

PAID INC  
Form 10-K  
April 15, 2013

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K**

**Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**For the fiscal year ended December 31, 2012 or**

**Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**COMMISSION FILE NUMBER 0-28720**

**(Exact Name of Registrant as Specified in its Charter)**

**DELAWARE**

(State or Other Jurisdiction of Incorporation or Organization)

**73-1479833**

(I.R.S. Employer Identification No.)

**40 Washington Street, Westborough, Massachusetts 01581**

(Address of Principal Executive Offices) (Zip Code)

**(617) 861-6050**

(Registrant's Telephone Number, Including Area Code)

Securities registered under Section 12(b) of the Act:

**None**

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

**Common Stock, \$0.001 Par Value**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not 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-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated Filer  Non-accelerated filer  Smaller reporting company

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

The aggregate market value of the common stock held by non-affiliates of the registrant based on the last sale price of such stock as reported by the Over-the-Counter Bulletin Board on June 30, 2012 (the last business day of the Registrant's most recently completed second fiscal quarter) was approximately \$36,000,000

As of April 15, 2013, the registrant had 328,874,050 shares of Common Stock outstanding.

#### DOCUMENTS INCORPORATED BY REFERENCE

No documents are incorporated by reference into this Annual Report except those Exhibits so incorporated as set forth in the Exhibit Index

**PAID, INC.**

**FORM 10-K**

**FOR THE YEAR ENDED DECEMBER 31, 2012**

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## **PART I**

### **Forward Looking Statements**

This Annual Report on Form 10-K contains certain forward-looking statements (within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934) regarding the Company and its business, financial condition, results of operations and prospects. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates", "could", "may", "should", "will", "would", and similar expressions or variations of such words are intended to identify forward-looking statements in this report. Additionally, statements concerning future matters such as the development of new services, technology enhancements, purchases of equipment, credit arrangements, possible changes in legislation and other statements regarding matters that are not historical are forward-looking statements.

Although forward-looking statements in this Annual Report reflect the good faith judgment of the Company's management, such statements can be based only on facts and factors currently known by the Company. Further, whether actual results will conform to our expectations and predictions is subject to a number of known and unknown risks and uncertainties, including the risks and uncertainties discussed in this Annual Report; general economic, market, or business conditions; the opportunities that may be presented to and pursued by us; competitive actions by other companies; changes in laws or regulations; and other circumstances, many of which are beyond our control. Thus, actual results and outcomes may differ materially from results and outcomes discussed in this report. Although the Company believes that its plans, intentions and expectations reflected in these forward-looking statements are reasonable, the Company can give no assurance that its plans, intentions or expectations will be achieved. For a more complete discussion of these risk factors, see Item 1A, "Risk Factors".

For example, the Company's ability to achieve positive cash flow and to become profitable may be adversely affected as a result of a number of factors that could thwart its efforts. These factors include the Company's inability to successfully implement the Company's business and revenue model, tour or event cancellations, higher costs than anticipated, the Company's inability to sell its products and services to a sufficient number of customers, the introduction of competing products by others, the Company's failure to attract sufficient interest in and traffic to its sites, the Company's inability to complete development of its sites, the failure of the Company's operating systems, and the Company's inability to increase its revenues as rapidly as anticipated. If the Company is not profitable in the future, it will not be able to continue its business operations.

Except as required by applicable laws, we do not intend to publish updates or revisions of any forward-looking statements we make to reflect new information, future events or otherwise. Readers are urged to review carefully and to consider the various disclosures made by the Company in this Annual Report, which attempts to advise interested parties of the risks and factors that may affect our business, financial condition, results of operations and prospects.

## Item 1. Business

### Overview

PAID, Inc. (the “Company”) was incorporated in Delaware on August 9, 1995. The Company's main web address is located at [www.paid.com](http://www.paid.com), which offers updated information on various aspects of our operations. Information contained in the Company's website shall not be deemed to be a part of this Annual Report. The Company's principal executive offices are located at 40 Washington Street, Westborough, Massachusetts 01581, and the Company's telephone number is (617) 861-6050.

We file annual reports on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K with the Securities and Exchange Commission (the “SEC”). These reports, any amendments to these reports, proxy and information statements and certain other documents we file with the SEC are available through the SEC's website at [www.sec.gov](http://www.sec.gov) or free of charge on our website as soon as reasonably practicable after we file the documents with the SEC. The public may also read and copy these reports and any other materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

## Our Business

The Company's primary focus is to provide brand-related services to businesses and celebrity clients in the entertainment industry as well as charitable organizations. PAID's brand management, brand marketing, social media marketing, product design and merchandising, website design, development and hosting services are designed to grow each client's customer base in size, loyalty and revenue generation. We offer entertainers and business entities comprehensive web-presence and related services supporting and managing clients' official websites and fan-community services including e-commerce, VIP ticketing, live event fan experiences, user-generated content, client content publishing and distribution, fan forums, social network management, social media marketing, customer data capture, management and analysis. PAID's brand support services also include design and production of print, audio and video promotion marketing materials for client branded products and events. In addition to sourcing, designing and marketing, PAID sells merchandise for celebrities and businesses, through official website stores and other web-based outlets as well as on-tour and retail outlets. Our celebrity services proprietary content management system and our use of both off-the-shelf best of class and proprietary software applications provides an opportunity for our clients to offer a Direct-To-Consumer solution enabling more information, merchandise and experiences directly to their customers and communities while optimizing our ability to capture customer data and build robust customer data-bases for them. We provide business management tools for online retailers, through AuctionInc, which is home to our patented shipping calculator and automated auction checkout and order processing system. This system provides the fundamental structure for our celebrity web hosting and development services, and for individuals seeking a professional and interactive presence on the Internet.

All the sales for our celebrity and entertainment services, other than retail and tour merchandise, are made through the client's official website and official social network site and PAID's proprietary content managed system. A customer interested in a membership, merchandise, fan experience or ticket would use our system to make purchases, and then depending on the sale, the Company either ships the merchandise, or delivers the fan experience at a concert or other event. The services offered by a client depend upon the client's desire and willingness to offer different initiatives. Not all clients and customer bases are the same and the Company works closely with its different clients to cater to their unique needs. Our services also include marketing, management, sponsorship, mobile marketing, and website development and management. We provide services for artists and organizations such as Aerosmith, The Moody Blues, Stand Up 2 Cancer, Global Merchandise Services, and others.

*AuctionInc Software.* AuctionInc is a suite of online shipping and tax management tools assisting businesses with e-commerce storefronts, shipping solutions, tax calculation, inventory management, and auction processing. The application was designed originally to reduce overhead costs for auction sales, but over time the functionality and core business is strictly focused on shipping and tax calculations. The product does have tools to assist with other aspects of the fulfillment process, but the main purpose of the product is to provide accurate shipping and tax calculations and packaging algorithms that provide customers with the best possible shipping and tax solutions.

The AuctionInc system was originally designed to assist and improve just the Company's sales, but management realized that there was a need for an order management system for individuals and businesses that sell on the Internet,



specifically at auctions and sites with multiple sellers. In 2000 the Company's technology team focused its attention on the core fundamental piece of the system called the Shipping Calculator. The Company recognized the potential importance of the calculator and filed for a patent before launching it to the public in April of 2001. The Company obtained its first patent on the shipping calculator in January 2008, the second patent in April 2011 and the third patent in January 2013. The product is modular based and we continue to develop new tools and products for its customers.

## **Industry Background**

### *Growth of the Internet and the Web*

The Internet enables millions of people worldwide to share information, communicate and conduct business electronically. The growth in the number of Web users is being driven by the increasing importance of the Internet as a communications medium, an information resource, and a sales and distribution channel. The Internet has also evolved into a unique marketing channel. Unlike the traditional marketing channels, Internet retailers do not have many of the overhead costs borne by traditional retailers. The Internet offers the opportunity to create a large, geographically dispersed customer base more quickly than traditional retailers. The Internet also offers customers a broader selection of goods to purchase, provides sellers the opportunity to sell their goods more efficiently to a broader base of buyers and allows business transactions to occur at all hours.

### *State of Viral Communities on the Internet*

The massive growth of online communities over the past decade has reached viral proportions. Internet communities are built revolving around ideas, music, individuals, artists, writers, or any tangible or intangible entity, and new content can be distributed within minutes of exposure. Artists can announce tours or other news, sell premium tickets to fan club members, sell merchandise, and other fan experiences. Viral communities and viral marketing are a phenomenon that web users are embracing with vigor. As traffic and communities continue to grow, more services will be required to sustain the appetite of these users.

## **Business Strategy**

Our mission is to increase the Company's market share and revenues by providing products and services that grow each of our client's customer bases in size, loyalty and revenue generation. As the Company continues to support our clients in earning more, owning more and keeping more of the business they are responsible for having created in the first place we continue to strengthen our reputation, add new clients to our client base and share in the increase in revenues across the aggregate of the Company's client roster. Our strategy to achieve our mission is based upon the following:



During 2012 we experienced continued expansion of our Direct-to-Consumer marketing, ecommerce and fulfillment services, celebrity web-hosting, merchandising and fan experience programs. We believe there will be an increase in online and social communities that will create an opportunity for more celebrity web store management, fan community monetization and fulfillment services. It is our view that our services and programs will become more desirable as these communities and social interactions increase. Our proprietary Content Management System was built to handle news, events, ticketing, fan experiences, e-commerce, video, music streaming, mobile services, downloads and forums. Our Customer Relationship Management was developed to facilitate the capture, analysis and management of customer data.

**Fulfillment:** The Company continues to increase fulfillment services by adding new business relationships to our fulfillment client roster. The Company is providing fulfillment services as a partner to companies in a growing sector of commerce, ecommerce and social commerce service providers with ecommerce platforms which facilitate engagement and monetization of consumers via social media networks, distributed affiliate sites, and advertising networks but which do not offer inventory management and pick-pack-ship fulfillment services themselves.

The Company recognizes that fulfillment is a customer-facing service wherein the action of delivering a product to a customer provides the Company with the opportunity to 'touch' the customer multiple times throughout the fulfillment cycle. The Company sees this as an opportunity to incorporate into the fulfillment process increased sales and marketing tools and practices which result in an increase in per-customer purchases and new customer referrals.

**Consumer Data Management:** The monetization of consumer data continues to prove to be a growing and profitable business practice. The Company manages fan and customer communities also known as affinity groups which are representative of taste-makers and trend-setters whose interests and behaviors are valuable to the Company and the Company's clients as well as to a much greater range of marketers generally. These affinity groups can be quantified and qualified by the Company owing to the Company's established direct-to-consumer communication channels and practices, our robust Customer Relationship Management system and our consumer data analytics capabilities.

Our key objectives include the capture, analysis and monetization of consumer data with both short and longer term goals. We believe that by knowing the consumer better, we are able to turn consumers into customers. By targeting the customer with greater accuracy, delivering messages the customer has expressed interest in receiving, the Company can offer our customers and our clients' customers products and services they want to buy. Doing so reduces cost of sale, enables quicker inventory turns, results in higher margins and profits and also engenders customer trust and loyalty. Customer loyalty provides for a business-to-customer relationship in which the customer is positively inclined to share information about themselves - consumer data. Loyal customers engage in greater numbers and when incented by contests, VIP experiences, various promotions and product discounts, loyal fans/customers are willing to share information about themselves, their likes, dislikes, affiliations and consumer behaviors. The compilation and analysis of this consumer data can be fashioned into a suite of predictive modeling tools and made available as a B-to-B product for marketers of goods and services across a broad range of industries.

**Strategic Partnerships:** Our growth strategy includes strategic partnerships with music business industry leaders in providing software solutions, which enable Direct-To-Consumer ecommerce. We also partner with providers of turnkey solutions for their celebrity clients for design, product development, manufacturing and sales in all channels of retail distribution: live events, web stores, sponsorships, and third-party licensing. We provide web store development, ecommerce, inventory management and pick-pack-ship services to their celebrity clients including One Direction, Motley Crue, Slash, Slayer, Alice Cooper, and others.

We expect the above plan will enable us to increase our celebrity services and offer a wider variety of management services providing more resources for a sales and a marketing campaign to promote the Company.

In providing our services, our business plan includes the payment of advances to some clients on merchandise and VIP programs and appearances, and recoument of those advances from the artists' and celebrities' share of profits, as agreed upon in any agreement with the artist or celebrity.

The business strategy described above is intended to enhance our opportunities in the online e-commerce market. However, there are a number of factors that may impact our plans and inhibit our success. See “Risk Factors” included in Item 1A. Therefore, we have no guarantees and can provide no assurances, that our plans will be successful.

## **Marketing and Sales**

Successful branding of our corporate identity and services is the key to our success. We changed our name to PAID, Inc. at the end of 2003 and have consolidated our websites and brands under one Internet presence.

In 2012 we looked to streamline and focus our resources on cutting edge technology to drive the awareness and to deliver our products and services to a larger audience. Promoting and marketing PAID's celebrity services will continue by using various mediums of marketing; social engine marketing; "adword" campaigns, search engine optimization, email marketing, social media marketing, traditional print media and public relations methods, and presence at industry conferences and trade shows. However, as our celebrity services continue to gain exposure, we have had substantial opportunity to grow our business through referrals. Networking and referral business is a large portion of sales and marketing for these types of services. As we market and promote our celebrity services, we also will be supporting our proprietary content management system, increasing our CRM capabilities with enhanced marketing services, and continue to invest in our shipping calculator products.

The Company will continue to market AuctionInc throughout 2013. In the past, representatives of the Company attended trade shows, events and conferences to analyze the potential for AuctionInc and to expand the Company's marketing base. Based on experience with existing partnerships that promote AuctionInc, the Company believes that creating partnerships is an effective marketing tool to promote and encourage new registrations. The Company will continue to seek new partnerships. The Company may promote the AuctionInc product line in trade publications to reach small and midsize companies.

Although we believe that this marketing strategy, if successful, will lead to increased revenues, and attract more users to our site, we have no commitments that our marketing will be successful or our sales will increase. There are a number of factors that may impact our plans and inhibit our success. See "Risk Factors" included in Item 1A. Therefore, we have no guarantees and can provide no assurances that our plans will be successful.

## **Revenue Sources**

In 2012, our revenues were derived from our online merchandise and fulfillment operations, client services and touring programs. Although we expect that this revenue model will generate increased revenue, if we are not successful in implementing this model, if the entertainment industry and fans do not accept the services we provide, if costs are higher than anticipated, or if revenues do not increase as rapidly as hoped, we may not be able to generate positive cash flow. There are a number of factors that may impact our plans and inhibit our success. See "Risk Factors" included in Item 1A. Therefore, we have no guarantees and can provide no assurances, that our plans will be successful.

## **Competition**

Our web hosting software program, AuctionInc software suite, is proprietary. We received three patents related to our online auction shipping and tax calculators in January 2008, April 2011, and January 2013. We do not have any other

patents for our designs or innovations and we may not be able to obtain copyright, patent or other protection for our proprietary technologies or for the processes developed by our employees. Legal standards relating to intellectual property rights in computer software are still developing and this area of the law is evolving with new technologies. Our intellectual property rights do not guarantee any competitive advantage and may not sufficiently protect us against competitors with similar technology. We believe that our products and other proprietary rights do not infringe on the proprietary rights of third parties. However, there can be no assurance that third parties will not assert infringement claims against us in the future with respect to current or future products or other works of ours. This assertion may require us to enter into royalty arrangements or result in costly litigation.

We also utilize free open-source technology in certain areas. Unlike proprietary software, open-source software has publicly available source code and can be copied, modified and distributed with minimal restrictions. The client websites we build are developed on a Coldfusion proprietary content management and ecommerce engine. We use open source software and technology as well to support the growing social and viral opportunities on the Internet. By using 'best-of-breed' products and tools we can maximize our clients opportunities while minimizing our costs, which we are able to pass on to our customers.

## **Research and Development**

Over the past 2 years the Company has not made additional investments in research and development.

## **Employees**

As of April 15, 2013, the Company currently has 11 full time equivalent employees. We have no collective bargaining agreements and consider the relationship with our employees to be good.

## **Government Regulation**

We are not currently subject to direct federal, state or local regulation, and laws or regulations applicable to access or commerce on the Internet, other than regulations applicable to businesses generally. However, due to the increasing popularity and use of the Internet and other online services, it is possible that a number of laws and regulations may be adopted with respect to the Internet or other online services covering issues such as user privacy, freedom of expression, pricing, content and quality of products and services, taxation, advertising, intellectual property rights and information security.

## Item 1A. Risk Factors

*You should carefully consider the risks and uncertainties described below before deciding to invest in shares of our common stock. If any of the following risks or uncertainties actually occurs, our business, prospects, financial condition and operating results would likely suffer, possibly materially. In that event, the market price of our common stock could decline and you could lose all or part of your investment.*

### Risks Relating to the Company

*We have experienced significant operating losses.*

Our business and prospects must be considered in light of the risks, expenses and difficulties that are inherent in our business. The risks include:

- our ability to anticipate and adapt to a developing market;
- our ability to attract new businesses in the entertainment market for our brand-related services;
- our ability to engage musical artists and celebrities and name brands, to service a sustainable fan base for each musical artist and celebrity, and to sell merchandise, VIP tickets, fan experiences and other services;
- dependence upon the level of hits to our artists' sites and on sites that we use to sell our products and services;
  - the popularity and success of the artists and name brands who receive our services;
  - artist tour activities and fan attendance;
- our ability to recoup any advance paid to an artist or celebrity for merchandise, artist appearances, and VIP programs;
  - our ability to engage organizations for web site development and sponsorship;

- our ability to market, license and enforce our patented shipping calculator; and
- development of equal or superior Internet portals, auctions and related services by competitors.

To address these risks, we must, among other things, successfully market celebrities, musical artists, and name brands and service their fan or consumer base, increase traffic to their web sites, maintain our customer base, attract significant numbers of new customers and clients, respond to competitive developments, implement and execute successfully our business strategy and continue to develop and upgrade our technologies and customer services. We cannot offer any assurances that we will be successful in addressing these risks.

We incurred substantial losses each year since 1999. There can be no assurance that we will be profitable in the future.

***Our capital is limited and we may need additional financing to continue operations.***

We require substantial working capital to fund our business. Additional funds or authorized common stock may be necessary for our Company to continue its operations and to make recoupable advances for merchandise, artist appearances, and VIP programs. If we are unable to obtain financing in the amounts desired and on acceptable terms, or at all, or issue stock, we could be required to reduce significantly the scope of our expenditures or limit our ability to engage an artist, which would have a material adverse effect on our business potential and the market price of our common stock. If we raise additional funds by issuing equity securities, our shareholders will be further diluted. Based on our cash position as of December 31, 2012, we may need additional capital to fund our anticipated operating expenses over the next 12 months. If we require additional funding, there can be no assurances that the financing will be obtained, or if obtained, that funding will be obtained on reasonably acceptable terms.

***We are unable to guarantee that the marketplace will accept our software products.***

The software markets are characterized by rapid technological change, frequent new product enhancements, uncertain product life cycles, changes in customer demands and evolving industry standards. Our software products could be rendered obsolete if products based on new technologies are introduced or new industry standards emerge, or if we do not obtain adequate intellectual property protection. We are unable to provide any assurances that the marketplace will accept our software products and services, or that we will be able to provide these products and services at a profit.



*Our operating results are unpredictable and are expected to fluctuate in the future.*

You should not rely on the results for any period as an indication of future performance. Our operating results are unpredictable and are expected to fluctuate in the future due to a number of factors, many of which are outside our control. These factors beyond our control include:

our ability to engage well known celebrities, musical artists, and businesses in the entertainment industry with name brands for merchandise sales, web site and fan management, as well as other entities for web site development and sponsorship;

- our ability to engage celebrities for ticket sales services;

our ability to significantly increase our customer base and traffic to our web sites, manage our inventory mix and the mix of products offered, liquidate our inventory in a timely manner, maintain gross margins, and maintain customer satisfaction;

- our ability to market and sell our software products;

- the availability and pricing of merchandise from vendors;

- consumer confidence in encrypted transactions in the Internet environment;

- the timing, cost and availability of advertising on our web sites and other entities' web sites;

- popularity of celebrities;

- the amount and timing of costs related to expansion of our operations and the hiring of experienced personnel;

- the announcement or introduction of new types of services or products by our competitors;

- technical difficulties with respect to consumer and fan use of our web sites;

- our ability to make acquisitions of complementary business and technologies;

- governmental regulation by federal or local governments; and
- general economic conditions and economic conditions specific to the Internet and electronic commerce.

As a strategic response to changes in the competitive environment, we may from time to time make certain service, marketing or supply decisions or acquisitions that could have a material adverse effect on our results of operations and financial condition. In 2012, our revenues were derived from our celebrity services, fulfillment services, and ticketing and fan experiences.

***The successful operation of our business depends upon the supply of critical technology elements from other third parties, including our Internet service provider and technology licensors.***

Our operations depend on a number of third parties for Internet/telecom access, delivery services, and software services. We have limited control over these third parties and no long-term relationships with any of them. We rely on an Internet service provider to connect our web sites to the Internet. From time to time, we have experienced temporary interruptions in our web sites' connection and also our telecommunications access. We license technology and related databases from third parties for certain elements of our properties. Furthermore, we are dependent on hardware suppliers for prompt delivery, installation, and service of servers and other equipment to deliver our products and services. Our internally developed software depends on an operating system, database and server software that was developed and produced by and licensed from third parties. We have from time to time discovered errors and defects in the software from these third parties and, in part, rely on these third parties to correct these errors and defects in a timely manner. Any errors, failures, interruptions, or delays experienced in connection with these third-party technologies and information services could negatively impact our relationship with users and adversely affect our brand and our business, and could expose us to liabilities to third parties.

***We rely on third parties for our order fulfillment, and failures on the part of these third parties could harm our business.***

We use overnight courier and delivery services for substantially all of our merchandise and products. We use third party manufacturers to produce our merchandise. Should these vendors be unable to deliver our products for a sustained time period as a result of a strike, war, act of terrorism, business failure, or other reason, our business, results of operations and financial condition would be adversely affected. If, due to computer systems failures or other problems related to these third-party service providers, we experience any delays in shipment, our business, results of operations and financial condition would be adversely affected.

***Our failure to manage growth could place a significant strain on our management, operational and financial resources.***

Growth places a significant strain on our management, operational and financial resources, and has placed significant demands on our management, which currently includes one executive officer. In order to manage growth, we will be required to expand existing operations, particularly with respect to customer service and merchandising, to improve existing and implement new operational, financial and inventory systems, procedures and controls.

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We have experienced a significant strain on our resources because of:

- the need to manage relationships with our clients, including musical artists, businesses in the entertainment industry with name brands, and other celebrities;

- the need to manage relationships with various technology licensors, advertisers, other web sites and services, Internet service providers and other third parties;

- difficulties in hiring and retaining skilled personnel necessary to support our businesses;
- the need to train and manage a growing employee base; and
- pressures for the continued development of our financial and information management systems.

Difficulties we may encounter in dealing successfully with the above risks could seriously harm our operations. We cannot offer any assurance that our current personnel, systems, procedures and controls will be adequate to support our future operations or that management will be able to identify, hire, train, retain, motivate and manage required personnel.

***If our acquisitions are not successful, or if we are not able to structure future acquisitions in a financially efficient manner, there could be an adverse effect on our business and operations.***

If appropriate opportunities present themselves, we may acquire businesses, technologies, services or products that we believe will help us develop and expand our business. The process of integrating an acquired business, technology, service or product may result in operating difficulties and expenditures which we cannot anticipate and may absorb significant management attention that would otherwise be available for further development of our existing business. Moreover, the anticipated benefits of any acquisition may not be realized. Any future acquisitions of other businesses, technologies, services or products might require us to obtain additional equity or debt financing, which might not be available to us on favorable terms or at all, and might be dilutive. Additionally, we may not be able to successfully identify, negotiate or finance future acquisitions or to integrate acquisitions with our current business.

***Our Company's success still depends upon the continued services of its current management and other relationships.***

We are substantially dependent on the continued services of our key executive officer, , W. Austin Lewis, IV, as CEO, and CFO. Mr. Lewis has specialized knowledge and skills with respect to our Company and our operations and relationships with our clients. As a result, if Mr. Lewis were to leave our Company, we could face substantial difficulty in hiring qualified successors and could experience a loss in revenue while any successor obtains the necessary training and experience or builds new relationships. We do not maintain any key person life insurance.

***Loss of our key relationships, management and other personnel could result in the loss of key tours.***

The live music business is uniquely dependent upon personal relationships, as promoters and executives leverage their existing network of relationships with artists, agents and managers in order to secure the rights to the live music tours and events which are critical to our success. Due to the importance of those industry contacts to our business, the loss of any of our officers, relationships or other key personnel could adversely affect our operations.

***Our Company's success will depend on our ability to attract and retain qualified personnel.***

We believe that our future success will depend upon our ability to identify, attract, hire, train, motivate and retain other highly skilled managerial, merchandising, accounting, technical consulting, marketing and customer service personnel. We cannot offer assurances that we will be successful in attracting, assimilating or retaining the necessary personnel, and the failure to do so could have a material adverse effect on our business.

***Our success depends upon market awareness of our brand.***

Development and awareness of our Company will depend largely on our success in increasing our customer and client base. If vendors do not perceive us as an effective marketing and sales channel for their merchandise, or artists do not perceive our Company as offering an entertaining and desirable way to purchase services and merchandise through websites we develop, we may be unsuccessful in promoting and maintaining our brand. If celebrities, musical artists or sports figures do not recognize or trust our name, they will be less likely to engage us for our services. To attract and retain customers and to promote and maintain our Company in response to competitive pressures, we may find it necessary to increase our marketing, networking, and advertising budgets and otherwise to increase substantially our financial commitment to creating and maintaining brand loyalty among vendors, clients and consumers. We will need to continue to devote substantial financial and other resources to increase and maintain the awareness of our online brands among web site users, advertisers and e-commerce entities that we have advertising relationships with through:

- web advertising, marketing, and social media;
- traditional media advertising campaigns; and

- providing a high quality user experience.

Our results of operations could be seriously harmed if our investment of financial and other resources, in an attempt to achieve or maintain a leading position in Internet commerce or to promote and maintain our brand, does not generate a corresponding increase in net revenue, or if the expense of developing and promoting our online brands becomes excessive.

***System failures could result in interruptions in our service, which could harm our business.***

A key element of our strategy is to generate a high volume of traffic to, and use of, our web sites, and the web sites that we manage. Accordingly, the satisfactory performance, reliability and availability of these web sites, transaction processing systems, network infrastructure and delivery and shipping systems are critical to our operating results, as well as our reputation and our ability to attract and retain customers and maintain adequate customer service levels.

We periodically have experienced minor systems interruptions, including Internet disruptions. Some of the interruptions are due to upgrading our equipment to increase speed and reliability. During these upgrades the outages have generally lasted for a few hours, and even longer, on occasion. Any systems interruptions, including Internet disruptions, which result in the unavailability of these web sites or reduced order fulfillment performance would reduce the volume of goods sold, which could harm our business. In addition to placing increased burdens on our engineering staff, these outages create a large number of user questions and complaints that need to be responded to by our personnel. We cannot offer assurances that:

- we will be able to accurately project the rate or timing of increases if any, in the use of our web sites;

we will be able to expand and upgrade on a timely basis our systems and infrastructure to accommodate increases in the use of these web sites;

- we will have uninterrupted access to the Internet;
- our users will be able to reach these web sites;
- communications via these web sites will be secure;

we or our suppliers' network will be able to timely achieve or maintain a sufficiently high capacity of data transmission, especially if the customer usage of these web sites increases.

Any disruption in the Internet access to our web sites or any systems failures could significantly reduce consumer demand for our services, diminish the level of traffic to our web sites, impair our reputation and reduce our commerce and advertising revenues.

***We do not have redundant systems, a disaster recovery plan or alternate providers with respect to our communications hardware and computer hardware.***

Our main servers are located within 15 minutes from our corporate headquarters. Our Massachusetts facilities are not protected from fire, flood, power loss, telecommunication failure, break-in and similar events. We do not presently have fully redundant systems, a formal disaster recovery plan or alternative providers of hosting services. A substantial interruption in these systems would have a material adverse effect on our business, results of operations and financial condition.

Our servers are also vulnerable to computer viruses, physical or electronic break-ins, attempts by third parties to deliberately exceed the capacity of our systems and similar disruptive problems. Computer viruses, break-ins or other problems caused by third parties could lead to interruptions, delays, loss of data or cessation in service to users of our services and products and could seriously harm our business and results of operations.

***There are certain provisions of Delaware law that could have anti-takeover effects.***

Certain provisions of Delaware law and our Certificate of Incorporation, and Bylaws could make an acquisition of our Company by means of a tender offer, a proxy contest or otherwise, and the removal of our incumbent officers and directors more difficult. Our Certificate of Incorporation and Bylaws do not provide for cumulative voting in the election of directors. Our Bylaws include advance notice requirements for the submission by stockholders of nominations for election to the Board of Directors and for proposing matters that can be acted upon by stockholders at a meeting.

We are subject to the anti-takeover provisions of Section 203 of the Delaware General Corporation Law (the "DGCL"), which will prohibit us from engaging in a "business combination" with an "interested stockholder" for three years after the date of the transaction in which the person became an interested stockholder unless the business combination is approved in a prescribed manner. Generally, a "business combination" includes a merger, asset or stock sale, or other transaction resulting in a financial benefit to the interested stockholder. Generally, an "interested stockholder" is a person who, together with affiliates and associates, owns (or within three years prior to the determination of interested stockholder status, did own) 15% or more of a corporation's voting stock. The existence of this provision would be expected to have an anti-takeover effect with respect to transactions not approved in advance by the Board of Directors, including discouraging attempts that might result in a premium over the market price for the shares of common stock held by stockholders. Section 203 could adversely affect the ability of stockholders to benefit from certain transactions, which are opposed by the Board or by stockholders owning 15% of our common stock, even though such a transaction may offer our stockholders the opportunity to sell their stock at a price above the prevailing



market price.

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***Our success is dependent in part on our ability to obtain and maintain proprietary protection for our technologies and processes.***

Our most important intellectual property relates to the software for our AuctionInc products, our web-hosting services and our research center. We do not have any patents or patent applications for our designs or innovations, except for our patent with respect to our online auction shipping and tax calculator, one of our software products. We may not be able to obtain copyright, patent or other protection for our proprietary technologies or for the processes developed by our employees. Legal standards relating to intellectual property rights in computer software are still developing and this area of the law is evolving with new technologies. Our intellectual property rights do not guarantee any competitive advantage and may not sufficiently protect us against competitors with similar technology.

As part of our confidentiality procedures, we generally enter into agreements with our employees and consultants and limit access to and distribution of our software, documentation and other proprietary information. We cannot offer assurances that the steps we have taken will prevent misappropriation of our technology or that agreements entered into for that purpose will be enforceable. Notwithstanding the precautions we have taken, it might be possible for a third party to copy or otherwise obtain and use our software or other proprietary information without authorization or to develop similar software independently. Policing unauthorized use of our technology is difficult, particularly because the global nature of the Internet makes it difficult to control the ultimate destination or security of software or other data transmitted. The laws of other countries may afford our Company little or no effective protection of its intellectual property. Because our success in part relies upon our technologies, if proper protection is not available or can be circumvented, our business may suffer.

***Intellectual property infringement claims would harm our business.***

We may in the future receive notices from third parties claiming infringement by our software or other aspects of our business. Any future claim, with or without merit, could result in significant litigation costs and diversion of resources, including the attention of management, and require us to enter into royalty and licensing agreements, which could have a material adverse effect on our business, results of operations and financial condition. Royalty and licensing agreements, if required, may not be available on terms acceptable to the Company or at all. In the future, we may also need to file lawsuits to enforce our intellectual property rights, to protect our trade secrets, or to determine the validity and scope of the proprietary rights of others. This litigation, whether successful or unsuccessful, could result in substantial costs and diversion of resources, which could have a material adverse effect on our business, results of operations and financial condition.

***Our success is dependent on licensed technologies.***

We rely on a variety of technologies that we license from third parties. We license some of our software from third party vendors. We have two perpetual licenses for the proprietary software eCMS and acquired the source codes for the software. We also rely on encryption and authentication technology licensed from a third party through an online user agreement to provide the security and authentication necessary to effect secure transmission of confidential information.

We cannot make any assurances that these third-party technology licenses will continue to be available to us on commercially reasonable terms. Although no single software vendor licensor provides us with irreplaceable software, the termination of a license and the need to obtain and install new software on our systems would interrupt our operations. Our inability to maintain or obtain upgrades to any of these technology licenses could result in delays in completing our proprietary software enhancements and new developments until equivalent technology could be identified, licensed or developed and integrated. These delays would materially and adversely affect our business, results of operations and financial condition.

***We may be exposed to liability for content retrieved from our web sites.***

Our exposure to liability from providing content on the Internet is currently uncertain. Due to third party use of information and content downloaded from our web sites, we may be subject to claims relating to:

the content and publication of various materials based on defamation, libel, negligence, personal injury and other legal theories;

- copyright, trademark or patent infringement and wrongful action due to the actions of third parties; and
- other theories based on the nature and content of online materials made available through our web sites.

Our exposure to any related liability could result in us incurring significant costs and could drain our financial and other resources. We do not maintain insurance specifically covering these claims. Liability or alleged liability could further harm our business by diverting the attention and resources of our management and by damaging our reputation in our industry and with our customers.

***The Company may be exposed to potential risks relating to our significant deficiencies and material weaknesses in our internal controls over financial reporting.***

As directed by Section 404 of the Sarbanes-Oxley Act of 2002 (“SOX 404”), the Securities and Exchange Commission adopted rules requiring public companies to include a report of management on the company's internal control over financial reporting in their annual reports, including Form 10-K. We have identified significant deficiencies and material weaknesses in our internal controls and have taken steps to remediate them as cost-effectively as possible. Based on these significant deficiencies and material weaknesses, investors and others may lose confidence in the reliability of our financial statements and our ability to obtain equity or debt financing could suffer.

## **Risks Associated With Our Industry**

*The market for online services is intensely competitive with low barriers to entry.*

The market for Internet products and services is very competitive. Barriers to entry are relatively low, and current and new competitors can launch new sites at a relatively low cost using commercially available software. We currently or potentially compete with a variety of other companies depending on the type of merchandise and sales format offered to customers. These competitors include:

- other companies that manage celebrity web sites or that sell concert tour tickets online, such as Live Nation/Ticketmaster/VIP Nation, MusicToday, Ground Control, Artist Arena, and FanAsylum;

- a number of indirect competitors that specialize in electronic commerce or derive a substantial portion of their revenue from electronic commerce, including Internet Shopping Network, Google, Shopping.com, Amazon and Ebay.

- a variety of other companies that offer merchandise similar to ours but through physical auctions and with which we compete for sources of supply.

We believe that the principal competitive factors affecting our market are the ability to engage celebrities, musical artists, and businesses in the entertainment industry with name brands, the tour activities of our musical artists, and ability to attract customers at favorable customer acquisition costs, operate the web sites in an uninterrupted manner and with acceptable speed, provide effective customer service and obtain merchandise at satisfactory prices. We cannot offer any assurances that we can maintain our competitive position against current and potential competitors, especially those with greater financial, marketing, customer support, technical and other resources.

Current competitors have established or may establish cooperative relationships among themselves or directly with celebrities, and musical artists, and with vendors to obtain exclusive or semi-exclusive sources of merchandise. Accordingly, it is possible that new competitors or alliances may emerge and rapidly acquire market share. Increased

competition is likely to result in reduced operating margins, loss of market share and a diminished brand franchise, any one of which could materially adversely affect our business, results of operations and financial condition. Many of our current and potential competitors have significantly greater financial, marketing, customer support, technical and other resources than the Company. As a result, these competitors may be able to secure merchandise from vendors on more favorable terms than we can, and they may be able to respond more quickly to changes in customer preferences or to devote greater resources to the development, promotion and sale of their merchandise than we can.

***Our success in providing services and merchandise depends upon the popularity of the musical artist, celebrity, and other entities that we serve.***

We provide a full line of services for musical artists, and celebrities, as well as other entities with name brands, including sales of merchandise, online ticketing and fan experiences, and a fan web site. Our success depends in part on the level of popularity of a particular artist, the depth of the fan base, and the continued popularity of the artist. The Company can be adversely affected, and incur substantial loss of revenue, if an entire tour, or one or more shows within a tour, is terminated due to lack of interest, illness, death, or for any other reason. In the event that a show or tour is canceled or postponed, the Company may incur losses for that show, or fail to recoup any advance monies paid to the artist. In addition, we may not be able to obtain sufficient insurance coverage at reasonable costs to adequately protect us against the death, disability or other failure of such artists to continue engaging in revenue-generating activities under those arrangements.

***Any inability to fund the significant up-front cash requirements associated with our touring business could result in the loss of key tours.***

To secure a tour, including global tours by major artists, or to establish a relationship, we are often asked to advance funds to the artist or celebrity prior to the sale of any tickets for that tour. If we do not have sufficient cash on hand or capacity under any credit agreement to obtain cash to advance the necessary funds for any given tour, we would not be able to secure the artist and our revenue would be negatively impacted.

***The live entertainment business is highly sensitive to public tastes and dependent on our ability to secure popular artists and other live entertainment events, and we may be unable to anticipate or respond to changes in consumer preferences, which may result in decreased demand for our services.***

Our ability to generate revenue from our entertainment operations is highly sensitive to rapidly changing public tastes and dependent on the availability of popular artists, brands and events. Our success depends in part on our ability to anticipate the tastes of consumers and to offer events that appeal to them. Since we rely on unrelated parties to create and perform live entertainment content, such as concerts, musical performances, or appearances, any unwillingness to tour or lack of availability of popular artists, could limit our ability to generate revenue. In particular, there are a limited number of artists that can headline a major North American or global tour or who can sell out larger venues. If those key artists do not continue to tour, or if we are unable to secure the rights to their future tours, then our business would be adversely affected.

In addition, we often agree to pay an artist an upfront recoupable advance for artist or celebrity appearances, VIP programs, and merchandise, prior to our receiving any operating income. We may agree to advance funds for the artist to record an album, or to pre-fund other artist or brand ventures, and agree to recoup the advance based on future sales. Therefore, if the public is not receptive to the tour, merchandise, album, or other venture, we may incur a loss depending on the amount of any advance or incurred costs relative to any revenue earned. We may not have cancellation insurance policies in place to cover our losses if a performer cancels a tour. Furthermore, consumer preferences change from time to time, and our failure to anticipate, identify or react to these changes could result in reduced demand for our services, which would adversely affect our operating results and profitability.

***We may be adversely affected by the deterioration in economic conditions, which could affect consumer and corporate spending and our ability to raise capital, and, therefore, significantly adversely impact our operating results.***

A decline in attendance at or reduction in the number of live entertainment events may have an adverse effect on our revenue and operating income. The impact of slowdowns on our business is difficult to predict, but they may result in reductions in ticket sales, sponsorship opportunities and our ability to generate revenue. The risks associated with our businesses may become more acute in periods of slowing economy or recession, which may be accompanied by a decrease in attendance at live entertainment events. Instability in the financial markets as a result of recession or otherwise, as well as insufficient financial sector liquidity, also could affect the cost of capital and energy suppliers and our ability to raise capital.

Our business depends on discretionary consumer and corporate spending. Many factors related to corporate spending and discretionary consumer spending, including economic conditions affecting disposable consumer income such as employment, fuel prices, interest and tax rates and inflation can significantly impact our operating results. Business conditions, as well as various industry conditions, including corporate marketing and promotional spending and

interest levels, can also significantly impact our operating results. These factors can affect attendance at our events, premium seats, sponsorship, advertising and hospitality spending, concession and souvenir sales, as well as the financial results of sponsors of our venues, events and the industry. Negative factors such as challenging economic conditions, public concerns over additional terrorism and security incidents, particularly when combined, can impact corporate and consumer spending, and one negative factor can impact our results more than another. There can be no assurance that consumer and corporate spending will not be adversely impacted by economic conditions, thereby possibly impacting our operating results and growth.

***Market consolidation has created and continues to create companies that are larger and have greater resources than us.***

As the online commerce market continues to grow, other companies may enter into business combinations or alliances that strengthen their competitive positions. For example, in early 2010, Live Nation merged with Ticketmaster. The effects that any completed and pending acquisitions and strategic plans may have on us cannot be predicted with accuracy, but some of these companies that maintain divisions that compete with us are aligned with companies that are larger or better established than us. Even though some of the competitive services offered by these companies may comprise a small amount of their business, their potential access to greater financial, marketing and technical resources would put them in a stronger competitive position as compared to our Company. In addition, these companies include television broadcasters with access to unique content and substantial marketing resources that may not be available to our Company.

***Security breaches and credit card fraud could harm our business.***

We rely on encryption and authentication technology licensed from a third party through an online user agreement to provide the security and authentication necessary to effect secure transmission of confidential information. We believe that a significant barrier to electronic commerce and communications is the secure transmission of confidential information over public networks. We cannot give assurances, that advances in computer capabilities, new discoveries in the field of cryptography or other events or developments will not result in a compromise or breach of the algorithms we use to protect customer transaction data. If this compromise of our security were to occur, it could have a material adverse effect on our business, results of operations and financial condition. A party who is able to circumvent our security measures could misappropriate proprietary information or cause interruptions in our operations. To the extent that activities of our Company or third-party contractors involve the storage and transmission of proprietary information, such as credit card numbers, security breaches could expose us to a risk of loss or litigation and possible liability. We may be required to expend significant capital and other resources to protect against the threat of security breaches or to alleviate problems caused by these breaches. We cannot offer assurances that our security measures will prevent security breaches or that failure to prevent these security breaches will not have a material adverse effect on our business.

*Our industry may be exposed to increased government regulation.*

Our Company is not currently subject to direct regulation by any government agency, other than regulations applicable to businesses generally, and laws or regulations directly applicable to access to, or commerce on, the Internet. Today there are relatively few laws specifically directed towards online services, other than to protect user privacy or children. However, due to the increasing popularity and use of the Internet, it is possible that a number of laws and regulations may be adopted with respect to the Internet, covering issues such as user privacy, freedom of expression, pricing, content and quality of products and services, fraud, taxation, advertising, intellectual property rights and information security. Compliance with additional regulation could hinder our growth or prove to be prohibitively expensive.

The applicability to the Internet of existing laws in various jurisdictions governing issues such as property ownership, sales tax, libel and personal privacy is uncertain and may take time to resolve. In addition, because our service is available over the Internet in multiple states, and we sell to numerous consumers resident in these states, these jurisdictions may claim that we are required to qualify to do business as a foreign corporation in each state. Our failure to qualify as a foreign corporation in a jurisdiction where it is required to do so could subject our Company to taxes and penalties for the failure to qualify. Any new legislation or regulation, or the application of laws or regulations from jurisdictions whose laws do not currently apply to our business, could have a material adverse effect our business, results of operations and financial condition.

**Risks Associated with our Common Stock**

*Our stock price has been and may continue to be very volatile.*

The market price of the shares of our common stock has been, and is likely to be, highly volatile. During the 12 months prior to December 31, 2012, our stock price as traded on the OTC Bulletin Board has ranged from a high of \$.26 per share to a low of \$.0262 per share. The variance in our share price makes it difficult to forecast with any certainty the stock price at which you may be able to buy or sell your shares of our common stock. The market price for our stock could be subject to wide fluctuations in response to factors that are out of our control such as:

- actual or anticipated variations in our results of operations,
- announcements of new products, services or technological innovations by our competitors;



- developments with respect to patents, copyrights or proprietary rights;
  
- short selling our common stock and stock price manipulation;
  
- developments in Internet regulation; and
  
- general conditions and trends in the Internet, entertainment and electronic commerce industries.

The trading prices of many technology companies' stock have experienced extreme price and volume fluctuations. These fluctuations often have been unrelated or disproportionate to the operating performance of these companies. These broad market factors may adversely affect the market price of our common stock. These market fluctuations, as well as general economic, political and market conditions such as recessions or interest rate fluctuations, may adversely affect the market price of our common stock. Any negative change in the public's perception of the prospects of Internet or e-commerce companies could depress our stock price regardless of our results.

***We have issued options, warrants that have had and will have a dilutive effect on our shareholders.***

We have issued numerous options, and convertible securities to acquire our common stock that have had a dilutive effect on our shareholders. We depend on our ability to issue stock and options to conserve cash. We compensate a number of employees and consultants through stock option grants under the Company's 2001 Non-Qualified Stock Option Plan and more recently under the 2011 Non-Qualified Stock Option Plan. One hundred twenty million shares were registered under the 2001 plan since its inception in 2001, and thirty million shares were registered in 2011 under the 2011 plan. Typically, shares are immediately exercised by the employee or consultant. In 2012, employees received options for 249,097 shares equal to \$40,000 in compensation, and consultants and professionals received 16,365,272 shares equal to \$2,126,831 in compensation. Dilution is more substantial when our stock price is low.

***We may have difficulty obtaining additional financing as a result of the significant number of shares that have been issued and the few remaining shares available for issuance.***

New investors may either decline to make an investment in our Company due to the large number of shares outstanding and the few remaining shares that are authorized and available for issuance.

*“Penny stock” regulations may impose certain restrictions on marketability of securities.*

The SEC adopted regulations, which generally define "penny stock" to be an equity security that has a market price of less than \$5.00 per share. Our common stock may be subject to rules that impose additional sales practice requirements on broker-dealers who sell these securities to persons other than established customers and accredited investors (generally those with assets in excess of \$1,000,000, or annual incomes exceeding \$200,000 or \$300,000 together with their spouse). For transactions covered by these rules, the broker-dealer must make a special suitability determination for the purchase of these securities and have received the purchaser's prior written consent to the transaction.

Additionally, for any transaction, other than exempt transactions, involving a penny stock, the rules require the delivery, prior to the transaction, of a risk disclosure document mandated by the SEC relating to the penny stock market. The broker-dealer also must disclose the commissions payable to both the broker-dealer and the registered representative, current quotations for the securities and, if the broker-dealer is the sole market-maker, the broker-dealer must disclose this fact and the broker-dealer's presumed control over the market. Finally, monthly statements must be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks. Consequently, the "penny stock" rules may restrict the ability of broker-dealers to sell our common stock and may affect the ability to sell our common stock in the secondary market.

*The market for our Company's securities is limited and may not provide adequate liquidity.*

Our common stock is currently traded on the OTC Bulletin Board (“OTCBB”), a regulated quotation service that displays real-time quotes, last-sale prices, and volume information in over-the-counter equity securities. As a result, an investor may find it more difficult to dispose of, or obtain accurate quotations as to the price of, our securities than if the securities were traded on the Nasdaq Stock market, or another national exchange. There is a limited number of active market makers of our common stock. In order to trade shares of our common stock you must use one of these market makers unless you trade your shares in a private transaction. In the twelve months prior to December 31, 2012, the actual daily trading volume ranged from a low of 15,000 shares of common stock to a high of over 3.7 million shares of common stock with 13 days exceeding a trading volume of 1,000,000 shares. Selling our shares can be more difficult because smaller quantities of shares are bought and sold and news media coverage about us is limited. These factors result in a limited trading market for our common stock and therefore holders of our Company's stock may be unable to sell shares purchased should they desire to do so.

**Item 1B. Unresolved Staff Comments**

None.

## **Item 2. Properties**

As of December 31, 2012 the Company maintained its principal office, including its corporate offices and fulfillment center in Westborough, Massachusetts, pursuant to a lease, which expires in April 2016, for 26,061 square feet of office and warehouse space. The Company closed its Boston office in January 2012, and its Worcester office in April 2012, and occupied the new facility on January 13, 2012.

## **Item 3. Legal Proceedings**

From time to time we may be a party to various legal proceedings arising in the ordinary course of our business. Our management is not aware of any litigation outstanding, threatened or pending as of the date hereof by or against us or our properties which we believe would be material to our financial condition or results of operations.

## **Item 4. Mine Safety Disclosure**

None.

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**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

Our common stock, par value \$.001 per share, is presently traded on the Over-the-Counter Bulletin Board ("OTCBB") under the symbol, "PAYD".

The following table sets forth the high and low bid information for our common stock as reported by OTCBB for the eight quarters ended December 31, 2012. The quotations from the OTCBB reflect inter-dealer prices without retail mark-up, mark-down, or commission and may not represent actual transactions.

|                                  |        |        |
|----------------------------------|--------|--------|
| 2011                             | High   | Low    |
| Quarter ended March 31, 2011     | \$0.34 | \$0.22 |
| Quarter ended June 30, 2011      | \$0.49 | \$0.23 |
| Quarter ended September 30, 2011 | \$0.39 | \$0.20 |
| Quarter ended December 31, 2011  | \$0.27 | \$0.12 |
| 2012                             | High   | Low    |
| Quarter ended March 31, 2012     | \$0.26 | \$0.14 |
| Quarter ended June 30, 2012      | \$0.16 | \$0.08 |
| Quarter ended September 30, 2012 | \$0.11 | \$0.04 |
| Quarter ended December 31, 2012  | \$0.17 | \$0.03 |

As of March 14, 2013, there were approximately 1,544 holders of record of our common stock. Because many of the shares are held by brokers and other institutions on behalf of stockholders, the Company is unable to estimate the total number of individual stockholders represented by these holders of record.

We have not previously paid cash dividends on our common stock, and intend to utilize current resources to operate the business; thus, it is not anticipated that cash dividends will be paid on our common stock in the foreseeable future.

**Equity Compensation Plan Information**

|   | Number of Securities<br>To be<br>Issued Upon Exercise<br>of<br>Outstanding Options,<br>Warrants<br>and Rights | Weighted-Average<br>Exercise<br>Price of Outstanding<br>Options,<br>Warrants and Rights | Number of Securities<br>Remaining<br>Available For Future<br>Issuance<br>Under Equity<br>Compensation<br>Plans (Excluding<br>Securities<br>Reflected in Column<br>(a))<br>(c) |
|---|---|---|---|
|   | (a)   | (b)   | (c)   |
| Equity Compensation Plans Approved by<br>Security Holders     | 8,000,000   | \$ 0.095  | -   |
| Equity Compensation Plans Not Approved<br>by Security Holders | 10,030,582  | \$ 0.073  | 3,000,000   |
| Total   | 18,030,582  | \$ 0.083  | 3,000,000   |

Refer to Note 12, Notes to Financial Statements for the Years ended December 31, 2012, and 2011 incorporated by reference herein from Part II, Item 8, of this Annual Report, for a discussion of the material features of the stock options, warrants and related stock plans.

#### Recent Sales of Unregistered Securities

None.

#### Repurchase of Equity Securities

None.

## **Item 6. Selected Financial Data**

As a smaller reporting company, the Company is not required to provide the information for this Item 6.

## **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

### **Forward Looking Statements**

This Annual Report on Form 10-K contains certain forward-looking statements (within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934) regarding the Company and its business, financial condition, results of operations and prospects. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates", "could", "may", "should", "will", "would", and similar expressions or variations of such words are intended to identify forward-looking statements in this report. Additionally, statements concerning future matters such as the development of new services, technology enhancements, purchase of equipment, credit arrangements, possible changes in legislation and other statements regarding matters that are not historical are forward-looking statements.

Although forward-looking statements in this annual report reflect the good faith judgment of the Company's management, such statements can only be based on facts and factors currently known by the Company. Consequently, forward-looking statements are inherently subject to risks, contingencies and uncertainties, and actual results and outcomes may differ materially from results and outcomes discussed in this report. Although the Company believes that its plans, intentions and expectations reflected in these forward-looking statements are reasonable, the Company can give no assurance that its plans, intentions or expectations will be achieved. For a more complete discussion of these risk factors, see Item 1A, "Risk Factors."

For example, the Company's ability to achieve positive cash flow and to become profitable may be adversely affected as a result of a number of factors that could thwart its efforts. These factors include the Company's inability to successfully implement the Company's business and revenue model, tour or event cancellations, higher costs than anticipated, the Company's inability to sell its products and services to a sufficient number of customers, the introduction of competing products or services by others, the Company's failure to attract sufficient interest in, and traffic to, its sites, the Company's inability to complete development of its sites, the failure of the Company's operating systems, and the Company's inability to increase its revenues as rapidly as anticipated. If the Company is not profitable in the future, it will not be able to continue its business operations.

## Overview

The primary focus of PAID, Inc. (the “Company”) is to provide brand-related services to businesses, celebrity clients in the entertainment industry as well as charitable organizations. PAID's brand management, brand marketing, social media marketing, product design and merchandising, website design; development and hosting services are designed to grow each client's customer base in size, loyalty and revenue generation. We offer entertainers, charities, and business entities comprehensive web-presence and related services supporting and managing clients' official websites and fan-community services including e-commerce, VIP ticketing, live event fan experiences, user-generated content, client content publishing and distribution, fan forums, social network management, social media marketing, customer data capture, management and analysis.

## Critical Accounting Policies

Our significant accounting policies are more fully described in Note 3 to our financial statements. However, certain of our accounting policies are particularly important to the portrayal of our financial position and results of operations and require the application of significant judgment by our management; as a result, they are subject to an inherent degree of uncertainty. In applying these policies, our management makes estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures. Those estimates and judgments are based upon our historical experience, the terms of existing contracts, our observance of trends in the industry, information that we obtain from our customers and outside sources, and on various other assumptions that we believe to be reasonable and appropriate under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Our critical accounting policies include:

### *Inventories*

Inventories are stated at the lower of average cost or market on a first-in, first-out method. On a periodic basis we review inventories on hand to ascertain if any is slow moving or obsolete. In connection with this review, we establish reserves based upon management's experience and assessment of current product demand. A substantial portion of the Company's inventories is comprised of movie posters for which valuation is more subjective than with more standard inventories. The balance is comprised of merchandise and collectibles that relate to performing artists. General economic conditions, tour schedules of performing artists, and the reputation of the performing artists/athletes, might make sale or disposition of these inventories more or less difficult. Any increases in the reserves would cause a decline in profitability, since such increases are recorded as charges against operations.

*Prepaid royalties*

The Company accounts for prepaid royalties in accordance with FASB ASC 928, "Financial Reporting in the Record and Music Industry". Prepaid royalties represent amounts paid in advance to certain clients and are recoupable against future royalties earned by the clients. Advances are issued in either cash or stock and advance amounts are calculated based on the client's projected earning potential over a fixed period of time. Advances issued in stock are recorded at the fair value on the date of issue.

**Results of Operations***Comparison of the years ended December 31, 2012 and 2011*

The following discussion compares the Company's results of operations for the year ended December 31, 2012 with those for the year ended December 31, 2011. The Company's financial statements and notes thereto included elsewhere in this annual report contain detailed information that should be referred to in conjunction with the following discussion.

*Revenues*

The following table compares total revenue for the periods indicated.

|                               | Years ended December 31, |             |          |   |
|-------------------------------|--------------------------|-------------|----------|---|
|                               | 2012                     | 2011        | % Change |   |
| Merchandising and fulfillment | \$4,093,600              | \$2,736,900 | 49.6     | % |
| Client services               | 396,300                  | 387,400     | 2.3      | % |
| Touring revenue               | 9,478,300                | 3,796,200   | 148.6    | % |
| Total revenues                | \$13,968,200             | \$6,920,500 | 101.2    | % |

Revenues increased 102% in 2012 primarily from a 149% increase in touring revenue, a 2% increase in client services, and a 49% increase in merchandising and fulfillment.



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Merchandise and fulfillment revenues increased \$1,356,700 or 49.6% to \$4,093,600 compared to a increase of \$563,500 in 2011. In 2012 the Company focused on marketing and social media campaigns, which resulted in reaching new customers. The increase in new customers resulted in double digit revenue increases in a number of the Company's existing as well as new clients. In addition, the Company rolled out its new sales data management system which allowed the Company to develop client specific promotional campaigns, which resulted in better targeting of the existing customer base.

Client Services revenues increased \$8,900 or 2% to \$396,300 compared to \$387,400 in 2011.

Touring revenue increased \$5,682,100 or 150% to \$9,478,300 compared to \$3,796,200 in 2011. The Company has generated a consistent touring base and revenues are directly impacted by our client's touring schedules and frequency. In 2012 Aerosmith, Motley Crue, and the Moody Blues were the primary contributors to the increase in revenues.

### *Gross Profit*

Gross profit increased \$397,953 or 17% to \$2,722,927 compared to \$2,324,974 in 2011. Gross margin decreased 15 percentage points to 19% from 34% in 2011. The decrease in gross margin was mainly attributable to an increase in Touring revenue which has a lower margin.

### *Operating Expenses*

Total operating expenses in 2012 were \$6,470,477 compared to \$6,313,119 in 2011, an increase of \$157,358 or 2%. The increase is due to increases in personnel and facility costs.

*Net Loss*

The Company realized a net loss in 2012 of \$4,146,200 compared to a net loss of \$3,974,179 for the same period in 2011. The losses for 2012 and 2011 each represent \$(0.01) per share.

*Inflation*

The Company believes that inflation has not had a material effect on its results of operations.

*Comparison of the years ended December 31, 2011 and 2010*

The following discussion compares the Company's results of operations for the year ended December 31, 2011 with those for the year ended December 31, 2010. The Company's financial statements and notes thereto included elsewhere in this annual report contain detailed information that should be referred to in conjunction with the following discussion.

*Revenues*

The following table compares total revenue for the periods indicated.

|                               | Years ended December 31, |             |          |
|-------------------------------|--------------------------|-------------|----------|
|                               | 2011                     | 2010        | % Change |
| Merchandising and fulfillment | \$2,736,900              | \$2,173,400 | 26 %     |
| Client services               | 387,400                  | 490,200     | (21 )%   |
| Touring revenue               | 3,796,200                | 4,531,100   | (16 )%   |
| Total revenues                | \$6,920,500              | \$7,194,700 | (4 )%    |

Revenues decreased 4% in 2011 primarily from a 16% decrease in touring revenue and a 21% decrease in client services. The decrease was offset by a 26% increase in merchandising and fulfillment.

Merchandise and fulfillment revenues increased \$563,500 or 26% to \$2,736,900 compared to \$2,173,400 in 2010. In 2011 the Company focused on marketing and social media campaigns, which resulted in reaching new customers. The increase in new customers resulted in double digit revenue increases in a number of the Company's existing clients. In addition, the Company rolled out its new sales data management system, which allowed the Company to develop client specific promotional campaigns, which resulted in better targeting of the existing customer base.

Client Services revenues decreased \$102,800 or 21% to \$387,400 compared to \$490,200 in 2010. In 2010 the Company completed a large consulting project it obtained in 2009, and was hired by one of our major clients to provide creative and general business consulting services for a large US tour. At the end of 2010, those projects were completed. In 2011 the Company obtained smaller technology related projects resulting in the decrease in revenues for 2011 as compared to 2010.

Touring revenue decreased \$734,900 or 16% to \$3,796,200 compared to \$4,531,100 in 2010. The Company has generated a consistent touring base and revenues are directly impacted by our client's touring schedules and frequency. In 2011 our clients generally had shorter touring schedules and toured less frequently which was the primary contributor to the decrease in revenues.

#### *Gross Profit*

Gross profit increased \$163,900 or 8% to \$2,325,000 compared to \$2,161,100 in 2010. Gross margin increased 3.6 percentage points to 33.6% from 30.0% in 2010. The increase was mainly attributable to an increase in merchandising and fulfillment margins due to lower inventory cost and an increase in shipping and handling fees.

#### *Operating Expenses*

Total operating expenses in 2011 were \$6,313,100 compared to \$5,467,400 in 2010, an increase of \$845,700 or 15%. The increase is due to increases of \$229,200 in client expenses related to touring activities, credit card processing costs, and international shipping costs, \$347,100 in personnel costs due to an increase in key personnel and general increases in salary cost, \$243,700 in option compensation due to additional option grants, and \$21,500 in administrative costs.

*Net Loss*

The Company realized a net loss in 2011 of \$3,974,200 compared to a net loss of \$3,306,800 for the same period in 2010. The losses for 2011 and 2010 each represent \$0.01 per share.

*Inflation*

The Company believes that inflation has not had a material effect on its results of operations.

**Operating Cash Flows**

A summarized reconciliation of the Company's net loss to cash provided by (used in) operating activities for the years ended December 31, 2012, and 2011, is as follows

|  | 2012        | 2011        |
|--|-------------|-------------|
| Net loss   | (4,146,200) | (3,974,200) |
| Depreciation and amortization  | 77,055      | 40,626      |
| Unrealized gain on investment  | 38,056      | (80,000 )   |
| Inventory Reserve  | 398,120     | 125,000     |
| Bad debt   | 5,000       | 23,300      |
| Payments received in common stock  | -           | (125,000 )  |
| Payments made in common stock  | 24,167      | -           |
| Payment of stock option exercise received as compensation                              | -           | 235,750     |
| Change in fair value derivative  | 365,846     | 63,294      |
| Share based compensation   | 850,459     | 699,925     |
| Stock Subscription Receivable  | (64,000 )   |             |
| Amortization of prepaid facility costs   | 238,013     |             |
| Fair value of stock options awarded<br>in payment of outside services and compensation | 2,166,831   | 2,220,436   |
| Deferred revenues, net of prepaid royalties  | 119,398     | 576,372     |
| Changes in current assets and liabilities  | 416,284     | 631,457     |
| Net cash provided by operating activities  | 553,029     | 288,660     |

**Working Capital and Liquidity**

The Company had cash and cash equivalents of \$1,433,035 at December 31, 2012, compared to \$996,000 at December 31, 2011. The Company had approximately \$487,700 of working capital at December 31, 2012, a decrease of \$739,400 compared to \$1,227,100 at December 31, 2011. The decrease in working capital is attributed to the write down in inventories of \$398,000, an increase in accounts payable and accrued expenses of \$493,700, offset by increases in accounts receivables of \$159,500.

The Company had cash and cash equivalents of \$996,000 at December 31, 2011, compared to \$747,300 at December 31, 2010. The Company had approximately \$1,227,100 of working capital at December 31, 2011, a decrease of \$1,015,300, compared to \$2,242,400 at December 31, 2010. The decrease in working capital is attributed to increases of \$527,000 in accounts payable and accrued expenses directly related the the costs associated with fourth quarter touring and related royalties, \$506,000 due to the derivative liability related to the rent guarantee associated with or new facility, offset by a \$200,000 increase in investments.

The Company may need an infusion of additional capital to fund anticipated operating costs over the next 12 months. Management believes that that there are sufficient resources to generate positive cash flow through the continued growth in new business, through the recoupment of prepaid royalties, and an increase in inventory turns. Subject to the discussion below, management believes that the Company has adequate cash resources to fund operations during the next 12 months. In addition, management continues to explore opportunities and has added additional resources to monetize its patents. However, there can be no assurance that anticipated touring activity will occur, and that the Company will be successful in monetizing its patents. Management continues to seek alternative sources of capital to support operations. Finally, world economic conditions, in particular those in the United States, may impact sales of fan experiences and the availability of financing.

**Item 7A. Quantitative and Qualitative Disclosure about Market Risk**

As a smaller reporting company, the Company is not required to provide the information for this Item 7A.

**Item 8. Financial Statements and Supplementary Data**

The financial statements listed in Item 15(a) are incorporated herein by reference and are filed as a part of this report and follow the signature pages to this Annual Report on Form 10-K on page F-1.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures**

**Evaluation of Disclosure Controls and Procedures**

The Company's management, including the President of the Company, as its principal executive officer, and the Chief Financial Officer of the Company, as its principal financial officer, has evaluated the effectiveness of the Company's "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based upon this evaluation, the President and Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were not effective, due to material weaknesses in internal control over financial reporting described below, for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission is recorded, processed, summarized and reported within the time period specified by the Securities and Exchange Commission's rules and forms, and is accumulated and communicated to the Company's management, including its principal executive and financial officers, as appropriate to allow timely decisions regarding required disclosure.

As described in our accompanying *Management's Report on Internal Control over Financial Reporting*, we have identified five remaining material weaknesses in internal control over financial reporting. Because of these remaining material weaknesses, we concluded that, as of December 31, 2012, our internal control over financial reporting was not effective based on the criteria outlined in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Accordingly, we have also concluded that our disclosure controls and procedures were not effective as of December 31, 2012.

We have implemented new procedures and controls in 2012 and expect to take further steps to remediate the material weaknesses at the entity and activity levels, and to review further our procedures and controls in 2013. In addition, we expect to make additional changes to our infrastructure and related processes that we believe are also reasonably likely to strengthen and materially affect our internal control over financial reporting.

Prior to the complete remediation of these material weaknesses, there remains risk that the processes and procedures on which we currently rely will fail to be sufficiently effective, which could result in material misstatement of our financial position or results of operations and require a restatement. Moreover, because of the inherent limitations in all control systems, no evaluation of controls—even where we conclude the controls are operating effectively—can provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, our control systems, as we develop them, may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected and could be material to our financial statements.

The certifications of our principal executive officer and principal financial officer required in accordance with Rule 13a-14(a) under the Exchange Act and Section 302 of the Sarbanes-Oxley Act of 2002 are attached as exhibits to this Annual Report on Form 10-K. The disclosures set forth in this Item 9A contain information concerning (i) the evaluation of our disclosure controls and procedures, and changes in internal control over financial reporting, referred to in paragraph 4 of the certifications, and (ii) material weaknesses in the design or operation of our internal control over financial reporting, referred to in paragraph 5 of the certifications. Those certifications should be read in conjunction with this Item 9A for a more complete understanding of the matters covered by the certifications.

## Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining effective internal control over financial reporting of the Company. Internal control over financial reporting is a process designed by, or under the supervision of, our Chief Executive Officer and Chief Financial Officer and effected by our Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Our internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect our transactions and dispositions of our assets; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

Management, with the participation of our principal executive officer and principal financial officer, is required to evaluate the effectiveness of our internal controls over financial reporting as of December 31, 2012 based on criteria established under the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") integrated framework of internal controls. The COSO framework identifies five components of internal control and provides a basis for evaluating the effectiveness of internal controls. Management has concluded that our internal controls over financial reporting were not effective as of December 31, 2012 due to the following:

1. Entity Level Controls

Ineffective control environment, including lack of corporate governance

Ineffective communication of information

Ineffective monitoring of activities



2. Activity Level Controls

Lack of procedures and control documentation

Lack of segregation of duties

**1. Inadequate Entity Level Controls**

*Ineffective Control Environment*

The Control Environment is the tone of an organization and how the tone influences the control consciousness of its people. Control environment factors include, the integrity, ethical values, and competence of the entity's people; management's philosophy and operating style; the way management assigns authority and responsibility; the way management organizes and develops its people; and the attention and direction provided by the audit committee and board of directors. The control environment includes the Company's Corporate Governance which is made up of a set of practices, policies, laws, and principals, designed to provide guidance and structure to directors, managers, and employees with a clear view of corporate goals and business objectives. These processes and procedures need to be clearly defined, presented and administered to each participant in the organization, and should document the distribution of rights and responsibilities among employees, management, clients and customers.

*Steps taken towards Remediation for an Ineffective Control Environment:*

The Company has strengthened its hiring and employment practices by completing in-depth screenings of new personnel, and has initiated formal employee review procedures.

In 2011, the Company contracted with an outside consulting company to provide training to our managers, customer service and operational personnel. The Company is also assisting us in developing and documenting our policies, procedures and controls which will assist us in the remediation of our weakness in internal controls.

Management has direct oversight and responsibility for independent contractors and consultants. All independent contractors and consultants are required to follow strict corporate policies relating to confidential information, and non-disclosure of corporate and client data. Management sets project goals and objectives for each independent contractor and consultant and measures the performance of each on a regular basis.

Management and the Board formally meet to discuss our filings and the discussions are being documented for future reference. During these discussions, our auditors, and legal counsel may present to the Company various information which may be of material importance to our financial reporting and internal controls.

The Company has made improvements by designing and drafting a corporate governance policy which has been approved by the Board of Directors, which documents the role of the Board and management, functions of the Board, role of the Audit Committee, agenda items for Board meetings, recoupment of unearned compensation, indemnification, reporting of concerns and complaints, and director access to management.

#### *Ineffective Communication of Information*

Information and communication systems support the identification, capture, and, exchange of information in a form and time frame that enable people to carry out their responsibilities. This component includes information technology controls which are specific activities performed by persons or systems designed to ensure that the business objective can be met, protect the business from fraud and collusion, and keep the corporate assets protected and safe.

#### *Steps taken towards Remediation of Information Technology Controls:*

Enhanced the documentation and procedures of our information technology to control assurance that changes to financial applications are properly authorized and tested and that access to our information systems and financial applications are appropriately restricted.

- Updated our information systems user profiles to improve access controls.
- Implemented improvements to our information systems to further address control deficiencies.

Updated secure backup procedures with best practice methodologies for protecting our financial data and, in case of a problem, continuously testing restoration from backup tapes.

Enhanced the documentation of certain core proprietary technologies so that there is more redundancy and protection of corporate assets.

#### *Ineffective Monitoring*

Monitoring is a process that assesses the quality of internal control performance over time.

*Steps taken towards Reduction of Monitoring:*

The Company has reorganized the organizational reporting structure to enable greater oversight and control of operations which has increased the level of awareness and accountability.

The Company meets regularly throughout the year to review operating results, policies and procedures, and employee reviews and practices. The Company also has an annual planning meeting to set strategy and goals for the coming year, and consults with its outside professionals on compliance requirements.

New management personnel are required to review their procedures and policies to make sure they are effective. The Company is evaluating the procedure and policies that have material weakness and developing corrective action plans to strengthen our internal controls.

The Company has made sweeping changes to its policies and procedures with regard to its financial reporting systems. Upgrades to software systems have been made throughout 2011 which has resulted in the automation of accounting transactions and has enhanced our financial reporting and timeliness of operating results. Management and staff are more integrated into the review process, and results are tracked against expectations.

Finance staff are required to review expenses for proper approval and accounting treatment. Managers and staff are required to have expenditures pre-approved by their supervisor, all significant expenditures require multiple approvals including Company officers.

In 2011 the Company implemented new procedures and policies, upgraded systems, and hired additional personnel. The Company believes significant improvements have been made to remediate its material weakness in the internal controls over financial reporting at the entity level, but does not have the appropriate documentation to support its efforts. The Company also believes that further work is still required to develop appropriate controls in some aspects of entity level control to provide reasonable assurance that controls are designed in the most effective and efficient manner possible. While we believe these changes will be effective at mitigating risk of material error, there continues to be additional work required for us to conclude that all three of these control areas are operating effectively. As noted in the Management's Report on Internal Control over Financial Reporting, we consider each of these control areas within the entity level control to constitute a material weakness.

## 2. Inadequate Activity Level Controls

### *Lack of procedures and control documentation*

The Company's lacks sufficient documentation relating to certain accounts, revenue recognition, purchasing, accounts payable, inventory, and financial closing, which in effect make these internal controls ineffective. The lack of documentation in internal controls relating to these accounts may affect the financial statements and will directly affect the nature and timing of other auditing procedures for certain activities.

### *Steps taken towards Remediation of Revenue Recognition:*

- Most revenue transactions are online credit card payments from products placed for sale on various clients' web sites. The pricing for the products listed is reviewed and approved by management and documented on purchase orders that are reviewed by each department manager.

In 2011 the Company upgraded its transactional processing systems which resulted in the automation of several manual accounting tasks. This automation eliminated the risk of human error for these manual tasks and created a more concise audit trail in the revenue recognition process.

Each week client managers and marketing staff receive a document outlining the revenues from all clients with strategic information enabling them to compare actual results versus plan and be able to prepare goal and objectives for future weeks. Management reviews the document and works with client management and marketing personnel to hit incremental milestones and forecast.

All web sales are reconciled across the Company's multiple revenue and accounting systems comparing for any discrepancies.

Improved systems and procedures reconciling offsite revenue nightly. This process reconciles individual revenues directly back to individual general ledger accounts. There is a clear segregation of duties throughout the process minimizing risk of fraud and requiring more individuals to be accountable at different times.

*Steps taken towards Remediation of Expenditures and Accounts Payable:*

Established improved procedures documenting and providing an approval process for authorizing a merchandising agent to complete and submit a purchase order. Each purchase order, has been authorized by management, and a clear segregation of duties exists between the merchandise being ordered, received and payment made.

An internal control procedure has been implemented for receiving goods accurately and validating the cost, quantities, quality of goods against the purchase order.

- Implemented a policy to obtain at least two quotes on inventory purchases.

Implemented a signature authorization policy outlining specific authority prior to any commitment of our funds for various transactions and purchases.

Client accounts are reviewed monthly with client managers and accounting staff to assess project performance against expectations. Client revenues are reviewed weekly with client managers and marketing to assess actual results versus plan. Expenses are reviewed as incurred for proper accounting treatment and approval. Client royalty statements are prepared as required and reviewed by management and client managers.

The Vendor Master File is reviewed on a weekly basis for updates and changes and any changes are analyzed and monitored for their activity and frequency.

*Steps taken towards Remediation of Inventory Controls:*

Access to changing data within the inventory management software has been restricted to only essential personnel.

Other individuals have access to view data and access reports, but they are restricted from making any changes within the system.

Policies have been implemented that require all purchases and inventory maintenance to be reviewed by management to authorize pricing, sales and promotional events through client web sites.

Improved procedures regarding receiving logs, quality assurance checks, and purchase order processes have been implemented to provide for a clear separation of duties. These procedures deter fraud and protect against collusion.

Improved physical inventory controls, and interim cycle counts, are overseen by management, with weekly reviews randomly checking floor to sheet and sheet to floor. This procedure, along with improved reporting, is designed to tighten inventory controls and increase inventory turns. Management and merchandising personnel meet regularly to review inventory levels, and client product lines.

*Steps taken towards Remediation of Financial Closing:*

- The Company has moved all accounting functions in-house from a third party certified accounting firm. The Company closes its books and reconciles all accounts monthly, and provides management with a comprehensive set of financial and operating reports and analysis of results.

*Lack of Segregation of Duties*

A clear and concise segregation of duties is important to maximize checks and balances so that no single individual has control over two or more phases of a transaction or operation. A strong segregation of duty also is critical to reduce effectively the risk of mistakes and inappropriate actions preventing fraud and discourages collusion. It can be difficult for small businesses to always have a clear separation of duties because there simply are not enough personnel to cover each and every process and procedure. Ultimately, checks and balances need to be in place as a supportive measure to the business operations, but also as a fraud prevention measure as well.

*Steps taken towards Remediation for Segregation of Duties:*

The Company has changed processes and procedures, has hired additional personnel, and has made upgrades to its inventory management system to better align duties and responsibilities so that there is a greater segregation of duties. The Company has added additional personnel and has segregated certain duties and tasks to provide greater oversight. Transactional processing requires review and approval from an independent staff member or manager. Manual tasks are required to follow written or verbal procedures that have been approved by the Company. The Company implemented new project management software, which was designed to increase efficiencies and reduce overhead. The software also identifies deliverables, which may be dependent on other deliverables enabling the project managers to redirect duties to other individuals. This software assists the Company with reducing its dependency on any one particular employee with multiple responsibilities, thus preventing a bottleneck and risk of too much control on any one individual.

In 2012 the Company made significant improvements to the activity level controls specifically with regard to the deficiencies with the financial close and inventory controls. With the consolidation of facilities in 2012, the Company expects to take additional steps in 2013 to remediate the deficiency in information technology controls and has begun to outline the steps needed to cure this deficiency. In addition, further work is required to develop appropriate controls

in the other aspects of activity level control to provide reasonable assurance that controls are designed in the most effective and efficient manner possible. Therefore, while we believe these changes are effective at mitigating risk of material error, there continues to be additional work required for us to conclude that both of these control areas are operating effectively. Therefore, as noted in the Management's Report on Internal Control over Financial Reporting, we consider each of these control areas within the activity level control to constitute a material weakness.

A factor for our internal control deficiencies is the small size of the Company and the lack of a financial expert on the Audit Committee of the Board of Directors and other corporate governance controls. As defined by the Public Company Accounting Oversight Board Auditing Standard No. 5, a material weakness is a significant control deficiency or a combination of significant control deficiencies that results in there being more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. Management continues to monitor and assess the controls to ensure compliance.

As a smaller reporting company, our independent registered public accounting firm is not required to issue a report on the Company's internal control over financial reporting as of December 31, 2012.

#### *Changes in Internal Control Over Financial Reporting*

As discussed in the Managements' Annual Report on Internal Control over Financial Reporting, the Company made a number of changes to improve its internal controls over financial reporting late in 2008. Although significant steps were taken late in 2008, no additional changes were made in 2009 or 2010. In 2011 the Company made considerable improvements to the entity and activity controls and expects to take further steps in 2013 to remediate the outlined deficiencies. However, while we believe they are effective at mitigating risk of material error, we have not yet concluded that they are operating effectively. There was no change in our internal control over financial reporting during the fourth fiscal quarter of 2012 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information**

Not applicable.

**PART III**

**Item 10. Directors, Executive Officers and Corporate Governance**

**Directors and Executive Officers**

The following table sets forth certain information regarding the directors and executive officers of PAID:

| Name                | Age | Position                         |
|---------------------|-----|----------------------------------|
| W. Austin Lewis, IV | 37  | President, CEO, CFO and Director |
| Andrew Pilaro       | 43  | Director                         |

Andrew Pilaro was elected as of September 19, 2000, for a term expiring at the 2001 Annual Meeting of Stockholders and until their successors are elected and qualified. W. Austin Lewis was appointed on July 31, 2012. The Company has not held an annual meeting or elected directors since September 19, 2000. Under the Delaware General Corporation Law, each director holds office until such director's successor is elected and qualified or until such director's earlier resignation or removal. The following is a description of the current occupation and business experience for at least five years for each director and executive officer.

**Andrew Pilaro** has served as a Director of PAID since September 2000. Since 2005, he has served as Chairman of CAP Advisors Limited, an investment management company, with responsibility for asset management. Mr. Pilaro was asked to serve as a director because he provides investment management skills and general business background.

**W. Austin Lewis, IV** currently serves CEO, CFO, and Director of PAID as well as the CEO of Lewis Asset Management Corp., an investment management company headquartered in New York City, which he founded in 2004. From 2003 to 2004, Mr. Lewis was employed at Puglisi & Company, a New York based broker-dealer registered with FINRA, where he served as a registered representative and managed individual client accounts,



conducted due diligence for investment banking activities and managed his own personal account. In 2002, Mr. Lewis co-founded Thompson Davis & Company, Inc., a registered broker-dealer headquartered in Richmond, Virginia. From 1998 to 2002, Mr. Lewis was employed by Branch Cabell and Company, Inc. in Richmond, Virginia where he was a registered representative. Following the November 2000 acquisition of Branch Cabell by Tucker Anthony Incorporated (“Tucker Anthony”), Mr. Lewis served as a Vice President for Tucker Anthony and subsequently RBC Dain Rauscher, Inc. which acquired Tucker Anthony in August of 2001. Mr. Lewis received his Bachelor of Science degree in Finance and Financial Economics from James Madison University in 1998. Mr. Lewis is also a director on the following companies with a class of securities registered: MAM Software Group, Inc. and Viryanet LTD. Mr. Lewis was also a director of Diamondhead Casino Corp. and resigned as director in 2011. Mr. Lewis was asked to serve as a director because he had a thorough knowledge, through his prior investment in the Company, of the Company’s strengths and weaknesses and has a strong background in being able to make companies run efficiently and successfully.

The Company has not made any material changes to the procedures by which security holders may recommend nominees to the Board of Directors. The Board does not have a separate nominating committee or compensation committee.

#### **Audit Committee**

The Securities and Exchange Commission has adopted rules to implement certain requirements of the Sarbanes-Oxley Act of 2002 pertaining to public company audit committees. One of the rules requires a company to disclose whether it has an “audit committee financial expert” serving on its audit committee. Based on its review of the criteria of an audit committee financial expert under the rule adopted by the SEC, the Board of Directors does not believe that any member of the Board of Directors' Audit Committee would be described as an audit committee financial expert. At this time, the Board of Directors believes it would be desirable for the Audit Committee to have an audit committee financial expert serving on the committee. While from time to time informal discussions as to potential candidates have occurred, no formal search process has commenced. Andrew Pilaro, the Company's only independent director, is the sole member of the audit committee. The audit committee does not have a charter.

## **Audit Committee Report**

The Audit Committee reviewed and discussed our audited financial statements for the year ended December 31, 2012 with our management. The Audit Committee also reviewed and discussed our audited financial statements and the matters required to be discussed, by the Public Company Accounting Oversight Board (“PCAOB”), including material weaknesses and other internal control deficiencies with Rosen Seymour Shapss Martin & Company LLP, our independent registered public accounting firm. The Audit Committee received from Rosen Seymour Shapss Martin & Company LLP the written disclosures and letter required by applicable requirements of the PCAOB regarding the independent accountant's communications with the audit committee concerning independence, and has discussed with the independent accountant the independent accountant's independence.

Based on the reviews and discussions referred to above, the Audit Committee recommended to our Board of Directors that our audited financial statements be included in our Annual Report on Form 10-K for the year ended December 31, 2012.

### The Audit Committee

Andrew Pilaro

## **Code of Ethics**

The Company has adopted a Code of Ethics that applies to all of its directors, officers, and employees, including its principal executive officer, principal financial officer, principal accounting officer, or controller, or persons performing similar functions. A written copy of the Company's Code of Ethics will be provided to anyone, free of charge, upon request to: W. Austin Lewis, President, PAID, INC., 40 Washington Street, Westborough, Massachusetts 01581.

Any waiver of the code of business conduct and ethics for directors or executive officers, or any amendment to the code that applies to directors or executive officers, may only be made by the board of directors. We intend to satisfy the disclosure requirement under Item 5.05 of Form 8-K regarding an amendment to, or waiver from, a provision of this code of ethics by posting such information on our web site, at the address and location specified above. To date, no such waivers have been requested or granted.

## **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's directors and executive officers, and persons who own more than 10% of the Company's outstanding Common Stock to file with the Securities and Exchange Commission initial reports of ownership and reports of changes in ownership of Common Stock. These persons are required by SEC regulation to furnish the Company with copies of all such reports they file. To the Company's knowledge, based solely on a review of the copies of such reports furnished to the Company and representations that no other reports were required, all Section 16(a) filing requirements applicable to its officers and directors and beneficial owners of more than 10% of the Company's stock, have been complied with for the period which this Form 10-K relates.

**Item 11. Executive Compensation**

Our two member board of directors serves in lieu of a compensation committee. The Board does not have a separate compensation committee. The Board is responsible for establishing policies and otherwise discharging the responsibilities of a compensation committee with respect to the compensation of our executive officers.

**Compensation to the Named Executive Officers**

The following table sets forth the compensation of the Company's chief executive officer, the chief financial officer, and each officer whose total cash compensation exceeded \$100,000, for the last three fiscal years ended December 31, 2012, 2011, and 2010.

| Name and<br>Principal Position  | Summary Compensation Table |            |          |                    |           |
|---|----------------------------|------------|----------|--------------------|-----------|
|   | Year                       | Salary (5) | Bonus    | Option Awards (\$) | Total     |
| W. Austin Lewis, IV (1) (PEO)(PFO)  | 2012                       | \$ 39,808  | \$0      | \$ 493,457         | \$533,265 |
| Gregory Rotman (2)(6)<br>President and Chief Executive Officer                  | 2012                       | \$ 206,731 | \$0      | \$ 0               | \$206,731 |
|   | 2011                       | \$ 276,400 | \$0      | \$ 363,400         | \$639,800 |
|   | 2010                       | \$ 113,000 | \$0      | \$ 0               | \$113,000 |
| Christopher Culross (4)<br>Chief Financial Officer                              | 2012                       | \$ 169,231 | \$0      | \$ 0               | \$169,231 |
|   | 2011                       | \$ 200,000 | \$0      | \$ 173,500         | \$373,500 |
|   | 2010                       | \$ 196,635 | \$0      | \$ 0               | \$196,635 |
| Richard Rotman (3)<br>Chief Operating Officer, Vice<br>President, and Secretary | 2012                       | \$ 94,200  | \$0      | \$ 0               | \$94,200  |
|   | 2011                       | \$ 204,369 | \$0      | \$ 74,200          | \$278,569 |
|   | 2010                       | \$ 113,000 | \$57,331 | \$ 0               | \$170,331 |

1. Mr. Lewis's start date was July 31, 2012

2. Mr. G. Rotman resigned as of October 12, 2012.

3. Mr. R. Rotman resigned as of September 24, 2012, but remains an employee of the Company.

4. Mr. Culross was promoted to CFO in March 2010 and resigned as of November 30, 2012.

Represents the dollar amount recognized for financial statement reporting purposes for the year ended December 31, 2011 in accordance with FASB ASC Topic 718, as outlined in Note 8 of our Audited Financial Statements contained herein.

6. Mr. G. Rotman reimbursed the Company for certain expenses in the amount of \$47,300.

The following tables set forth certain information related to outstanding equity awards as of December 31, 2012 for our executive officers.

## OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

| Name   | Option Awards   |   |   |   | Option Exercise Price (\$) | Option Expiration Date |
|--|---|---|---|---|----------------------------|------------------------|
|  | Number of Securities Underlying Unexercised Options (#) Exercisable | Number of Securities Underlying Unexercised Options (#) Unexercisable | Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Options (#) | Number of Securities Underlying Exercisable Options (#) |                            |                        |
| W. Austin Lewis, IV President and CEO (PEO)(PFO)                                   | 5,000,000   | 0   | 0   | 0   | \$ 0.065                   | 8/8/2022               |
|  | 5,000,000   | 0   | 0   | 0   | \$ 0.041                   | 10/15/2022             |
|  | 1,000,000   | 0   | 0   | 0   | \$ 0.048                   | 12/6/2022              |
| Gregory Rotman, President and CEO  | 2,500,000   | 0   | 0   | 0   | \$ 0.15                    | 11/10/2021             |
| Christopher Culross,<br>Chief Financial Officer, Treasurer and Assistant Secretary | 1,500,000   | 0   | 0   | 0   | 0.145                      | 11/10/2021             |
| Richard Rotman,<br>Chief Operating Officer, Vice President and Secretary           | 2,500,000   | 0   | 0   | 0   | \$ 0.15                    | 1/10/2018              |

None of the Company's executive officers who serve as directors receive separate compensation from the Company for serving as directors. On October 11, 2002, Andrew Pilaro received options to purchase 2,000,000 shares of common stock at an exercise price of \$.041, pursuant to the 2002 Stock Option Plan, subject to the following vesting schedule: options to purchase 800,000 shares of common stock vested immediately; options to purchase an additional 600,000 shares of common stock vested on October 11, 2003, and options to purchase 600,000 shares of common stock vested on October 11, 2004, of which 1,000,000 shares were exercised in 2012 and 1,000,000 expired in 2012. On November 10, 2011 Andrew Pilaro received an additional option grant to purchase 500,000 shares of common stock at an exercise price of \$0.145, pursuant to the 2002 Stock Option Plan. The shares granted vested immediately and expire on November 10, 2021. On December 6, 2012, Mr. Pilaro received an additional option grant to purchase 1,000,000 shares of common stock at an exercise price of \$0.048 which expires on December 6, 2022.

The following table provides compensation information for the one-year period ended December 31, 2012 for the only non-employee member of our Board of Directors.

| Name and | Director Compensation in 2012<br>Total |
|----------|--|
|----------|--|

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|               | Fees<br>earned or (\$)<br>paid in<br>cash | Option Awards |
|---------------|---|---------------|
| Andrew Pilaro | \$ 41,000                                 | \$ 38,834     |
|               |   | \$ 79,834     |

In 2012, we compensated a number of non-executive employees and consultants through stock option grants under the Company's 2001 Non-Qualified Stock Option Plan. The 2001 Plan expired on January 31, 2011 and was replaced with the 2011 Non-Qualified Stock Option Plan. One hundred twenty million shares were reserved under the 2001 Plan since its inception, and thirty million shares were reserved under the 2011 Plan. Typically, except for executive officers, shares were immediately exercised by the employee or consultant. In 2012, employees received options for 249,097 shares equal to \$39,751 in compensation, and consultants and professionals received 16,365,272 shares equal to \$2,110,466 in compensation.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

To the knowledge of the management of the Company the following table sets forth the beneficial ownership of our common stock as of March 29, 2013 of each of our directors and executive officers, and all of our directors and executive officers as a group, and other beneficial owners holding more than five percent of the Company’s issued and outstanding shares.

| Name of Beneficial Owner  | Amount and Nature of Beneficial Ownership | Percent of Class (3) |
|---|---|----------------------|
| W Austin Lewis IV   | 36,689,145 (1)                            | 11.24 %              |
| Andrew Pilaro   | 2,568,700 (2)                             | 0.79 %               |
| All directors and executive officers as a group (2 individuals) | 39,257,845                                | 12.03 %              |

Included are options to purchase 11,000,000 shares of the Company’s common stock and shares held for the (1) following funds for which W. Austin Lewis, IV is the General Partner: 23,549,960 by Lewis Opportunity Fund, L.P. and 1,612,685 shares by LAM Waiting Game Fund LTD.

(2) Includes 17,200 shares held indirectly as custodian for Mr. Pilaro's minor sons and options to purchase 2,500,000 shares of the Company's common stock all of which are vested.

(3) Percentages are calculated on the basis of the amount of outstanding securities plus for such person or group, any securities that person or group has the right to acquire within 60 days.

To the knowledge of the management of the Company, based solely on our review of SEC filings, no other shareholder is the beneficial owner of more than five percent of the Company’s common stock.

The information regarding the Company's "Equity Compensation Plan Information" is incorporated herein by reference in Part II, Item 5 of this Annual Report on Form 10-K.

**Item 13. Certain Relationships and Related Transactions, and Director Independence**



The Company did not engage in any transaction in 2011 or 2012, and does not currently propose any transaction, in which the Company was is a participant and the amount involved exceeds \$120,000, and in which any related person had or will have a direct or indirect material interest.

### **Review, Approval or Ratification of Transactions with Related Parties**

It is our unwritten policy, which policy is not otherwise evidenced, for any related party transaction that involves more than a de minimis obligation, expense or payment or stock option or equity grants, to obtain approval by our entire board of directors prior to our entering into any such transaction. In conformity with our various policies on related party transactions, any transactions discussed in this Item 13 has been reviewed and approved by our board of directors.

### **Director Independence**

We are currently traded on the OTCBB. Accordingly, we are not required to and do not have a majority of independent directors or a compensation or nominating committee. Andrew Pilaro is the sole member of the audit committee.

Our board of directors currently consists of two members. Our board of directors determined that one of the two directors, Andrew Pilaro, is independent under the standards of the "Nasdaq Global Market" pursuant to Nasdaq Listing Rule 5605.

### **Item 14. Principal Accountant Fees and Services**

*Audit Fees.* The aggregate fees billed by Rosen Seymour Shapss Martin & Company LLP for the audit of the Company's annual financial statements for the fiscal year ended December 31, 2012, and the reviews of the quarterly financial statements included in the Company's Forms 10-Q for fiscal years 2012 were \$222,006.

The aggregate fees billed by Grant Thornton LLP for the audit of the Company's annual financial statements for the fiscal year ended December 31, 2012, and the reviews of the quarterly financial statements included in the Company's Forms 10-Q for fiscal year 2012 and 2011, were \$77,990 and \$95,300 respectively.

*Audit Related Fees.* There were no audit related fees for the past two fiscal years. There were no fees billed to the Company by Rosen Seymour Shapss Martin & Company LLP for the past two fiscal years for assurance and related services that are reasonably related to the performance of the audit or review of the Company's financial statements.

*Tax Fees.* There were no fees billed to the Company by Rosen Seymour Shapss Martin & Company LLP in either of the past two fiscal years for professional services for tax compliance, tax advice, and tax planning.

*All Other Fees.* In 2012 the Company was billed by Rosen Seymour Shapss Martin & Company LLP \$9,156 in fees for other services. There were no fees billed to the Company by Rosen Seymour Shapss Martin & Company LLP for any other services in 2011.

The Audit Committee approves all audit and audit-related fees. The Audit Committee is required to pre-approve all non-audit services to be performed by the auditor. The percentage of hours expended on the principal accountant's engagement to audit the Company's financial statements for the most recent fiscal year that were attributed to work performed by persons other than the principal accountant's full-time, permanent employees was 0%.

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

(a)(1) Financial Statements

For a list of the financial information included herein, see “Index to Audited Financial Statements” on page 41 of this Annual Report on Form 10-K.

(a)(2) Financial Statements Schedules

All schedules are omitted because they are not applicable or the required information is included in the financial statements or notes thereto.

(a)(3) Exhibits

The list of exhibits filed as a part of this Annual Report on Form 10-K is set forth on the Exhibit Index immediately preceding the exhibits hereto and is incorporated herein by reference.

**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.

PAID, INC.

By: /s/ W. Austin Lewis, IV  
W. Austin Lewis, IV, President, CEO and Chief  
Financial Officer (PEO and PFO)

Date: April 15, 2013

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.

| Signature                          | Title    | Date           |
|------------------------------------|----------|----------------|
| /s/ Andrew Pilaro<br>Andrew Pilaro | Director | April 15, 2013 |

|  |          |                |
|--|----------|----------------|
| /s/ W. Austin Lewis, IV<br>W. Austin Lewis, IV | Director | April 15, 2013 |
|--|----------|----------------|

**EXHIBIT INDEX**

| No.   | Description of Exhibits   |
|-------|---|
| 3.1   | Certificate of Incorporation, as amended (incorporated by reference to Exhibit 3.1 to Form 8-K, filed on November 25, 2003)   |
| 3.2   | Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 to Form 8-K, filed on December 8, 2004)   |
| 4.1   | Specimen of certificate for Common Stock (incorporated by reference to Exhibit 4.1 to Form SB-2/A filed on December 1, 2000)  |
| 4.2   | Agreement dated November 21, 2008, by and between the Company and Lewis Asset Management Equity Fund, LLP with respect to the purchase of 2,500,000 shares at \$.20 per share (incorporated by reference to Exhibit 4.2 to Form 10-KSB filed on March 31, 2009) |
| 4.3   | Form of Warrant to Lewis Asset Management with respect to Promissory Note dated April 29, 2009 (incorporated by reference to Exhibit 4.2 to Form 10-Q filed on May 12, 2009)  |
| 10.1+ | 2001 Non-Qualified Stock Option Plan, as amended (incorporated by reference from Exhibit 99.1 to Form S-8 filed on September 5, 2003)   |
| 10.2+ | 2002 Non-Qualified Stock Option Plan (incorporated by reference from Exhibit 10.17 to Form 10-KSB filed on March 31, 2003)  |
| 10.3+ | 2011 Non-Qualified Stock Option Plan (incorporated by reference from Exhibit 99.1 to Form S-8 filed on February 2, 2011)  |
| 10.4  | Promissory Note dated April 29, 2009 for up to \$2,500,000 to Lewis Asset Management (incorporated by reference to Exhibit 10.2 to Form 10-Q filed on May 12, 2009)   |
| 10.5  | Lease agreement, dated December 7, 2011 between Forty Washington, LLC and the Company (incorporated by reference to exhibit 10.1 to our Report on Form 8-K/A filed on December 13, 2011)  |
| 10.6+ | PAID, Inc. 2012 Non-Qualified Stock Option Plan (incorporated by reference to Exhibit 10.1 to Form 10-Q filed on October 18, 2012)  |
| 10.7+ | Agreement for Non-Qualified Stock Option under the PAID, Inc. 2012 Non-Qualified Stock Option Plan awarded to W. Austin Lewis, IV, dated October 15, 2012 (incorporated by reference to Exhibit 10.2 to Form 10-Q filed on October 18, 2012)                    |
| 10.8+ | Agreement for Non-Qualified Stock Option under the PAID, Inc. 2011 Non-Qualified Stock Option Plan awarded to W. Austin Lewis, IV, dated August 8, 2012 (incorporated by reference to Exhibit 10.3 to Form 10-Q filed on October 18, 2012)                      |
| 10.9  | Agreement dated January 31, 2013 between Paid, Inc., and MCN Interactive, LLC d/b/a MusicCityNetworks (incorporated by reference to Exhibit 10.1 to Form 8-K filed on February 5, 2013)   |
| 23*   | Consent of Rosen Seymour Shapss Martin & Company LLP  |
| 31.1* | CEO Certification required under Section 302 of Sarbanes-Oxley Act of 2002  |
| 31.2* | CFO Certification required under Section 302 of Sarbanes-Oxley Act of 2002  |
| 32.0* | CEO and CFO Certification required under Section 906 of Sarbanes-Oxley Act of 2002  |

\*filed herewith

+Indicates a management contract or any compensatory plan, contract or arrangement



**PAID, INC.**

**INDEX TO AUDITED FINANCIAL STATEMENTS**

**DECEMBER 31, 2012 AND 2011**

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and

Stockholders of PAID, Inc.

We have audited the accompanying balance sheets of PAID, Inc. as of December 31, 2012, and 2011, and the related statements of operations, shareholders' equity and cash flows for each of the years in the two-year period ended December 31, 2012. PAID, Inc.'s management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of PAID, Inc. as of December 31, 2012, and 2011, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2012 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the financial statements, the Company has had recurring losses from operations since inception and has an accumulated deficit of \$50,284,867 as of December 31, 2012. The future of the Company is dependent upon its ability to raise equity and debt financing and achieve profitable operations. These circumstances create substantial doubt about the Company's ability to continue as a going concern. Management's intentions with respect to this matter are described in Note 2. The accompanying financial statements do not include any adjustments that might result from the outcome of these circumstances.

/s/ Rosen Seymour Shapss Martin & Company LLP

CERTIFIED PUBLIC ACCOUNTANTS



New York, New York

April 15, 2013

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**PAID, INC.****BALANCE SHEETS****AS OF DECEMBER 31,**

|   | 2012<br>(Audited) | 2011<br>(Audited) |
|---|-------------------|-------------------|
| <b>ASSETS</b>   |                   |                   |
| Current assets:   |                   |                   |
| Cash and cash equivalents   | \$1,433,034       | \$995,989         |
| Investments   | 142,777           | 205,000           |
| Accounts receivable, net  | 348,855           | 194,321           |
| Inventories, net  | 420,709           | 876,712           |
| Prepaid expenses and other current assets   | 310,180           | 574,096           |
| Prepaid royalties   | 329,796           | 522,120           |
| Total current assets  | 2,985,351         | 3,368,238         |
| Property and equipment, net   | 212,923           | 91,013            |
| Intangible asset, net   | 6,125             | 7,066             |
| Prepaid facility Costs  | 1,027,148         | 1,468,036         |
| Total assets  | \$4,231,547       | \$4,934,353       |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>   |                   |                   |
| Current liabilities:  |                   |                   |
| Accounts payable  | \$728,026         | \$491,362         |
| Capital leases - current portion  | 26,303            | 13,815            |
| Accrued expenses  | 1,512,842         | 1,332,516         |
| Deferred revenues   | 230,481           | 303,407           |
| Total current liabilities   | 2,497,652         | 2,141,100         |
| Long term liabilities   |                   |                   |
| Capital leases - net of current   | 48,624            | 21,034            |
| Commitments and contingencies   |                   |                   |
| Shareholders' equity:   |                   |                   |
| Common stock, \$.001 par value, 350,000,000 shares authorized; 328,874,050, and 308,736,705 shares issued and outstanding at December 31, 2012, and 2011 respectively | 328,874           | 308,737           |
| Additional paid-in capital  | 52,376,455        | 49,273,340        |

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|  |              |              |
|--|--------------|--------------|
| Accumulated deficit                        | (50,956,058) | (46,809,858) |
| Stock subscription receivable              | (64,000 )    | -            |
| Total shareholders' equity                 | 1,685,271    | 2,772,219    |
| Total liabilities and shareholders' equity | \$4,231,547  | \$4,934,353  |

See accompanying notes to financial statements

**PAID, INC.****STATEMENTS OF OPERATIONS****FOR THE YEARS ENDED DECEMBER 31,**

|   | 2012           | 2011           |
|---|----------------|----------------|
| Revenues  | \$13,968,231   | \$6,920,508    |
| Cost of revenues                                      | 11,245,304     | 4,595,534      |
| Gross profit  | 2,722,927      | 2,324,974      |
| Operating expenses                                    | 6,470,477      | 6,313,119      |
| Loss from operations                                  | (3,747,550 )   | (3,988,145 )   |
| Other Income (expense)                                |                |                |
| Interest expense                                      | (5,769 )       | (2,747 )       |
| Other income  | 11,021         | -              |
| Unrealized gain (loss) on investment                  | (38,056 )      | 80,000         |
| Unrealized loss on stock price guarantee              | (365,846 )     | (63,294 )      |
| Total other income (expense), net                     | (398,650 )     | 13,959         |
| Loss before taxes                                     | (4,146,200 )   | (3,974,186 )   |
| Provision for income taxes                            | -              | -              |
| Net loss  | \$(4,146,200 ) | \$(3,974,186 ) |
| Loss per share - basic                                | \$(0.01 )      | \$(0.01 )      |
| Weighted average number of shares - basic and diluted | 320,705,220    | 294,685,429    |

See accompanying notes to financial statements

**PAID, INC.****STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY****FOR THE FOR THE YEARS ENDED DECEMBER 31, 2012, AND 2011**

|   | Common stock<br>Shares | Amount    | Additional<br>Paid-in<br>Capital | Accumulated<br>Deficit | Stock<br>Subscription<br>Receivable | Total       |
|---|------------------------|-----------|----------------------------------|------------------------|-------------------------------------|-------------|
| Balance, December 31, 2010  | 286,449,511            | \$286,450 | \$44,861,127                     | \$(42,835,679)         | \$ -                                | \$2,311,898 |
| Issuance of common stock pursuant to exercise of stock options granted to employees for services        | 2,280,344              | 2,280     | 524,295                          | -                      | -                                   | 526,575     |
| Issuance of common stock pursuant to exercise of stock options granted to professionals and consultants | 7,211,585              | 7,212     | 1,686,649                        | -                      | -                                   | 1,693,861   |
| Issuance of restricted common stock for the prepayment of facility costs                                | 6,082,985              | 6,083     | 1,271,344                        | -                      | -                                   | 1,277,427   |
| Share based compensation related to issuance of incentive stock options                                 | -                      | -         | 699,925                          | -                      | -                                   | 699,925     |
| Options exercised   | 6,712,280              | 6,712     | 230,000                          | -                      | -                                   | 236,712     |
| Net loss  | -                      | -         | -                                | (3,974,179 )           | -                                   | (3,974,179) |
| Balance, December 31, 2011  | 308,736,705            | 308,737   | 49,273,340                       | (46,809,858)           | -                                   | 2,772,219   |
| Issuance of common stock pursuant to exercise of stock options granted to employees for services        | 249,097                | 249       | 39,751                           | -                      | -                                   | 40,000      |
| Issuance of common stock pursuant to exercise of stock options granted to professionals and consultants | 16,365,272             | 16,365    | 2,110,466                        | -                      | -                                   | 2,126,831   |

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|   |             |           |              |                |             |             |
|---|-------------|-----------|--------------|----------------|-------------|-------------|
| Share based compensation related to issuance of incentive stock options | -           | -         | 850,459      | -              | -           | 850,459     |
| Stock subscription receivable   |             |           |              |                | (64,000 )   | (64,000 )   |
| Options exercised   | 3,522,976   | 3,523     | 102,439      | -              | -           | 105,962     |
| Net loss  | -           | -         | -            | (4,146,200 )   | -           | (4,146,200) |
| Balance, December 31, 2012  | 328,874,050 | \$328,874 | \$52,376,455 | \$(50,956,058) | \$(64,000 ) | \$1,685,271 |

See accompanying notes to financial statements

**PAID, INC.****STATEMENTS OF CASH FLOWS****FOR THE FOR THE YEARS ENDED DECEMBER 31,**

|   | 2012          | 2011          |
|---|---------------|---------------|
| Operating activities:   |               |               |
| Net loss  | \$(4,146,200) | \$(3,974,179) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities:                     |               |               |
| Depreciation and amortization   | 77,055        | 40,626        |
| Unrealized loss (gain) on investment  | 38,056        | (80,000 )     |
| Bad debts   | 5,000         | 23,300        |
| Inventory reserve   | 398,120       | 125,000       |
| Payments received in common stock   | -             | (125,000 )    |
| Payments made in common stock   | 24,167        | -             |
| Share based compensation  | 850,459       | 699,925       |
| Payment of stock option exercise received as compensation   | -             | 235,750       |
| Change in fair value of stock price guarantee   | 365,846       | 63,294        |
| Amortization of prepaid facility costs  | 238,013       | -             |
| Fair value of stock options awarded to professionals and consultants in payment of fees for services provided | 2,126,831     | 1,693,861     |
| Fair value of stock options awarded to employees in payment of compensation                                   | 40,000        | 526,575       |
| Changes in assets and liabilities:  |               |               |
| Accounts receivable   | (159,534 )    | 86,320        |
| Inventories   | 57,883        | 50,812        |
| Prepaid expense and other current assets  | 263,916       | (209,538 )    |
| Prepaid royalties   | 192,324       | 437,592       |
| Prepaid facility costs  | (239,700 )    | -             |
| Accounts payable  | 236,664       | 198,869       |
| Accrued expenses  | 257,055       | 356,694       |
| Deferred revenue  | (72,926 )     | 138,780       |
| Net cash provided by operating activities   | 553,029       | 288,681       |
| Investing activities:   |               |               |
| Property and equipment additions  | (134,596 )    | (28,510 )     |
| Financing Activities:   |               |               |
| Payments on capital lease   | (23,350 )     | (12,389 )     |
| Proceeds from the exercise of stock options   | 41,962        | 962           |
| Net cash provided by (used) in financing activities   | 18,612        | (11,427 )     |
| Net increase in cash and cash equivalents   | 437,045       | 248,744       |
| Cash and cash equivalents, beginning  | 995,989       | 747,245       |

|   |             |             |
|---|-------------|-------------|
| Cash and cash equivalents, ending                         | \$1,433,034 | \$995,989   |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>  |             |             |
| Income taxes  | \$-         | \$-         |
| Interest  | \$5,769     | \$2,747     |
| <b>SUPPLEMENTAL DISCLOSURES OF NON-CASH INFORMATION</b>   |             |             |
| Acquisition of property and equipment under capital lease | \$63,428    | \$30,421    |
| Common stock issued in payment of future facility costs   | \$-         | \$1,277,427 |

See accompanying notes to financial statements

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**PAID, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2012, 2011**

**NOTE 1. ORGANIZATION**

The Company's primary focus is to provide brand-related services to businesses, celebrity clients in the entertainment industry as well as charitable organizations. PAID's brand management, brand marketing, social media marketing, product design and merchandising, website design; development and hosting services are designed to grow each client's customer base in size, loyalty and revenue generation. We offer entertainers and business entities comprehensive web-presence and related services supporting and managing clients' official websites and fan-community services including e-commerce, VIP ticketing, live event fan experiences, user-generated content, client content publishing and distribution, fan forums, social network management, social media marketing, customer data capture, management and analysis.

**NOTE 2. MANAGEMENT'S PLANS**

The Company has continued to incur significant losses. For the years ended December 31, 2012 and 2011, the Company reported losses of \$4,146,200 and \$3,974,186, respectively. The Company has an accumulated deficit of \$50,956,058 at December 31, 2012.

Management believes that its efforts over the past year to streamline operations and keep operating expenses under control are stabilizing the Company. The Company announced a plan in February of 2013 to associate with another company in the music and entertainment space, Music City Networks (MCN). This relationship is expected to further reduce overhead expenses while providing a revenue source for the Company.

Management believes that these changes will have a positive impact on the Company for 2013 and future years. The revenues will decline as we will be paid a portion of the total revenues that the partnership generates, however, the costs will also be reduced with the goal of generating positive cash flow from the relationship. In addition, the Company continues to increase its efforts to generate income from its patents.

**NOTE 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

## **Presentation and Basis of Financial Statements**

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP").

## **Use of Estimates**

In preparing financial statements in conformity with GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the balance sheets and reported amounts of revenue and expenses during the reporting periods. Material estimates that are particularly susceptible to significant change in the near term relate to inventories, deferred tax asset valuation, assumptions used in the determination of fair value of stock options and warrants using the Black-Scholes option-pricing model, and forfeiture rates related to unvested stock options. Although these estimates are based on management's knowledge of current events and actions, they may ultimately differ from actual results.

## **Cash and Cash Equivalents**

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

## **Investments**

As of December 31, 2012, the Company's investments consisted of trading securities that were stated at fair value, with gains or losses resulting from changes in fair value recognized in earnings as other (income) expense, net. Management determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date. Marketable debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and are reported at fair value, with unrealized gains and losses recognized as earnings. Debt securities are classified as held for maturity when the Company has the positive intent and ability to hold the securities to maturity. Held to maturity securities are recorded as either short term or long term on the balance sheet based on contractual maturity dates and are stated at cost. Securities not classified as held to maturity or as trading, are classified as available-for-sale, and are carried at fair market value, with the unrealized gains and losses, net of tax, included in the determination of comprehensive income and reported in shareholders' equity.



### **Accounts Receivable**

Accounts receivable are presented net of an allowance for doubtful collections of \$53,300 at December 31, 2012, and, \$48,300 at December 31, 2011. In determining this allowance, objective evidence that a single receivable is uncollectible as well as a historical pattern of collections of accounts receivable that indicates the entire face amount of a portfolio of accounts receivable may not be collectible is considered at each balance sheet date.

### **Inventories**

Inventories consist of merchandise for sale and are stated at the lower of average cost or market determined on a first-in, first-out (FIFO) method. When a purchase contains multiple copies of the same item, they are stated at average cost.

Management periodically reviews inventories on hand to ascertain if any is slow moving or obsolete. In connection with this review, at December 31, 2012, and 2011, the Company provided for reserves totaling \$1,053,200 and \$655,000, respectively.

### **Advanced Royalties**

In accordance with GAAP, prepaid royalties, which consist of artist royalty advances are deferred when paid and expensed based on the completion of performances, shows or other activities. Certain stock advances contain guarantees related to the proceeds from the sale of the stock, and are accounted for at fair value on the date of issuance.

### **Property and Equipment**

Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of 3 to 5 years. Any leasehold improvements are depreciated at the lesser of the useful life of the asset or the lease term.

## **Intangible Assets**

Intangible assets consist of patents which are being amortized on a straight-line basis over their estimated useful life of 17 years.

## **Asset Impairment**

Long lived assets to be held and used are reviewed to determine whether any events or changes in circumstances indicate that their carrying amount not be recoverable. The Company bases its evaluation on indicators about the future economic benefits that the assets can be expected to provide including historical or future profitability measurements. Management reviews the estimated useful lives, as well as other external market conditions or factors that may be present. If such impairment indicators are present or other factors exist that indicate that the carrying amount of the asset may not be recoverable, the Company determines whether an impairment has occurred through the use of an undiscounted cash flow analysis of assets at the lowest level for which identifiable cash flows exist. If impairment is indicated, the Company recognizes a loss for the difference between the carrying amount and the estimated fair value of the asset. The fair value of the asset is measured using an estimated discounted cash flow analysis.

## **Fair Value Measurement**

Financial instruments and certain non-financial assets and liabilities are measured at their fair value as determined based on the assets highest and best use. GAAP has established a framework for measuring fair value that is based on a hierarchy which requires that the valuation technique used be based on the most objective inputs available for measuring a particular asset or liability. There are three broad levels in the fair value hierarchy which describe the degree of objectivity of the inputs used to determine fair value. The fair value hierarchy is set forth below:

Level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement. They are based on best information available in the absence of level 1 and 2 inputs.

The fair value of the Company's cash and cash equivalents, accounts receivable, investments, accounts payable, accrued expenses, and capital leases are approximately the same as their carrying amounts. In addition, the Company's derivative instruments, consisting of stock options, stock purchase warrants, and a stock price guarantee, are all valued using the Black-Scholes option pricing model.

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## **Income Taxes**

Income taxes are accounted for under the liability method. Under this method, deferred income taxes are provided for temporary differences between the financial reporting and the tax bases of assets and liabilities and are measured using enacted laws and rates that will be in effect when the differences are expected to reverse. A valuation allowance is provided when management believes it is more likely than not that some or all of the deferred tax assets will not be realized. GAAP requires that, in applying the liability method, the financial statement effects of an uncertain tax position be recognized based on the outcome that is more likely than not to occur. Under this criterion the most likely resolution of an uncertain tax position should be analyzed based on technical merits and on the outcome that would likely be sustained under examination. The Company has no uncertain tax positions as of December 31, 2012.

## **Reclassifications**

Certain amounts in the 2011 financial statements have been reclassified to conform to the 2012 presentation with no effect on previously reported net loss or accumulated deficit.

## **Revenue Recognition**

The Company generates revenue principally from sales of fan experiences, fan club membership fees, sales of its purchased inventories, and from consulting services.

Fan experience sales generally include tickets and related experiences at concerts and other events conducted by performing artists. Revenues associated with these fan experiences are generally reported gross, rather than net, and are deferred until the related event has been concluded, at which time the revenues and related direct costs are recognized.

Fan club membership fees are recognized ratably over the term of the related membership, generally one year.

For sales of merchandise owned and warehoused by the Company, the Company is responsible for conducting the sale, billing the customer, shipping the merchandise to the customer, processing customer returns and collecting accounts receivable. The Company recognizes revenue upon verification of the credit card transaction and shipment of the merchandise, discharging all obligations of the Company with respect to the transaction.

Client services revenues include web development and design, creative services, film and video services, marketing services and general business consulting services. For contracts that are of a short duration and fixed price, revenue is recognized when there are no significant obligations and upon acceptance by the customer of the completed project. Revenues on longer-term fixed price contracts are recognized using the percentage-of-completion method. Services that are preformed on a time and material basis are recognized as the related services are performed.

### **Cost of Revenues**

Cost of revenues include event tickets, ticketing and venue fees, shipping and handling fees associated with e-commerce sales, merchandise and royalties paid to clients.

### **Selling and Administration Expenses**

Selling, general, and administrative expenses include indirect client related expenses, including credit card processing fees, payroll, travel, facility costs, and other general and administrative expenses.

### **Advertising Costs**

Advertising costs, which totaled \$4,679 in 2012 and \$9,856, in 2011, are charged to expense when incurred.

### **Share-Based Compensation**

Share-based compensation cost is measured at their fair value on the grant date, and is recognized as an expense over the employee's or non-employee's requisite service period (generally the vesting period of the equity grant).

### **Segment Reporting**

The Company has determined that it has only one discreet operating segment consisting of activities and services surrounding the sale of fan experiences, fan club memberships, and merchandise associated with its relationships with



performing artists and organizations.

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## Concentrations

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents. Management believes there is very little risk of loss.

For the years ended December 31, 2012 and December 31, 2011 revenues from a limited number of clients accounted for approximately 78% and 54%, respectively, of total revenues. These revenues were generated from the sales of tour merchandise, VIP services, and merchandising and fulfillment services.

## Earnings Per Common Share

Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate to outstanding stock options and warrants. The number of common shares that would be included in the calculation of outstanding options and warrants is determined using the treasury stock method. The assumed conversion of outstanding dilutive stock options and warrants would increase the shares outstanding but would not require an adjustment of income as a result of the conversion. Stock options and warrants applicable to 18,030,582 and 17,183,284, shares at December 31, 2012, and 2011, respectively, have been excluded from the computation of diluted earnings per share because they would reduce the reported loss per share and therefore have an anti-dilutive effect.

## NOTE 4. PROPERTY AND EQUIPMENT

At December 31, property and equipment consisted of the following:

|                                 | 2012      | 2011      |
|---------------------------------|-----------|-----------|
| Computer equipment and software | \$292,900 | \$226,900 |
| Office furniture and equipment  | 151,200   | 19,200    |
| Leasehold Improvements          | 59,400    | 0         |
| Website development costs       | 314,200   | 314,200   |
|                                 | 758,300   | 560,300   |
| Accumulated depreciation        | (545,400) | (469,300) |

\$212,900 \$91,000

Depreciation expense of property and equipment for the years ended December 31, 2012, and 2011 amounted to \$76,100, and \$39,700.

**NOTE 5. INTANGIBLE ASSETS**

The Company has a patent for the real-time calculation of shipping costs for items purchased through online auctions using a zip code as a destination location indicator. It includes shipping charge calculations across multiple carriers and accounts for additional characteristics of the item being shipped, such as weight, special packaging or handling, and insurance costs.

On April 19, 2011, the Company was granted a patent for a technique for facilitating advanced, rapid, accurate estimation of shipping costs across multiple shipping carriers and shipping options between buyer and seller in an online auction.

At December 31, intangible assets consisted of the following:

|                          | 2012     | 2011     |
|--------------------------|----------|----------|
| Patents                  | \$16,000 | \$16,000 |
| Accumulated depreciation | (9,900 ) | (8,900 ) |
|                          | \$6,100  | \$7,100  |

Amortization expense of intangible assets for the years ended December 31, 2012, and 2011 was \$900.

Estimated future annual amortization expense is \$900 for each year through 2019.

#### **NOTE 6. ACCRUED EXPENSES**

At December 31, accrued expenses consist of the following:

|                                     | 2012        | 2011        |
|-------------------------------------|-------------|-------------|
| Payroll and related costs           | \$18,100    | \$41,600    |
| Professional and consulting fees    | 77,400      | 51,200      |
| Royalties                           | 858,300     | 587,300     |
| Stock payment guarantee liabilities | 443,200     | 505,900     |
| Other                               | 115,800     | 146,500     |
| Total                               | \$1,512,800 | \$1,332,500 |

#### **NOTE 7. INCOME TAXES**

There was no provision for income taxes for the years ended December 31, 2012, and 2011, due to the Company's net operating losses and its valuation reserve against deferred income taxes.

The difference between the provision for income taxes using amounts computed by applying the statutory federal income tax rate of 34% and the Company's effective tax rate is due primarily to the net operating losses incurred by the Company and the valuation reserve against the Company's deferred tax asset.

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The tax effects of significant temporary differences and carry forwards that give rise to deferred taxes are as follows:

|  | 2012         | 2011         |
|--|--------------|--------------|
| Federal net operating loss carry forward | \$13,312,000 | \$12,536,000 |
| State net operating loss carry forward   | 1,900,000    | 1,653,000    |
|  | 15,212,000   | 14,189,000   |
| Valuation allowance                      | (15,212,000) | (14,189,000) |
| Net deferred tax asset                   | \$—          | \$—          |

The valuation reserve applicable to net deferred tax assets at December 31, 2012, and 2011 is due to the likelihood that the potential future benefits from the deferred tax assets will not to be realized.

The Company has not been audited by the Internal Revenue Service ("IRS") or any states in connection with income taxes. The Company files income tax returns in the U.S. federal jurisdiction and Massachusetts. The periods from 2009-2011 remain open to examination by the IRS and state jurisdictions. The Company believes it is not subject to any tax risk beyond the preceding discussion. The Company's policy is to recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense.

At December 31, 2012, the Company has federal and state net operating loss carry forwards of approximately \$41,000,000 and \$19,900,000, respectively, available to offset future taxable income. The state carry-forwards will expire intermittently through 2015, while the federal carry forwards will expire intermittently through 2032.

**NOTE 8. RELATED PARTY TRANSACTIONS**

Steven Rotman is the father of Gregory Rotman, former President of the Company, and Richard Rotman, former Vice-President/Secretary of the Company. The Company paid rent, at approximately \$2,500 per month, as a tenant at will, to a company in which Steven Rotman is a shareholder. On June 30, 2012 the Company terminated the tenant at will agreement, and vacated the premises as part of the facility consolidation to Westborough, Massachusetts. Rent expense for the twelve months ended December 31, 2012 and 2011 was approximately \$15,000 and \$30,000 respectively.

During the second and third quarters of 2008, in connection with \$1,100,000 of short term notes payable, the Company granted warrants to funds controlled by Lewis Asset Management for 1,100,000 shares of common stock exercisable at \$.25 per share. All of these warrants expired during the second and third quarter of 2011.

**NOTE 9. ADVANCE ROYALTIES**

Advance royalties represent amounts the Company has advanced to certain clients and are recoupable against future royalties earned by the clients. Advances are issued in either cash or stock and advance amounts are calculated based on the clients' projected earning potential over a fixed period of time. Advances made by issuing stock or stock options are recorded at the fair value on the date of issue. During the second quarter of 2012 the Company issued options to purchase common stock at an exercise price of \$0.001 per share for both advance and previously earned royalties. The options were exercised immediately along with a Company guarantee that the shares acquired would sell for at least \$1,246,118 within 6 months. If the shares do not reach the required \$0.12 per share within that period, the Company has the option of issuing additional shares at their fair value at the end of the period or making a cash payment for the difference between the guaranteed sales price and the fair value of the stock at the end of the 6 month period. At December 31, 2012 the Company extended the guarantee through 2013.

**NOTE 10. FAIR VALUE DISCLOSURE**

The following table presents fair values for those assets and liabilities measured at fair value on a recurring basis and the level within the fair value hierarchy in which the measurements fall. No transfers among the levels within the fair value hierarchy occurred during the years ended December 31, 2012 or December 31, 2011.

| Fair Value |      |
|------------|------|
| Level      | 2012 |
|            | 2011 |

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|                               |   |           |           |
|-------------------------------|---|-----------|-----------|
| Investments                   | 1 | 142,800   | 205,000   |
| Royalty guarantee             | 2 | (443,200) | —         |
| Stock lease payment guarantee | 2 | —         | (505,900) |

The fair value of the Company's investments classified as trading securities is determined based on the closing market prices of the respective common stocks as of December 31, 2012.

**NOTE 11. LONG-TERM LIABILITIES**

**Capital Lease Obligations**

The Company is obligated under various capital leases for equipment, which expire at various dates through April 2015. The assets capitalized under these leases and associated accumulated depreciation at December 31, are as follows.

|                          | 2012       | 2011      |
|--------------------------|------------|-----------|
| Property and equipment   | \$ 113,400 | \$ 49,900 |
| Accumulated depreciation | (37,000 )  | (14,000)  |
|                          | \$ 76,400  | \$ 35,900 |

Amortization of capital leases is included in depreciation expense.

Minimum future lease payments under capital lease obligations as of December 31, 2012 are as follows:

|   |          |
|---|----------|
| Year Ended December 31,                     |          |
| 2013  | \$30,900 |
| 2014  | 27,100   |
| 2015  | 21,600   |
| 2016  | 4,100    |
| Total future minimum lease payments         | 83,700   |
| Less amount representing interest           | 8,800    |
| Present value of net minimum lease payments | 74,900   |
| Less current portion                        | 26,300   |
|   | \$48,600 |

## NOTE 12. COMMON STOCK

### Warrants

During the second and third quarters of 2008, in connection with \$1,100,000 of short term notes payable, the Company granted warrants to W. Austin Lewis, IV for 1,100,000 shares of common stock exercisable at \$.25 per share. All of these warrants expired during the second and third quarter of 2011.

### Share-based Incentive Plans

During the years ended December 31, 2012, and 2011, the Company had three stock option plans that include both incentive and non-qualified options to be granted to certain eligible employees, non-employee directors, or consultants of the Company.

### Share-based Incentive Plans

#### Active Plans:



**2012 Plan**

On October 15, 2012, the Company adopted the 2012 Non-Qualified Stock Option Plan (the "2012 Plan"). The purpose of the 2012 Plan, is to provide long-term incentives and rewards to those employees of the Company, and any other individuals, whether directors, consultants or advisors who are in a position to contribute to the long-term success and growth of the Company. The options granted have a 10 year contractual term and vest one hundred percent on the date of grant. There are 3,000,000 shares reserved for future issuance under this plan. Information with respect to stock options granted under this plan during the year ended December 31, 2012 is as follows:

|  | Number of shares | Weighted average<br>exercise price per<br>share |
|--|------------------|---|
| Options outstanding at December 31, 2011 | —                | \$ —  |
| Granted                                  | 7,000,000        | 0.043   |
| Exercised                                | —                | —   |
| Options outstanding at December 31, 2012 | 7,000,000        | \$ 0.043  |

**2011 Plan**

On February 1, 2011, the Company adopted the 2011 Non-Qualified Stock Option Plan (the "2011 Plan"), to replace the 2001 Plan discussed below, and has filed Registration Statements on Form S-8 to register 30,000,000 shares of its common stock. Under the 2011 Plan, employees and consultants may elect to receive their gross compensation in the form of options, exercisable at \$.001 per share, to acquire the number of shares of the Company's common stock equal to their gross compensation divided by the fair value of the stock on the date of grant. The options granted have a 10 year contractual term and vest one hundred percent on the date of grant. Information with respect to stock options granted under this plan during the year ended December 31, 2012 and 2011 is as follows:

|  | Number of<br>shares | Weighted<br>average exercise<br>price per share |
|--|---------------------|---|
| Options outstanding at December 31, 2010 | -                   | \$ 0.001  |
| Granted                                  | 11,416,839          | 0.390   |
| Exercised                                | (8,416,839 )        | 0.001   |
| Options outstanding at December 31 2011  | 3,000,000           | 0.145   |
| Granted                                  | 16,614,369          | 0.001   |
| Exercised                                | (16,614,369)        | 0.001   |
| Options outstanding at December 31, 2012 | 3,000,000           | 0.015   |

A summary of the awards under this plan during the year ended December 31, 2012 and 2011 is as follows:

|                                  | Number of<br>shares | Gross Compensation |
|----------------------------------|---------------------|--------------------|
|                                  | 2012                |                    |
| Employee payroll                 | 249,097             | \$ 40,000          |
| Consulting and professional fees | 16,365,272          | 2,126,832          |
| Total                            | 16,614,369          | \$ 2,166,832       |
|                                  | 2011                |                    |
| Employee payroll                 | 2,262,367           | \$ 522,360         |
| Consulting and professional fees | 6,154,472           | 1,440,808          |
| Total                            | 8,416,839           | \$ 1,963,168       |

At December 31, 2012 there were no shares reserved for issuance under this plan.

**2002 Plan**

The 2002 Stock Option Plan ("2002 Plan") provides for the award of qualified and non-qualified options for up to 30,000,000 shares. The options granted have a ten-year contractual term and have a vesting schedule of either immediately, two years, or four years from the date of grant. Information with respect to stock options granted under this plan during the years ended December 31, 2012, and 2011 is as follows:

|  | Number of<br>shares | Weighted<br>average exercise<br>price per share |
|--|---------------------|---|
| Options outstanding at December 31, 2010 | 15,871,952          | \$ 0.159  |
| Granted                                  | 3,000,000           | 0.145   |
| Exercised                                | (5,750,000 )        | 0.041   |
| Options outstanding at December 31, 2011 | 13,121,952          | \$ 0.104  |
| Granted                                  | 5,000,000           | 0.065   |
| Cancelled or Expired                     | (7,560,976 )        | 0.015   |
| Exercised                                | (2,560,976 )        | 0.041   |
| Options outstanding at December 31, 2012 | 8,000,000           | \$ 0.095  |

There are currently no shares reserved for issuance under this plan.

**2001 Plan**

The 2001 Non-Qualified Stock Option Plan (the "2001 Plan") expired on January 31, 2011. The Company adopted the 2001 Plan on February 1, 2001 and filed Registration Statements on Form S-8 to register 120,000,000 shares of its common stock. Under the 2001 Plan, employees and consultants could have elected to receive their gross compensation in the form of options, exercisable at \$.001 per share, to acquire the number of shares of the Company's common stock equal to their gross compensation divided by the fair value of the stock on the date of grant. Information with respect to stock options granted under this plan during the years ended December 31, 2012, and 2011 is as follows:

|  | Number of<br>shares | Weighted<br>average exercise<br>price per share |
|--|---------------------|---|
| Options outstanding at December 31, 2010 | 2,023,612           | \$ 0.001  |
| Granted                                  | 1,075,090           | 0.001   |
| Exercised                                | (2,037,370)         | 0.001   |

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|  |            |    |       |
|--|------------|----|-------|
| Options outstanding at December 31, 2011 | 1,061,332  | \$ | 0.001 |
| Cancelled                                | (68,750 )  |    | 0.001 |
| Exercised                                | (962,000 ) |    | 0.001 |
| Options outstanding at December 31, 2012 | 30,582     | \$ | 0.001 |

A summary of the awards under this plan during the year ended December 31, 2011 is as follows:

|                                  | Number of<br>shares<br>2011 | Gross<br>Compensation |
|----------------------------------|-----------------------------|-----------------------|
| Employee payroll                 | \$17,977                    | \$ 4,200              |
| Consulting and professional fees | 1,057,113                   | 253,100               |
| Total                            | \$1,075,090                 | \$ 257,300            |

There are currently no shares reserved for issuance under this plan.

***Option Repricing***

In November 2011 the Board of Directors approved a vote to reprice 5,000,000 employee stock options. The options were originally issued on January 2008, and had an original grant price \$0.415. The grant price was lowered to \$0.145, which reflects the market value of the stock as of the reprice date. The repriced options continue to vest according to the original grant date. The options granted have a six year contractual term and vest one year from the date of grant. The Company recorded an additional compensation charge of \$148,415 at December 31, 2011, using the Black-Scholes option pricing model with the following weighted average assumptions:

|                               |          |
|-------------------------------|----------|
| Expected term (plain-vanilla) | 3 years  |
| Expected volatility           | 104.12 % |
| Expected dividends            | None     |
| Risk free interest rate       | 0.01 %   |

The intrinsic value of options exercised during the year ended December 31, 2012, was \$56,854 in exchange for \$962 cash. Out of the total options exercised in 2012, 1,000,000 were exercised as additional compensation and 1,560,976 were exercised through a subscription receivable, both of which were exercised at the options grant price. The intrinsic value of options exercised during the year ended December 31, 2011, was \$1,066,963 in exchange for \$236,700 in cash.

***Fair value of issuances***

The fair value of the Company's option grants under the 2012, 2011, and 2002 Plans was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

|  | 2012     | 2011     |
|--|----------|----------|
| Expected term (based upon historical experience) | <1 week  | <1 week  |
| Expected volatility                              | 118.35 % | 103.26 % |
| Expected dividends                               | None     | None     |
| Risk free interest rate                          | 0.10 %   | 0.02 %   |

The stock volatility for each grant is determined based on a review of the experience of the weighted average of historical daily price changes of the Company's common stock over the expected option term. The expected term was determined using the simplified method for estimating expected option life, which qualify as "plain-vanilla" options; and the risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected life of the option.

The fair value of options granted under all plans in 2012 was \$532,291 which, assuming no forfeiture rate, resulted in \$532,291 in additional compensation expense being charged to operations during 2012. The Company used the Black-Scholes option pricing model with the following weighted average assumptions:

|                               |        |       |
|-------------------------------|--------|-------|
| Expected term (plain-vanilla) | 6.67   | years |
| Expected volatility           | 110.85 | %     |
| Expected dividends            | None   |       |
| Risk free interest rate       | 0.09   | %     |

All but 2,750,000 options outstanding at December 31, 2012 are fully vested and exercisable. Information pertaining to options outstanding at December 31, 2012 is as follows:

| Exercise Prices | Number of shares | Weighted Average Remaining Contractual Life | Aggregate Intrinsic Value* |
|-----------------|------------------|---|----------------------------|
| 0.001           | 30,582           | 1.87  | \$ 2,110                   |
| 0.041           | 5,000,000        | 9.61  | 145,000                    |
| 0.048           | 2,000,000        | 9.94  | 44,000                     |
| 0.065           | 5,000,000        | 9.61  | 25,000                     |
| 0.145           | 6,000,000        | 8.86  | —                          |
|                 | 18,030,582       | 9.38  | 216,110                    |

\*The intrinsic value of a stock option is the amount by which the market value of the underlying stock exceeds the exercise price of the option

Summary of all stock option plans during the years ended December 31, 2012, and 2011 is as follows:

|  | Number of<br>Shares | Weighted<br>Average Price |
|--|---------------------|---------------------------|
| Options outstanding at December 31, 2010 | 17,895,564          | \$ 0.159                  |
| Granted                                  | 20,491,929          | \$ 0.078                  |
| Cancelled                                | (5,000,000 )        | \$ 0.415                  |
| Exercised                                | (16,204,209)        | \$ 0.015                  |
| Options outstanding at December 31, 2011 | 17,183,284          | \$ 0.105                  |
| Granted                                  | 28,614,369          | \$ 0.022                  |
| Cancelled                                | (7,629,726 )        | \$ 0.109                  |
| Exercised                                | (20,137,345)        | \$ 0.006                  |
| Options outstanding at December 31, 2012 | 18,030,582          | \$ 0.083                  |

### **NOTE 13. COMMITMENTS AND CONTINGENCIES**

#### **Lease commitment**

On January 21, 2012 the Company closed its Boston office and moved to its new facility in Westborough, Massachusetts. During the second quarter, the Company completed the move of its fulfillment center located in Worcester, Massachusetts, to its new facility in Westborough, Massachusetts.

The future minimum rent under the operating lease for each of the remaining years is:

|      |           |
|------|-----------|
| 2013 | 260,700   |
| 2014 | 260,700   |
| 2015 | 260,700   |
| 2016 | 260,700   |
| 2017 | 10,900    |
|      | 1,053,700 |

Amounts are to be settled with prepaid stock issuances, future stock issuances, or cash.

#### **Prepaid facility costs**



In 2011, the Company entered into a lease for premises located at 40 Washington Street, Westborough, Massachusetts (the "Washington Street Location"). The lease is for an initial five year term, with an option to renew for one additional five year term. Monthly rent is \$13,856 for the initial five year term, plus applicable taxes and operating expenses, all of which has been paid in shares of restricted stock of the Company.

The original lease payment consisted of 6,082,985 shares of common stock, having a closing market price of \$0.21 per share, on August 22, 2011. The payment was for rent over five years, projected taxes and operating expenses, and a security deposit.

### **Stock price guarantee**

The Company has guaranteed the landlord that the shares would sell on the open market for at least \$1,386,500, given the landlord sells the shares within a period of three months after the initial six month restriction on transfer has expired. Subsequently, the Company entered into the first amendment to the lease agreement, to extend the guarantee period to December 31, 2012.

### **Legal matters**

In the normal course of business, the Company periodically becomes involved in litigation. As of December 31, 2012, in the opinion of management, the Company had no pending litigation that would have a material adverse effect on the Company's financial position, results of operations, or cash flows.

### **NOTE 14. SUBSEQUENT EVENTS**

The Company has evaluated its subsequent events through April 14, 2013, the date that the accompanying financial statements were issued. On January 31, 2013 the Company filed Form 8K where the Company entered into an Inventory Transfer, E-Commerce Servicing and VIP Services Agreement with MCN Interactive, LLC d/b/a MusicCityNetworks ("MCN"). The Agreement provides that the Company will license to MCN all rights to service its celebrity services accounts with respect to e-commerce and merchandising, and MCN will license VIP services rights to the Company. MCN is a privately held, employee-owned and operated web design and e-commerce business located in Nashville, Tennessee. MCN provides merchandise design, production and fulfillment and mobile solutions.

