003 which were cancelled simultaneously with the June 1, 2006 shareholders' approval of the Planned Reorganization.
- (8) Includes the grant on July 13, 2006, of 2,500,000 common shares to each of the outside directors at \$.18 per share (100% of market value date of grant), which grants were ratified by the board during July 2007. Does not include the receipt by management of common stock, which was agreed to in 2006, but finalized in 2007.

**Changes in Control**

There have been no changes in control of the Company during the fiscal year ended December 31, 2006.

**Securities Authorized for Issuance Under Equity Compensation Plans**

The following table sets forth information as of December 31, 2006, with respect to compensation plans (including individual compensation arrangements) under which our common stock is authorized for issuance, aggregated as follows: (i) all compensation plans previously approved by security holders; and (ii) all compensation plans not previously approved by security holders.

**Equity Compensation Plan Information**

|  | NUMBER OF<br>SECURITIES TO<br>BE ISSUED UPON<br>EXERCISE OF<br>OUTSTANDING<br>OPTIONS,<br>WARRANTS,<br>AND RIGHTS | WEIGHTED<br>AVERAGE<br>EXERCISE PRICE<br>OF OUTSTANDING<br>OPTIONS,<br>WARRANTS, AND<br>RIGHTS | NUMBER OF<br>SECURITIES<br>REMAINING AVAILABLE<br>FOR FUTURE<br>ISSUANCES UNDER<br>EQUITY<br>COMPENSATION PLANS<br>(EXCLUDING<br>SECURITIES<br>REFLECTED IN<br>COLUMN |
|--|---|--|---|
| Equity compensation plans approved by security holders | None  | N/A  | None  |

**ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

Pursuant to the Planned Reorganization, IVI will receive Preferred Series A shares which are vested with ongoing 70% voting control in exchange for their forgiveness of amounts owed by the Company, the surrender of their common stock interest, and the licensing of further technology. Mary A. Grace, our President, Chief Executive Officer and Chief Financial Officer, is a director, executive officer and principal stockholder of IVI. Tamio Saito, our Chief Technology Officer, is also an executive officer and principal stockholder of IVI.

On November 15, 2003, we entered into a written Compensation Settlement Agreement with Mary A. Grace, our President, Chief Executive Officer and Chief Financial Officer. Pursuant to the agreement, we agreed to pay Ms. Grace a salary of \$250,000 per year commencing on January 1, 2004. In consideration for Ms. Grace's releasing us from our obligation to accrue her former salary of \$250,000 per year or \$750,000 net of \$300,000 in expenses that we paid on Ms. Grace's behalf for the three years ending December 31, 2003, we agreed to pay to Ms. Grace a preferred distribution of 50% of future profits limited to \$450,000. In addition, and in consideration for our return to Ms. Grace of certain of her

marketable securities, Ms. Grace released us from any prior obligations under a contemplated agreement to purchase such securities.

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**Table of Contents**

**ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K**

**Exhibits:**

- 3(i)\* Articles of Incorporation of Boppers Holdings, Inc., filed July 15, 1997, as amended August 11, 2000, as further amended December 22, 2000.
- 3(ii)\* Bylaws of e-Smart Technologies, Inc.
- 10(a)\* Exclusive Use and Distribution Agreement, dated as of October 26, 2001, by and between IVI Smart Technologies, Inc. & e-Smart Technologies, Inc.
- 10(b)\* Exclusive Use and Distribution Agreement, dated as of September 1, 2000, between Intermarket Ventures, Inc. and e-Smart Systems, Inc.
- 10(c)\* Notice and Consent, dated as of January 1, 2001, to that certain Exclusive Use and Distribution Agreement, dated as of September 1, 2000, between Intermarket Ventures, Inc. and e-Smart Systems, Inc.
- 10(d)\* Exclusive Use and Distribution Agreement, dated as of September 6, 2001, by and between IVI Smart Technologies, Inc. and e-Smart Technologies, Inc.
- 10(e)\* Exclusive Use and Distribution Agreement, dated August 27, 2000, by and between e-Smart Systems, Inc. and Newco (i.e., e-Smart City Card Co. Ltd., a Chinese JV company).
- 10(f)\* Advisory and Occupancy Services Agreement, dated May 29, 2003, but retroactively effective to January 1, 2001, by and between Associated Business Group, Inc. and e-Smart Technologies, Inc.
- 10(g)\* Compensation Settlement and Employment Agreement, dated as of November 15, 2003, by and between e-Smart Technologies, Inc. and Mary A. Grace.
- 10(h)\* Research and Development Services Agreement, dated as of January 1, 2001, and reduced to writing on May 29, 2003, by and between Big Bang Technologies, Inc and e-Smart Technologies, Inc.
- 10(i)\* E-Smart Technologies, Inc. 2003 Long Term Incentive Plan adopted December 1, 2003.
- 10(j)\* Master Teaming Agreement, dated as of February 27, 2004, by and between Samsung SDS Co., Ltd. and e-Smart Korea, Inc.
- 10(k)\* Cooperation Agreement, dated February 27, 2004, by and among e-Smart Technologies, Inc., Guo Xin Well-tel Technology Co., Ltd., and EarthNetMedia Trading Corporation.
- 10(l)\* Mutual Cooperation Agreement, dated February 25, 2004, by and between Daewoo International Corporation and e-Smart Korea, Inc.



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**Table of Contents**

- 10(m)\* Agreement with the Ministry of Transportation and Communication and the Republic of Kyrgyzstan's Supervisory Institute for e-Government dated April 4, 2004 (the Kyrgyzstan Agreement ).
- 10(n)\* Agreement with the Ministry of Economy of the Republic of Uzbekistan, Uzbekistan Uzbekprom Association and the Bank Association of the Republic of Uzbekistan dated August 13, 2004 (the Uzbekistan Agreement ).
- 10(o)\* Agreement with P.T. Primrose Gantari Indonesia dated November 8, 2004 (the Indonesia Agreement ).
- 10(p)\* Agreement with the Samsung Student Card Project Agreement with Samsung SDS Co., LTD., and Kobile Inc. dated December 3, 2004 (the Student Card Agreement ),
- 10(q)\* Agreement with Mybi Co, Ltd. dated December 3, 2004 (the Mybi Agreement )
- 23.1\* Consent of Independent Registered Public Accounting Firm.
- 31.1 Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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\* Previously filed

**Reports on Form 8-K**

During the last quarter of the fiscal year ended December 31, 2006, no reports on Form 8-K were filed.

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

**Audit Fees**

On January 3, 2006, we engaged Horowitz & Ullmann, P.C. ( H&U ) as our registered independent accountants to review the condensed quarterly financial statements previously included in our Form 10-QSB Quarterly Reports for June 30, 2005, and September 30, 2005, and audit our annual consolidated financial statements for the fiscal year ended December 31, 2005. Through December 31, 2006, we have paid H&U an aggregate of \$104,490 in fees for its professional services rendered in connection with the audit engagements. Rosenberg Rich Baker Berman & Company were our independent accountants for 2004 and prior.

**Audit-Related Fees**

In addition, we have paid H&U \$20,645 for their services in connection with reviewing our Forms 10-QSB for the two years ended December 31, 2006.

**Tax Fees**

There were no fees billed to us during the two fiscal year ended December 31, 2006, for professional services of H&U for tax compliance and related tax services regarding prior year tax returns.

**Table of Contents**

**All Other Fees**

There were \$5,005 in fees paid during the two fiscal year ended December 31, 2006, for services rendered by H&U other than the services described in the previous three paragraphs.

The engagement of H&U to render audit or non-audit services requires the prior approval of our Board of Directors since we do not yet have an audit committee of our Board of Directors.

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: October 24, 2007

**e-Smart Technologies, Inc.**

By: /s/ Mary A. Grace  
Mary A. Grace, President,  
Chief Executive Officer

/s/ Tamio Saito  
Tamio Saito  
Chief Technology Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

By: /s/ Mary A. Grace  
Mary A. Grace, Director  
Dated: October 24, 2007

By: /s/ Charles B. Black  
Charles B. Black, Director  
Dated: October 24, 2007

By: /s/ Gary Messina  
Gary Messina, Director  
Dated: October 24, 2007

By: /s/ Thomas J. Volpe  
Thomas J. Volpe, Director  
Dated: October 24, 2007

By: /s/ Elliott H. Cole  
Elliott H. Cole, Director  
Dated: October 24, 2007

**Table of Contents**

**Exhibit Index**

| <b>Exhibit No.</b> | <b>Description</b>  |
|--------------------|---|
| 31.1               | Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2               | Certifications Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1               | Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.  |