Siena Technologies, Inc.
Form 10QSB
November 14, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-QSB

(Mark One)

þ **QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2006

OR

o **TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from __________ to __________

Commission file number 000-25499

SIENA TECHNOLOGIES, INC.

(Exact name of small business issuer as specified in its charter)

Nevada	88-0390360
State or other jurisdiction of Incorporation or organization	(IRS Employer Identification Number)
5625 South Arville Street, Suite E, Las Vegas Nevada	89118
(Address of principal executive offices)	(Zip Code)

(702) 889-8777

(Issuer s telephone number, including area code)

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES o NO þ

As of November 14, 2006 there were 34,475,785 shares of common stock issued and outstanding, $0.001 par value.

Transitional Small Business Disclosure Format (check one) Yes o No þ

SIENA TECHNOLOGIES, INC. AND SUBSIDIARIES
(Formerly Network Installation Corp.)
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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

SIENA TECHNOLOGIES, INC.
(Formerly Network Installation Corp.)
Consolidated Balance Sheets

	September 30, 2006 (Unaudited)	December 31, 2005
ASSETS:		
CURRENT ASSETS:		
Cash	$ 133,664	$ 415,937
Accounts Receivable, Net of Allowance for Doubtful Accounts of $63,814 ($62,631 at 2005)	1,546,073	911,137
Inventories	1,080,402	2,928,366
Costs in Excess of Billings	487,697	232,778
Prepaid Expenses and Other Current Assets	352,467	133,810
Total Current Assets	3,600,303	4,622,028
Fixed Assets, Net of Accumulated Depreciation of $538,968 ($446,661 at 2005)	289,690	328,599
OTHER ASSETS:		
Goodwill	7,344,216	7,344,216
Patents	2,500	2,500
Assets Held for Sale	957,715	195,393
Total Other Assets	8,304,431	7,542,109
TOTAL ASSETS	$ 12,194,424	$ 12,492,736
LIABILITIES & STOCKHOLDERS EQUITY (DEFICIT):		
CURRENT LIABILITIES		
Bank Loans Payable	$ 599,557	$ 432,562
Accounts Payable	2,424,630	2,232,295
Billings in Excess of Costs	753,527	1,443,588
Current Portion of Notes Payable	240,254	336,115
Current Portion of Related Party Notes Payable	308,576	261,802
Current Portion of Convertible Debenture		316,333
Current Portion of Related Party Convertible Debentures		474,500
Total Current Liabilities	4,326,544	5,497,195
LONG-TERM DEBT		

Notes Payable	7,323,675	1,262,979
Related Party Notes Payable	375,551	95,497
Related Party Convertible Debentures, Net of Debt Discount		3,291,265
Total Long-Term Debt	7,699,226	4,649,741
NET LIABILITIES OF DISCONTINUED OPERATIONS	734,093	781,177
STOCKHOLDERS EQUITY (DEFICIT):		
Common Stock, $.001 par value; 100,000,000 shares authorized 29,180,914 and 49,534,721 shares issued and outstanding in 2006 and 2005, respectively	29,181	49,535
Additional Paid-in Capital	26,992,950	26,586,266
Shares to be Returned		(18,568)
Shares to be Issued	116,543	116,358
Warrants	28,796	
Accumulated Deficit	(27,732,909)	(25,168,968)
Total Stockholders Equity (Deficit)	(565,439)	1,564,623
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)	$ 12,194,424	$ 12,492,736

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SIENA TECHNOLOGIES, INC.
(Formerly Network Installation Corp.)
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005
REVENUE				
Sales	$ 15,817,664	$ 221,959	$ 4,174,364	$ 221,959
Cost of Goods Sold	12,684,666	169,725	3,165,793	169,725
GROSS PROFIT	3,132,998	52,234	1,008,571	52,234
OPERATING EXPENSES				
Investor Relations	137,925	241,685	72,142	
Non Cash Officer Compensation		6,575,426		
Salaries	1,770,666	28,390	612,978	28,390
Other Operating Expenses	1,632,121	273,422	593,874	137,244
Total Operating Expenses	3,540,712	7,118,923	1,278,994	165,634
LOSS FROM CONTINUING OPERATIONS	(407,714)	(7,066,689)	(270,423)	(113,400)
OTHER INCOME (EXPENSE)				
Interest Expense	(1,695,305)	(930,918)	(155,770)	(431,467)
Gain on Debt Restructuring	903,771			
Loss on Disposition of Assets	(194,452)		(201,407)	
Total Other (Expense)	(985,986)	(930,918)	(357,177)	(431,467)
LOSS FROM DISCONTINUED OPERATIONS	(1,170,241)	(2,130,760)		(1,380,298)
Net Loss	$ (2,563,941)	$ (10,128,367)	$ (627,600)	$ (1,925,165)
Basic and Diluted Loss Per Common Share	$ (0.07)	$ (0.49)	$ (0.02)	$ (0.11)
Weighted Average Shares Outstanding	35,837,851	20,606,252	29,180,914	17,764,338

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SIENA TECHNOLOGIES, INC.
(Formerly Network Installation Corp.)
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine-Months Ended September 30, 2006	2005
CASH FLOWS USED IN OPERATING ACTIVITIES:		
Net loss	$ (2,563,941)	$ (10,128,367)
Adjustments to reconcile net loss to net cash used in operating activities		
Stock issued for settlement	139,800	
Stock issued for officer compensation		6,476,085
Amortization of stock-based officer compensation		99,341
Beneficial conversion feature expense	777,090	556,250
Stock rescinded		(530,590)
Stock warrants issued for debt inducement	302,493	
Amortization of debt discount	267,610	172,750
Amortization of stock-based compensation for services	100,125	230,587
Conversion of debt		65,000
Accretion of notes payable balances	65,979	
Depreciation	102,070	660
Gain on disposal of assets	(6,955)	
Loss on writeoff of inventory	201,407	
Gain on debt restructuring	(903,771)	
Changes in operating assets and liabilities		
(Increase) decrease in accounts receivable	(634,936)	52,434
Decrease (increase) in inventories	1,646,557	(150,250)
(Increase) decrease in costs in excess of billings	(254,919)	79,470
(Increase) decrease in prepaid expenses and other assets	(108,657)	530,206
Increase in accounts payable	120,609	193,404
Decrease in billings in excess of costs	(690,061)	(207,029)
(Decrease) increase in net liabilities of discontinued operations	(47,084)	126,021
NET CASH USED IN OPERATING ACTIVITIES	(1,486,584)	(2,434,028)
CASH FLOWS USED IN INVESTING ACTIVITIES:		
Investments in assets held for sale	(762,322)	
Cash paid to acquire COM		(50,000)
Purchase of property and equipment	(30,885)	(9,523)
NET CASH USED IN INVESTING ACTIVITIES	(793,207)	(59,523)
CASH FLOWS PROVIDED BY FINANCING ACTIVITIES:		
Payments made on notes payable related party	(149,422)	
Proceeds from notes payable		45,389
Proceeds from convertible debt financing	2,803,712	1,900,000
Proceeds from factor	4,560,000	128,750
Payments to factor	(4,560,000)	(213,707)

Payments on notes payable		(656,772)		(35,000)
Issuances of stock for cash				943,451
NET CASH PROVIDED BY FINANCING ACTIVITIES		1,997,518		2,768,883
NET (DECREASE) INCREASE IN CASH & CASH EQUIVALENTS		(282,273)		275,332
BEGINNING CASH & CASH EQUIVALENTS		415,937		
CASH ACQUIRED				930,828
ENDING CASH & CASH EQUIVALENTS	$	133,664	$	1,206,160
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION				
Cash paid for interest	$	430,255	$	452,157
Cash paid for Income Taxes	$		$	
SUPPLEMENTAL DISCLOSURES OF NON-CASH TRANSACTIONS				
Assets acquired in exchange for capital lease obligation	$	25,321	$	
Shares of common stock to be issued for prepaid services	$	110,000	$	
Conversion of debentures	$	153,783	$	
Stock issued for acquisition	$		$	200,000

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SIENA TECHNOLOGIES, INC.
(Formerly Network Installation Corp.)
Notes to Consolidated Financial Statements September 30, 2006
(Unaudited)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

OVERVIEW

On October 25, 2006, Network Installation Corp. (NIC) changed its name to Siena Technologies, Inc. (the Company). The Company was incorporated on March 24, 1998 under the laws of the state of Nevada.

The accompanying unaudited consolidated financial statements of the Company have been prepared without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the accompanying consolidated financial statements reflect all adjustments of a normal recurring nature considered necessary to present fairly the Company s financial position, results of operations and cash flows for such periods. The accompanying interim consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company s Annual Report on Form 10-KSB for the year ended December 31, 2005. Results of operations for interim periods are not necessarily indicative of results that may be expected for any other interim periods or the full fiscal year.

The Company is a holding company that currently does business through its wholly owned subsidiaries. The Company s only subsidiary that is currently operating is Kelley Communication Company, Inc. (Kelley). Kelley specializes in the design, development and integration of communication technology and system networks for the gaming, resort and hospitality markets and has developed a patent-pending, proprietary, next-generation race & sports book platform designed for the gaming industry.

Kelley designs and manages projects, and builds and deploys communication technology for large entertainment technology and systems networks. Kelley s systems networks include: data, telecommunications, audio and video components, casino surveillance, security and access control systems, entertainment audio and video, special effects and multi-million dollar video conference systems. Kelley does work primarily in the Las Vegas area, but has also done projects in New Jersey, Oklahoma, Colorado, California, and the Caribbean. Kelley has distinguished itself from its peers by employing experienced and educated design personnel and by providing high quality products and service to the gaming industry.

ACQUISITION OF KELLEY COMMUNICATION COMPANY, INC. (d/b/a Kelley Technologies)

Pursuant to an acquisition agreement, the Company acquired 100% of the outstanding shares of common stock of Kelley Communication Company, Inc., a Nevada corporation, on September 22, 2005 for $10,232,101 in common stock. Goodwill of $11,144,216 was recorded upon the acquisition and was valued based on Kelley s customer pipeline and customer backlog at the time of acquisition. Mike Kelley, the 100% owner of Kelley prior to the acquisition, received 14,016,577 shares of the Company s common stock.

The audit of Kelley as of September 22, 2005 has not yet been completed. However, the Company s preliminary financial analysis and due diligence related to the acquisition is complete. Kelley s unaudited balance sheet as of the date of acquisition is as follows.

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Cash	$ 177,495
Accounts receivable	1,234,668
Inventory	965,927
Costs in excess of billings	488,370
Other assets	5,599
Fixed assets	713,220
Accumulated depreciation	(407,534)
Goodwill	11,144,216
Accounts payable	(879,995)
Notes payable	(2,297,227)
Billings in excess of earnings	(912,638)
Total	$ 10,232,101

The following pro forma information is presented as though the Company had completed the acquisition of Kelley as of the beginning of the year, on January 1, 2005 and to account for the restatement of the Company s net revenues and net loss as a result of the Company s decision to discontinue the operations of its subsidiaries, NIC and Com Services, Inc. (COM) Revenues represent total revenues and net loss represents total net loss of the Company for the three and nine months ended September 30, 2005 if Kelley had been acquired as of January 1, 2005.

	Nine Months Ended September 30, 2005	Three Months Ended September 30, 2005
Net Revenues	$ 3,257,574	$ 221,959
Net loss	$ (7,810,903)	$ (4,232)

ACQUISITION OF COM SERVICES, INC.

On January, 17, 2005, the Company purchased 100% of the outstanding shares of Com Services, Inc., a California corporation (COM). The purchase price was $430,000, of which $50,000 was paid in cash, $200,000 was paid in Company stock, issued at market value, and $180,000 in promissory notes payable over a two year period, with interest at 6%. Below is the unaudited condensed balance sheet of COM as of January 17, 2005, which is prepared only to present the major asset captions for which the Company has applied the purchase price of $430,000 towards.

Accounts receivable	$ 142,073
Fixed assets	56,032
Goodwill	331,895
Bank line of credit	(100,000)
Total assets and liabilities	$ 430,000

The net revenues and net loss on a pro forma basis, as though the Company had completed the acquisition of COM as of the beginning of the year, on January 1, 2005 would not be materially different than the net revenues and net loss reported for the nine months ended September 30, 2005 due to the lack of net revenues and expenses of COM from January 1, 2005 through January 16, 2005.

ACQUISITION OF DEL MAR SYSTEMS INTERNATIONAL, INC.

On March 1, 2004, the Company acquired 100% of the outstanding shares of common stock of Del Mar Systems International, Inc. (DMSI), a telecommunication solutions provider. The operations of DMSI have been consolidated with the operations of the Company, since March 1, 2004 and the operations of DMSI have since been phased out.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of the Company and its 100% owned subsidiaries, NIC, Kelley, COM, and DMSI. All significant inter-company accounts and transactions have been eliminated in consolidation. The results of operations included within these financial statements include the accounts of the Company and Kelley for the three and nine months ended September 30, 2006. The results of operations included within these financial statements include the accounts of the Company for the three and nine months ended September 30, 2005 and Kelley for the period from September 22, 2005 (the date the Company acquired Kelley) to September 30, 2005. The results of NIC and COM have been included in Loss from Discontinued Operations in the Company s accompanying consolidated financial statements for all periods presented.

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CASH & CASH EQUIVALENTS

The Company considers all highly liquid debt instruments, purchased with an original maturity at date of purchase of three months or less, to be cash equivalents. Cash and cash equivalents are carried at cost, which approximates market value.

PROPERTY & EQUIPMENT

Property and equipment are stated at cost. Depreciation is provided using the straight-line method over the estimated useful lives of the related assets, e.g. computers (5 years), software (3 years), office furniture and equipment (3 to 7 years), and tenant improvements (life of the lease-approximately 60 months).

ACCOUNTS RECEIVABLE

The Company maintains an allowance for doubtful accounts for estimated losses that may arise if any of its consumers are unable to make required payments. Management specifically analyzes the age of customer balances, historical bad debt experience, customer credit-worthiness and changes in customer payment terms when making estimates of the uncollectibility of the Company s trade accounts receivable balances. If the Company determines that the financial conditions of any of its customers have deteriorated, whether due to customer specific or general economic issues, increase in the allowance may be made. Accounts receivable are written off when all collection attempts have failed.

INVENTORY

Inventory consists of networking materials and equipment in the process of being installed, and materials purchased specifically for customer contracts, at the balance sheet date. Inventories are stated at the lower of cost or market. Cost is determined by the average cost method. The Company has reviewed its inventory for obsolescence on a quarterly basis since operations began and has not written-off any inventory for obsolescence other than the $201,407 shown in the accompanying unaudited financial statements.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company s financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities are carried at cost, which approximates their face value, due to the relatively short maturity of these instruments. As of September 30, 2006 and December 31, 2005, the Company s notes payable have stated borrowing rates that are consistent with those currently available to the Company and, accordingly, the Company believes the carrying value of these debt instruments approximates their fair value.

GOODWILL

Under SFAS No. 142. Goodwill and other Intangible Assets, all goodwill amortization ceased effective January 1, 2002. Rather, goodwill is now subject only to impairment reviews. A fair-value based test is applied at the reporting level. This test requires various judgments and estimates. A goodwill impairment loss will be recorded for any goodwill that is determined to be impaired. Goodwill is tested for impairment at least annually.

ACCOUNTING FOR IMPAIRMENTS IN LONG-LIVED ASSETS

Long-lived assets and identifiable intangibles are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amounts of assets may not be recoverable. Management periodically evaluates the carrying value and the economic useful life of its long-lived assets based on the Company s operating performance and the expected future undiscounted cash flows and will adjust the carrying amount of assets which may not be recoverable.

USE OF ESTIMATES

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States, 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 revenue and expenses during the reporting period. Significant estimates made in preparing these financial statements include the allowance for doubtful accounts, deferred tax asset valuation allowance, impairment of goodwill, certain gross margins on long term construction contracts and useful lives for depreciable and amortizable assets. Actual results could differ from those estimates.

REVENUE RECOGNITION

The Company s revenue recognition policies are in compliance with all applicable accounting regulations, including American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 81-1, Accounting for Performance of Construction-Type and Certain Production-Type Contracts. Revenues from design, installations, and networking contracts are recognized using the percentage-of-completion method of accounting. Accordingly, income is recognized in the ratio that costs incurred bears to estimated total costs. Adjustments to cost estimates are made periodically, and losses expected to be incurred on contracts in progress are charged to operations in the period such losses are determined. The aggregate of costs incurred and income recognized on uncompleted contracts in excess of related billings is shown as a current asset, and the aggregate of billings on uncompleted contracts in excess of related costs incurred and income recognized is shown as a current liability.

The Company s revenue recognition policy for the sale of its products is in compliance with Staff accounting bulletin (SAB) 104. Revenue is recognized when a formal arrangement exists, the price is fixed or determinable, the delivery is completed and collectibility is reasonably assured. Generally, the Company extends credit to its customers and does not require collateral. The Company performs ongoing credit evaluations of its customers and historic credit losses have been within management s expectations.

STOCK-BASED COMPENSATION

The Company has historically accounted for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees. Compensation cost for stock options, if any, is measured as the excess of the fair value of the Company s stock at the date of grant over the amount an employee must pay to acquire the stock. Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans.

In December 2004, the FASB issued SFAS No. 123 (Revised), Share-based Payment (SFAS 123(R)). SFAS 123(R) replaces SFAS 123 and supersedes APB 25. SFAS 123(R) is effective as of the beginning of the first interim period or annual reporting period that begins after December 15, 2005. SFAS 123(R) requires that the costs resulting from all share-based payments transactions be recognized in the financial statements. SFAS 123(R) applied to all awards granted after the required effective date and shall not apply to awards granted in periods before the required effective date, except if prior awards are modified, repurchased, or cancelled after the effective date.

On October 20, 2005, the Company issued 972,500 stock options to various Kelley employees in accordance with the Company s 2005 Stock Option Plan. The exercise price at the time of grant was $.79 per share, which was equal to the fair market value of the common stock on the date of grant, and the right to exercise the options were subject to vesting provisions over a 26-month period. Subsequent to issuance, 375,000 of such options were retired resulting from employees who left the Company prior to vesting.

On March 30, 2006, the Company issued 1,347,500 stock options to various Kelley employees in accordance with the Company s 2005 Stock Option Plan. The exercise price at the time of grant was $.42 per share, which was equal to the fair market value of the common stock on the date of grant, and the right to exercise the options were subject to vesting provisions over a three year period. Subsequent to issuance, 92,500 of such options were retired resulting from employees who left the Company prior to vesting.

On June 2, 2006, the Company issued 600,000 stock options to two Kelley employees in accordance with the Company s 2005 Stock Option Plan. The exercise price at the time of grant was $.41 per share, which was equal to the fair market value of the common stock on the date of grant, and the right to exercise the options were subject to vesting provisions over a three year period.

On August 8, 2006, the Company issued 192,500 stock options to various Kelley employees in accordance with the Company s 2005 Stock Option Plan. The exercise price at the time of grant was $.21 per share, which was equal to the fair market value of the common stock on the date of grant, and the right to exercise the options were subject to vesting provisions over a three year period.

On September 1, September 21, and September 25, 2006, the Company issued 350,000, 750,000 and 25,000 stock options to six Kelley employees respectively, in accordance with the Company s 2005 Stock Option Plan. The exercise prices at the time of grant were $.42, $.39 and $.32 per share, respectively, which was equal to the fair market value of the common stock on the date of grant. The right to exercise the options were subject to vesting provisions over a three year period.

Subsequent to September 30, 2006, the Company issued 75,000 stock options to three Kelley employees, in accordance with the Company s 2005 Stock Option Plan. The exercise prices at the time of grant were $.35 per share for 50,000 stock options and $.36 per share for 25,000 stock options, which was equal to the fair market value of the common stock on the date of grant. The right to exercise the options were subject to vesting provisions over a three-year period.

BASIC AND DILUTED NET LOSS PER SHARE

Net loss per share is calculated in accordance with the Statement of financial accounting standards No. 128 (SFAS No. 128), Earnings per share . Basic net loss per share is based upon the weighted average number of common shares outstanding. For all periods, all of the Company s common stock equivalents were excluded from the calculation of diluted loss per common share because they were anti-dilutive, due to the Company s net losses.

The Company s significant components of common stock equivalents are its convertible debentures (which were retired effective June 30, 2006), warrants to purchase the Company s common stock and stock options.

Stock options, which would have an anti-dilutive effect on the net loss per common share once exercised, to purchase 3,770,000 shares of common stock remained outstanding as of September 30, 2006. There were 972,500 stock options outstanding at December 31, 2005, 1,347,500 stock options were granted on March 30, 2006 and 600,000 stock options were granted on June 2, 2006. 192,500 stock options were granted on August 8, 2006 and 1,125,000 stock options were granted during September 2006. These stock options have a vesting period of three years from the date of grant.

Prior to the retirement of all convertible debentures effective June 30, 2006, the convertible debentures which could be exercised on any date subsequent to the issuance of the convertible debentures, would have an anti-dilutive effect on the net loss per common share once and if the holders elected to exchange the convertible debentures for shares of the Company s common stock. The number of common shares which could be exchanged by the Company for a full release of the obligation to repay the principal and interest balances associated with all convertible debentures could possibly have been based in part on the Company s price per common share as quoted on the OTC bulletin board on the date of conversion. Since the Company was not able to determine the price per common share of its common stock in the future, it did not believe it could reasonably determine the number of common shares to be issued pursuant to an exchange of its convertible debentures for common shares. Therefore, the Company could not accurately determine the number of common shares which could be exchanged by the Company that are related to the convertible debentures as of December 31, 2005. There were no convertible debentures outstanding as of September 30, 2006.

401(k) AND PROFIT SHARING PLANS

The Company has a qualified 401(k) profit sharing plan that covers substantially all full-time employees meeting certain eligibility requirements. The Company s annual profit sharing contribution is discretionary as determined by the Board of Directors; however, the contributions cannot exceed 25% of compensation for the eligible employees in any one tax year. For the year ended December 31, 2005, the Company s net contribution to the plan (after applying forfeiture credits) was $111,606. Contributions to the Plan are designated for each allocation group , and then allocated among eligible participants in each group based on the ratio of their salaries to the total salaries of all participants in the group. The plan document specifies the members of each allocation group.

Profit sharing contribution accounts are subject to a five year graded vesting schedule.

With respect to the plan s 401(k) feature, eligible employees may contribute from 1% to 75% of their annual compensation to the Plan, limited to a maximum annual amount as set periodically by the Internal Revenue Service. Although the plan provides for a discretionary matching contribution by the Company, no matching contributions were made for 2005 and the Company does not intend to make any contributions for 2006.

DEFINED BENEFIT PLAN

Kelley sponsors a defined benefit pension plan which covers all employees who have completed one year of service and have attained the age of twenty-one. The following table sets forth the benefit obligation, fair value of plan assets, and the funded status of the Kelley s Plan; amounts recognized in the Company s financial statements; and the principal weighted-average assumptions used:

		At December 31, 2005
Change in benefit obligation:		
Benefit obligation at beginning of year	$	379,331
Interest cost		20,863
Benefit obligation at end of year	$	400,194
Change in plan assets:		
Fair value of plan assets at beginning of year	$	371,951
Actual return on plan assets		30,708
Fair value of plan assets at end of year	$	402,659

		For the year ended December 31, 2005
Funded status	$	(2,465)
Unrecognized actuarial gain		1,131
Net amount recognized	$	(1,334)
Amounts recognized in the statement of financial position consist of:		
Prepaid benefit cost	$	(1,334)
Net amount recognized	$	(1,334)
Weighted-average assumptions as of December 31:		
Discount rate		5.50%
Expected return on plan assets		6.00%
Rate of compensation increase		3.00%

Components of net periodic benefit cost are as follows:

		For the year ended December 31, 2005
Service cost	$	0
Interest cost		20,863
Expected return on plan assets		(22,197)
Net periodic benefit cost	$	(1,334)

The projected benefit obligation, accumulated benefit obligation, and fair value of plan assets for the pension plans were $400,194, $400,194, and $402,659, respectively, as of December 31, 2005.

The provisions of Financial Accounting Standards Board Statement No. 87 (Employers Accounting for Pensions) require the Company to record an additional minimum liability of $0 at December 31, 2005. This liability represents the amount by which the accumulated benefit obligation exceeds the sum of the fair market value of plan assets and accrued amounts previously recorded. The additional liability may be offset by an intangible asset to the extent of previously unrecognized prior service cost.

The Company has discontinued the defined benefit pension plan as of November 13, 2006.

3. GOING CONCERN

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles, which contemplates continuation of the Company as a going concern. However, the Company has accumulated deficit of $27,732,909, and is generating losses from operations. The continuing losses have adversely affected the liquidity of the Company. The Company faces continuing significant business risks, including but, not limited, to its ability to maintain vendor and supplier relationships by making timely payments when due.

In view of the matters described in the preceding paragraph, recoverability of a major portion of the recorded asset amounts shown in the accompanying balance sheet is dependent upon continued operations of the Company, which in turn is dependent upon the Company s ability to raise additional capital, obtain financing and to succeed in its future operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. Management has taken the following steps to revise its operating and financial requirements, which it believes are sufficient to provide the Company with the ability to continue as a going concern in the near term: (i) restructuring all of the Company s convertible debt in exchange for promissory notes with payment terms ranging from two to five years, (ii) retiring the rights for the holders to convert the outstanding debt into common stock of the Company, and (iii) retiring all related warrants to purchase common stock of the Company. In addition, management has devoted considerable effort toward obtaining additional equity financing, and has successfully completed raising $1 million through a Private Placement on November 13, 2006, and is endeavoring to improve operational performance using marketing methods, cost cutting and the like.

4. PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets consists of

		September 30, 2006		December 31, 2005
Consulting services	$	11,812	$	124,360
Investor relations services		30,417		9,450
Employee advances		14,311		
Deferred financing fees		295,927		
	$	352,467	$	133,810