NEOMEDIA TECHNOLOGIES INC
Form 10-Q
November 09, 2006

U. S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10 - Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended September 30, 2006

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 0-21743

NEOMEDIA TECHNOLOGIES, INC.
(Exact Name of Issuer as Specified In Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**36-3680347** (I.R.S. Employer Identification No.)
2201 Second Street, Suite 600, Fort Myers, Florida (Address of Principal Executive Offices)	**33901** (Zip Code)

239-337-3434 Issuer's Telephone Number (Including Area Code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x Noo

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one): Large Accelerated Filer o Accelerated Filer x Non-accelerated Filer o

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

As of October 23, 2006, there were 663,369,101 outstanding shares of the issuer's Common Stock, and 22,000 outstanding shares of the issuer’s Series C convertible preferred stock.

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PART I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NeoMedia Technologies, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(In Thousands, Except Share Data)

	September 30, 2006 (unaudited)	(Restated) December 31, 2005 *
ASSETS		
Current assets:		
Cash and cash equivalents	$ 3,133	$ 1,704
Trade accounts receivable, net of allowance for doubtful accounts of $96 and $203, respectively	6,097	130
Inventories, net of allowance for obsolete & slow-moving inventory of $0	53	2
Investment in marketable securities	255	104
Prepaid expenses and other current assets	753	121
Assets held for sale	3,451	4,058
Total current assets	13,742	6,119
Leasehold improvements & property and equipment, net	564	110
Goodwill	50,082	—
Other Intangible assets, net	21,405	3,274
Cash surrender value of life insurance policy	797	769
Loan to Mobot	—	1,500
Other long-term assets	1,232	639
Total assets	$ 87,822	$ 12,411
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 5,550	$ 1,502
Amounts payable under settlement agreements	97	97
Liabilities of discontinued business unit	676	676
Liabilities held for sale	750	669
Taxes payable	1,178	85
Accrued expenses	4,771	1,833
Deferred revenues and other	1,925	307
Notes payable	2,340	3,015
Derivative financial instruments	26,677	—
Total current liabilities	43,964	8,184
Long term debentures payable	73	—
Preferred stock, $0.01 par value, 25,000,000 shares authorized, 22,000 issued and outstanding, liquidation value of $22,000, and accreted dividends of $1,220.	2,931	—

Shareholders' equity:				
Common stock, $0.01 par value, 5,000,000,000 shares authorized, 656,853,390 and 475,387,910 shares issued and 655,211,964 and 467,601,717 outstanding, respectively		6,552		4,676
Additional paid-in capital		155,359		106,287
Deferred equity financing costs		—		(13,256)
Accumulated deficit		(119,618)		(92,524)
Accumulated other comprehensive loss		(660)		(177)
Treasury stock, at cost, 201,230 shares of common stock		(779)		(779)
Total shareholders' equity		40,854		4,227
Total liabilities and shareholders' equity	$	87,822	$	12,411

The accompanying notes are an integral part of these condensed consolidated financial statements.

* - Derived from NeoMedia's audited financial statements for the year ended December 31, 2005 and restated for reclassification of assets and liabilities held for sale related to the Micro Paint business unit.

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NeoMedia Technologies, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
and Comprehensive Income (Loss) (Unaudited)
(In Thousands, Except Share and per Share Data)

	Three Months Ended September 30 2006	2005 (Restated *)
Net sales	$ 6,249	$ 193
Cost of sales	4,112	116
Gross profit	2,137	77
Sales and marketing expenses	2,795	589
General and administrative expenses	2,659	765
Research and development costs	1,013	123
Stock based compensation expense	2,320	93
Loss from operations	(6,650)	(1,493)
Gain on extinguishment of debt	—	1
Interest income (expense), net	(112)	(77)
Write-off of deferred equity financing costs	(13,256)	—
Change in fair value from revaluation of warrants and embedded conversion features	(9,271)	—
NET LOSS FROM CONTINUING OPERATIONS	**(29,289)**	**(1,569)**
DISCONTINUED OPERATIONS (Note 4)		
Net loss from Micro Paint business to be sold	(1,620)	(381)
NET LOSS	(30,909)	(1,950)
Accretion of dividends on convertible preferred stock	(604)	—
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS	**(31,513)**	**(1,950)**
Comprehensive Loss:		
Net loss	(30,909)	(1,950)
Other comprehensive loss:		
Unrealized loss on marketable securities	(312)	(4)
Foreign currency translation adjustment	108	15
COMPREHENSIVE LOSS	**$ (31,113)**	**$ (1,939)**
Loss per share from continuing operations--basic and diluted	**$ (0.05)**	**$ (0.00)**
Loss per share from discontinued operations--basic and diluted	**$ (0.00)**	**$ (0.00)**
Net loss per share--basic and diluted	**$ (0.05)**	**$ (0.00)**
Loss per share attributable to common shareholders -- basic and diluted	**$ (0.05)**	**$ (0.00)**

Weighted average number of common shares--basic and diluted	**644,720,857**	**456,695,836**

* - Restated for reclassification of operations related to the Micro Paint business unit (Note 4).

The accompanying notes are an integral part of these condensed consolidated financial statements.

NeoMedia Technologies, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
and Comprehensive Income (Loss) (Unaudited)
(In Thousands, Except Share and per Share Data)

	Nine Months Ended September 30			
	2006		2005	
			(Restated *)	
Net sales	$	14,129	$	762
Cost of sales		8,887		440
Gross profit		5,242		322
Sales and marketing expenses		6,719		1,332
General and administrative expenses		6,752		2,143
Research and development costs		2,309		365
Stock based compensation expense		4,948		593
Loss from operations		(15,486)		(4,111)
Gain (loss) on extinguishment of debt		(1,858)		172
Interest income (expense), net		(191)		(223)
Write-off of deferred equity financing costs		(13,256)		—
Change in fair value from revaluation of warrants and embedded conversion features		6,523		—
NET LOSS FROM CONTINUING OPERATIONS		(24,268)		(4,162)
DISCONTINUED OPERATIONS (Note 4)				
Net loss from Micro Paint business to be sold		(2,826)		(1,307)
NET LOSS		(27,094)		(5,469)
Accretion of dividends on convertible preferred stock		(1,220)		—
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS		(28,314)		(5,469)
Comprehensive Loss:				
Net loss		(27,094)		(5,469)
Other comprehensive loss:				
Unrealized loss on marketable securities		(49)		(133)
Foreign currency translation adjustment		(434)		24
COMPREHENSIVE LOSS	$	(27,577)	$	(5,578)
Loss per share from continuing operations--basic and diluted	**$**	(0.04)	**$**	(0.01)
Loss per share from discontinued operations--basic and diluted	**$**	(0.00)	**$**	(0.00)
Net loss per share--basic and diluted	**$**	(0.04)	**$**	(0.01)
Loss per share attributable to common shareholders -- basic and diluted	**$**	(0.05)	**$**	(0.01)

Weighted average number of common shares--basic and diluted	**602,132,555**	**451,487,240**

* - Restated for reclassification of operations related to the Micro Paint business unit (Note 4).

The accompanying notes are an integral part of these condensed consolidated financial statements.

NeoMedia Technologies, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)
(In Thousands)

	Nine Months Ended September 30, 2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES:		(Restated*)
Net loss from continuing operations	($24,268)	($4,162)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	2,209	359
Loss on early extinguishment of debt	1,858	—
Change in fair value from revaluation of warrants and embedded conversion features	(6,523)	—
Write-off of deferred equity financing costs	13,256	—
Stock-based compensation expense	4,948	593
Interest expense allocated to debt	22	—
Increase in value of life insurance policies	(28)	(13)
Changes in operating assets and liabilities		
Trade accounts receivable, net	(918)	(28)
Inventory	55	—
Other current assets	(252)	(671)
Accounts payable, amounts due under settlement agreements, liabilities		
in excess of assets of discontinued business unit and accrued expenses	553	(283)
Deferred revenue other current liabilities	707	(118)
Net cash used in operating activities	(8,381)	(4,323)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Cash paid to acquire Mobot, Inc., Sponge Ltd., Gavitec AG, and 12Snap AG, net of cash acquired	(11,891)	—
Acquisition of property and equipment	(339)	(54)
Capitalization of software development and purchased intangible assets	(160)	(1,639)
Investment in iPoint-media	—	(500)
Advances to discontinued Micro Paint Repair subsidiary	(1,633)	(1,924)
Acquisition related costs	(164)	—
Amounts issued under notes receivable	(500)	—
Net cash used in investing activities	(14,687)	(4,117)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowing under notes payable and convertible debt instrument	5,000	9,932
Repayments on notes payable and convertible debt instrument	(2,530)	(5,811)
Net proceeds from issuance of common stock, net of issuance costs of $24 in 2006 and $105 in 2005	210	6,262
Net proceeds from issuance of Series C convertible preferred stock, net of issuance costs of $2,725 in 2006	14,066	—
Net proceeds from exercise of stock options and warrants	8,419	909

Cash commitment fee for $100 million Standby Equity Distribution Agreement		—		(1,000)
Net cash provided by financing activities		25,165		10,292
EFFECT OF EXCHANGE RATE CHANGES ON CASH FOR CONTINUING OPERATIONS		(668)		—
NET INCREASE IN CASH AND CASH EQUIVALENTS FROM CONTINUING OPERATIONS		1,429		1,852
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD		1,704		2,606
CASH AND CASH EQUIVALENTS, END OF PERIOD	**$**	**3,133**	**$**	**4,458**
SUPPLEMENTAL CASH FLOW INFORMATION:				
Interest paid during the period		48		47
Non-cash investing and financing activities:				
Unrealized gain (loss) on marketable securities		(361)		—
Prepaid acquisition costs applied to purchase price		168		—
Fair value of shares and notes receivable from Pickups Plus, Inc. acquired in exchange for Series C Convertible Preferred Stock		594		—
Carrying value of promissory note and accrued interest paid in exchange for Series C Convertible Preferred Stock		(3,208)		—
Fair value of shares issued to acquire Mobot, Inc., Sponge Ltd., Gavitec AG, 12Snap AG, and BSD Software, Inc.		46,964		—
Change in net assets resulting from acquisitions of Mobot, Inc., Sponge Ltd., Gavitec AG, 12Snap AG, and BSD Software, Inc.		62,240		—
Accretion of dividends on Series C Convertible Preferred Stock		1,824		—
Fair value of outstanding warrants reclassified to liabilities		13,884		—
Portion of change in fair value of outstanding warrants converted to liabilities recorded to paid-in capital		3,790		—
Fair value of Series C Convertible Preferred Stock (host instrument only)		4,908		—
Deferred stock-based financing costs associated with Series C Convertible Preferred Stock		3,198		—
Difference between net proceeds and recorded fair value of Series C Convertible Preferred Stock		4,041		—
Advance receivable from Mobot, Inc. forgiven upon acquisition		1,500		—
Gain (loss) on extinguishment of debt paid in common stock		—		349
Fair value of stock issued for services and deferred to future periods		—		239
Direct costs associated with Standby Equity Distribution Agreement and Equity Line of Credit		—		1,204
Fair value of warrants issued as fees related to the $100 million Standby Equity Distribution Agreement		—		12,256

The accompanying notes are an integral part of these condensed consolidated financial statements.

*2005 cash flows have been restated to remove the cash flows from the NeoMedia Micro Paint Repair business unit, which has been reclassified to discontinued operations and assets and liabilities held for sale.

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NEOMEDIA TECHNOLOGIES, INC. AND SUBSIDIARIES
UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION AND NATURE OF BUSINESS OPERATIONS

Basis of Presentation

The condensed consolidated financial statements include the financial statements of NeoMedia Technologies, Inc. and its wholly-owned subsidiaries ("NeoMedia" or the "Company"). The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete consolidated financial statements. These condensed consolidated financial statements and related notes should be read in conjunction with the Company's Form 10-KSB for the fiscal year ended December 31, 2005. In the opinion of management, these condensed consolidated financial statements reflect all adjustments which are of a normal recurring nature and which are necessary to present fairly the consolidated financial position of NeoMedia as of September 30, 2006, the results of operations for the three and nine month periods ended September 30, 2006 and 2005, and cash flows for the nine month periods ended September 30, 2006 and 2005. The results of operations for the three and nine month periods ended September 30, 2006 are not necessarily indicative of the results which may be expected for the entire fiscal year. All significant intercompany accounts and transactions have been eliminated in preparation of the condensed consolidated financial statements.

Going Concern

The accompanying condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplate continuation of the Company as a going concern. Net loss for the nine months ended September 30, 2006 was $27,094,000, which includes a gain from the change in fair value from revaluation of warrants and embedded conversion features of $6,523,000 and a charge for the write-off of the deferred equity financing costs of $13,256,000. NeoMedia also reported net losses of $9,147,000 and $7,230,000 for the years ended December 31, 2005 and 2004, respectively, and has an accumulated deficit of $119,618,000 and a working capital deficit of $30,222,000 as of September 30, 2006.

In addition, NeoMedia has material liquidity events that could adversely affect its ability to continue as a going concern, primarily:

· In the event that NeoMedia's stock price at the time the consideration shares issued in connection with the acquisitions of Mobot, Sponge, Gavitec, and 12Snap become saleable is less than the contractual price (between $0.3839 and $0.3956), NeoMedia is obligated to compensate the sellers in cash for the difference between the price at the time the shares become saleable and the relevant contractual price. Assuming a stock price at the time the shares become saleable of $0.10, which was the last sale price on October 23, 2006, NeoMedia would have a cash liability of $32.7 million relating to the guarantees.

· During the nine months ended September 30, 2006, NeoMedia made cash payments totaling $2.1 million to silent partners of 12Snap, as partial payment under silent partner agreements entered into by 12Snap prior to the acquisition of 12Snap by NeoMedia. The agreements call for additional cash payments of approximately $2.5 million on or before December 31, 2006.

If the Company's financial resources are insufficient, the Company may require additional financing in order to execute its operating plan and continue as a going concern. The Company cannot predict whether this additional financing will be in the form of equity, debt, or another form. The Company may not be able to obtain the necessary additional capital on a timely basis, on acceptable terms, or at all. In any of these events, the Company may be unable to implement its current plans for expansion, repay its debt obligations as they become due or respond to competitive pressures, any of which circumstances would have a material adverse effect on its business, prospects, financial condition and results of operations. The financial statements do not include any adjustments relating to the recoverability and reclassification of recorded asset amounts or amounts and reclassification of liabilities that might be necessary, should the Company be unable to continue as a going concern.

During August 2006, NeoMedia announced its intent to sell its Micro Paint Repair business unit. NeoMedia expects to receive cash proceeds from the sale of the division, which will be used to fund the operations and growth of the NeoMedia Mobile and NeoMedia Telecom Services businesses.

Should these financing sources fail to materialize, management would seek alternate funding sources such as the sale of common and/or preferred stock, the issuance of debt, or the sale of its marketable assets. Management’s plan is to secure adequate funding to bridge the profitability from the NeoMedia Mobile and NeoMedia Telecom Services businesses.

Nature of Business Operations

Historically, NeoMedia has been structured and evaluated by its Board of Directors and management as three distinct business units: NeoMedia Internet Switching Software (NISS), NeoMedia Micro Paint Repair (NMPR), and NeoMedia Consulting and Integration Services (NCIS).

NCIS is the original business line upon which the Company was founded. This unit resells client-server equipment and related software, and general and specialized consulting services. Because of decreased demand for systems integration products, and increased consolidation and competition in the industry in general, during 2005 resources allocated to the NCIS business unit were increasingly used in sales and business development efforts associated with the NISS business unit. During February 2006, NeoMedia’s Board of Directors elected to formally wind down the NCIS business unit. As a result, during February 2006, NeoMedia closed its Lisle, Illinois facility out of which the NCIS business unit was based. NeoMedia does, however, plan to continue servicing existing contracts and customers.

During the first quarter of 2006, following the completion of the acquisitions of 12Snap AG (“12Snap”), Sponge Ltd. (“Sponge”), Gavitec AG (“Gavitec”), Mobot, Inc. (“Mobot”), and BSD Software, Inc. (“BSD”), as well as the winding down of the NCIS business unit, NeoMedia restructured into the following three business units:

- NeoMedia Mobile (NMM) - encompassing NeoMedia’s physical-world-to-internet and mobile marketing technologies branded under Qode®, 12Snap, Sponge, Gavitec and Mobot. During the second quarter of 2006, NeoMedia rebranded its PaperClick suite of products under the brand name Qode®.

- NeoMedia Telecom Services (NTS) - encompassing the billing, clearinghouse and information management services of Triton Global Business Services, the operating subsidiary of BSD Software, which was acquired in March 2006

- NeoMedia Micro Paint Repair (NMPR) - encompassing the micro paint and auto aftermarket accessories manufactured and distributed by NeoMedia

On August 30, 2006, NeoMedia signed a non-binding letter of intent to sell its Micro Paint Repair business unit to Jose Sada, a technology partner of NeoMedia Micro Paint Repair, backed by Global Emerging Markets Group of New York City. The letter of intent calls for completion of the transaction on or before November 24, 2006.

Reclassifications

Certain amounts in the 2005 condensed consolidated financial statements have been reclassified to conform to the 2006 presentation, most notably, "License revenue" and "Resales of software and technology equipment and service fees", which were formerly reported as separate line items on NeoMedia's consolidated statement of operations, are now condensed into the category entitled, "Technology license, service & products." This is primarily due to the winding down of the former NCIS business unit and consolidation of revenues relating to the NCIS unit into the NMM unit, as well as the addition of new revenue streams from Mobot, Sponge, Gavitec, 12Snap, and BSD that fall into the same general category.

In addition, due to the pending sale of the Micro Paint Repair business unit, results of operations from this unit have been reclassified to restate into the caption "Net loss from Micro Paint business to be sold" for all periods shown, and assets and liabilities relating to this unit are combined into the captions "Assets held for sale" and "Liabilities held for sale," respectively. Additionally, the statement of cash flows for the nine months ended September 30, 2005 has been restated to exclude the cash flows of the discontinued Micro Paint Repair business unit.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As a result of the addition of the operations of Mobot, Sponge, Gavitec, 12Snap and BSD, and the issuance of the Series C convertible preferred stock and a convertible debenture during the nine months ended September 30, 2006, NeoMedia is presenting certain significant accounting policies that were not applicable as of the filing of its last annual report for the year ended December 31, 2005.

Stock-based Compensation

Beginning January 1, 2006, NeoMedia began to account for stock-based compensation in accordance with SFAS No. 123(R), *Share-Based Payment*. Under the fair value recognition provisions of this statement, share-based compensation cost is measured at the grant date based on the value of the award and is recognized as expense over the vesting period. Determining the fair value of share-based awards at the grant date requires judgment, including estimating expected dividends. In addition, judgment is also required in estimating the amount of share-based awards that are expected to be forfeited. If actual results differ significantly from these estimates, stock-based compensation expense and our results of operations could be materially impacted. Stock-based compensation expense is calculated using the Black-Scholes-Merton option pricing model on the date of grant. This option valuation model requires input of highly subjective assumptions. Because NeoMedia's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing model does not necessarily provide a reliable single measure of fair value of its employee stock options.

Fair Value of Derivatives

The Company generally does not use derivative financial instruments to hedge exposures to cash-flow risks or market-risks that may affect the fair values of its financial instruments. However, certain other financial instruments, such as warrants and embedded conversion features that are indexed to the Company's common stock, are classified as liabilities when either (a) the holder possesses rights to net-cash settlement or (b) physical or net-share settlement is not within the control of the Company. In such instances, net-cash settlement is assumed for financial accounting and reporting, even when the terms of the underlying contracts do not provide for net-cash settlement. Such financial instruments are initially recorded at fair value and subsequently adjusted to fair value through a change to earnings at the close of each reporting period.

The caption “Derivative Financial Instruments” consists of (i) the fair values associated with derivative features embedded in the Series C convertible preferred stock, (ii) the fair values of the detachable warrants that were issued in connection with the preferred stock and the convertible debenture financing arrangements, and (iii) the fair value of detachable warrants that were outstanding prior to the issuance of the preferred stock and the convertible debenture financing arrangements.

Sales Taxes Payable

Sales taxes payable represents amounts collected on behalf of specific regulatory agencies that require remittance on a specified date. These amounts are collected at the time of sales and are detailed on invoices provided to customers. At September 30, 2006 sales taxes payable were $1,178,000, of which $851,000 were delinquent sales taxes assumed by NeoMedia in connection with its acquisitions, certain of which are subject to payment plans. In compliance with the Emerging Issues Task Force consensus on issue number 06-03, NeoMedia accounts for sales taxes on a net basis.

Revenue Recognition

NeoMedia derives revenues from the following sources: (1) license revenues relating to patents and internally-developed software, (2) hardware, software, and service revenues related to mobile marketing campaign design and implementation, and (3) sale of its proprietary Micro Paint Repair solution.

(1) Technology license fees, including Intellectual Property licenses, represent revenue from the licensing of NeoMedia's proprietary software tools and applications products. NeoMedia licenses its development tools and application products pursuant to non-exclusive and non-transferable license agreements. The basis for license fee revenue recognition is substantially governed by American Institute of Certified Public Accountants ("AICPA") Statement of Position 97-2 "Software Revenue Recognition" ("SOP 97-2"), as amended, and Statement of Position 98-9, Modification of SOP 97-2, "Software Revenue Recognition, With Respect to Certain Transactions". License revenue is recognized if persuasive evidence of an agreement exists, delivery has occurred, pricing is fixed and determinable, and collectibility is probable. The Company defers revenue related to license fees for which amounts have been collected but for which revenue has not been recognized in accordance with the above, and recognizes the revenue over the appropriate period.

(2) Technology service & product revenue, which includes sales of software and technology equipment, service fee and telecom revenue attributed primarily fees for processing Canadian and U.S. terminated call records for telecommunication companies. These revenue generating items are recognized based on guidance provided in SEC Staff Accounting Bulletin ("SAB") No. 104, "Revenue Recognition in Financial Statements," as amended (SAB 104). Software and technology equipment resale revenue is recognized when persuasive evidence of an arrangement exists, the price to the customer is fixed and determinable, delivery of the service has occurred and collectibility is reasonably assured. Service revenues including maintenance fees for providing system updates for software products, user documentation and technical support are recognized over the life of the contract. Software license revenue from long-term contracts has been recognized on a percentage of completion basis, along with the associated services being provided. Telecom revenues are recognized at the time that calls are accepted by the clearing house for billing to customers. The Company's recently acquired subsidiaries BSD, Mobot and Gavitec follow this policy. The Company defers revenue related to technology service & product revenue for which amounts have been invoiced and or collected but for which the requisite service has not been provided. Revenue is then recognized over the matching service period.

(3) Technology service also includes mobile marketing services to its customers which mobile marketing projects are recognized after the completion of the project and accepted by the customer. All response and messaging based revenues are recognized at the time such responses are received and processed and the Company recognizes its premium messaging revenues on a gross basis based on guidance provided in Emerging Issues Task Force Issues No. 99-19 (EITF 99-19), "Reporting Revenue Gross as Principal or Net as an Agent," and No. 01-09 (EITF 01-09) "Accounting for Consideration Given by a Vendor to a Customer." However, pursuant to EITF 01-09, the Company offsets any consideration given to its customers against revenue. Consulting and management revenues and revenues for periodic services are recognized as services are performed. NeoMedia uses stand-alone pricing to determine an element's vendor specific objective evidence ("VSOE") in order to allocate an arrangement fee amongst various

pieces of a multi-element contract. The Company's recently acquired subsidiaries 12Snap and Sponge follow this policy. The Company defers revenue related to mobile marketing service fees for which amounts have been invoiced and/or collected but for which revenue has not been recognized. Revenue is then recognized over the matching service period.

(4) Revenue for licensing and exclusivity on NeoMedia's Micro Paint Repair systems is recognized equally over the term of the contract, which is currently one year. A portion of the initial fee paid by the customer is allocated to licensing, training costs and initial products sold with the system. Revenue is recognized upon completion of training and shipment of the products, provided there is VSOE in a multiple element arrangement. Ongoing product and service revenue is recognized as products are shipped and services performed. The Company defers revenue related to micro paint repair licensing for which amounts have been invoiced and/or collected and revenue is then recognized over the estimated contract period, which is currently one year.

In December 2003, the SEC issued SAB 104, "Revenue Recognition." SAB 104 supersedes SAB 101, "Revenue Recognition in Financial Statements." SAB 104's primary purpose is to rescind accounting guidance contained in SAB 101 related to multiple element revenue arrangements, superseded as a result of the issuance of EITF 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables." Additionally, SAB 104 rescinds the SEC's Revenue Recognition in Financial Statements Frequently Asked Questions and Answers (the "FAQ") issued with SAB 101 that had been codified in SEC Topic 13, Revenue Recognition. Selected portions of the FAQ have been incorporated into SAB 104. While the wording of SAB 104 has changed to reflect the issuance of EITF 00-21, the revenue recognition principles of SAB 101 remain largely unchanged by the issuance of SAB 104, which was effective upon issuance. The adoption of SAB 104 did not impact NeoMedia's consolidated financial statements.

3. ACQUISITIONS

During the nine months ended September 30, 2006, NeoMedia completed acquisitions of Mobot, Sponge, Gavitec, 12Snap, and BSD.

Acquisition of Mobot

On February 9, 2006, NeoMedia and Mobot signed a definitive merger agreement, subject to closing conditions, under which NeoMedia acquired all of the outstanding shares of Mobot in exchange for $3,500,000 cash and 16,931,493 shares of NeoMedia common stock (2,604,845 of which are being held in escrow for a period of one year from the closing date for the purpose of securing the indemnification obligations outlined in the purchase agreement). On February 17, 2006, NeoMedia and Mobot completed the closing requirements and the acquisition became effective. In addition to cash and stock, at closing NeoMedia forgave notes payable totaling $1,500,000 due from Mobot. This amount is considered other additional consideration in the purchase price allocation. Pursuant to the terms of the merger agreement, the number of shares of NeoMedia common stock that were issued as stock consideration was calculated using a share price of $0.3839, which was the volume-weighted average closing price of NeoMedia common stock for the ten days up to and including February 8, 2006. The merger agreement between NeoMedia and Mobot also contained a provision that, in the event that NeoMedia's stock price at the time the consideration shares become saleable is less than $0.3839, NeoMedia would be obligated to compensate Mobot shareholders in cash for the difference between the price at the time the shares become saleable and $0.3839. Assuming a stock price at the time the shares become saleable of $0.10, which was the last sale price on October 23, 2006, NeoMedia would have had a cash liability of $4.8 million resulting from this clause.

Mobot is a pioneer in visual search and recognition technology designed to make marketing effective and innovative using mobile devices. Launched in 2004 to help companies cultivate rewarding relationships with mobile phone users, Mobot gives marketers, content providers and carriers the tools to make it easy for any consumer with a camera phone to interact with their offerings. Mobot's customers include, amongst others, ELLEgirl magazine, for which Mobot "turned on" advertisements throughout the magazine that linked to content and customer loyalty promotions on the mobile Internet; The Light Agency, who distributes Mobot's visual search and recognition technology to the U.K. grocery sector through its award-winning mobile phone-based loyalty program with the Sainsburys-owned convenience store chain Jackson's; and Warner Music Group's U.S. sales and retail marketing company WEA Corp., running a snap-and-enter contest in music stores for music fans to win tailored offers, samples and discounts.

NeoMedia completed the acquisitions of Mobot, Sponge, Gavitec, and 12Snap in an effort to gain entry into the rapidly evolving global mobile marketing industry.

The actual purchase price was based on cash paid, the fair value of NeoMedia stock around the date of the Mobot acquisition, and direct costs associated with the combination. The purchase price was allocated as follows:

		(Dollars in Thousands)
Value of 16,931,493 shares issued at $0.395 per share (1)	$	6,688
Cash paid		3,500
Direct costs of acquisition		8
Advances to Mobot forgiven at acquisition		1,500
Total Fair Value of Purchase Price		11,696
Assets Purchased:		
Cash and cash equivalents	$	328
Accounts receivable		68
Other current assets		49
Property, plant & equipment		30
Intangible assets		13
Customer contracts and relationships		440
Capitalized software platform		4,200
Copyrighted materials		90
Goodwill		6,778
Total Assets Purchased		11,996
Less Liabilities Assumed:		
Accounts payable	$	51
Accrued liabilities		132
Deferred revenue		117
Total Liabilities Assumed		300

(1) - Shares were valued using the average stock price for two days before and two days after the measurement date, as defined in SFAS 141 and EITF 99-12

The combination was accounted for as a purchase business combination as defined by Statement of Financial Accounting Standards No. 141, Business Combinations. The allocation of the purchase price to the assets acquired and liabilities assumed was based on an independent valuation report obtained by the Company. The allocation is subject to change resulting from the purchase price guarantee contingency described above.

The values assigned to intangible assets, aside from goodwill, are subject to amortization. The intangible assets were assigned the following lives for amortization purposes:

Intangible asset	Estimated useful life (in years)
Customer contracts and relationships	5
Copyrighted materials	5
Capitalized software platform	7

Goodwill was not assigned a life and will be tested for impairment as defined by Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.

The accompanying consolidated statement of operations presented herein for the nine months ended September 30, 2006, contains the results of operations for Mobot for the period from February 18, 2006, through September 30, 2006. The accompanying consolidated statement of operations presented herein for the three months ended September 30, 2006, contains the results of operations for Mobot for the entire nine month period. Pro-forma results of operations for the three and nine months ended September 30, 2006 and 2005 are presented at the end of this Note 3.

Acquisition of Sponge

On February 20, 2006, NeoMedia and Sponge signed a definitive share purchase agreement, subject to closing conditions, under which NeoMedia acquired all of the outstanding shares of Sponge in exchange for $6,141,000 cash and 33,097,135 shares of NeoMedia common stock (3,400,490 of which are being held in escrow for a period of one year from the closing date for the purpose of securing the indemnification obligations outlined in the purchase agreement). The agreement also calls for Sponge to earn an additional £2,500,000 (approximately $4.4 million) in the form of NeoMedia common stock if, during the two-year period beginning at closing, the Sponge business earns in excess of £1,300,000 (approximately $2.3 million) in net profits. On February 23, 2006, NeoMedia and Sponge completed the closing requirements and the acquisition became effective. Pursuant to the terms of the merger agreement, the number of shares of NeoMedia common stock to be issued as consideration was calculated using a share price of $0.384, which was the volume-weighted average closing price of NeoMedia common stock for the ten days up to and including February 8, 2006. In the event that NeoMedia's stock price (at the time the consideration shares are saleable) is less than $0.384, NeoMedia is obligated to compensate Sponge shareholders in cash for the difference between the price at the time the shares become saleable and $0.384. Assuming a stock price at the time the shares become saleable of $0.10, which was the last sale price on October 23, 2006, NeoMedia would have a cash liability of $9.4 million resulting from this clause.

Founded in 2001, Sponge has grown to become a U.K. market leader in providing mobile applications to agencies and media groups, and gain recognition as one of Europe's top independent developers of mobile applications and content. Today, Sponge counts more than 40 agencies, including WPP, Aegis and BBH, as clients, and supplies services for over 100 world-class brands, including Coca Cola®, Heineken® and Diageo. Sponge also supplies a range of mobile services to media groups, including News International, Trinity Mirror, Endemol and IPC. For Walker's (Frito-Lay) potato chips, Sponge enabled a promotion that offered consumers of Walker's -- the U.K.'s largest snack brand -- to win an iPod every 5 minutes for 4 weeks, by texting a unique code found on-pack into the Sponge platform. More than 5% of the total U.K. population participated in the campaign, which has been expanded to Belgium and the

Netherlands on the basis of its success in the U.K. A total of 23% of the U.K. population interacted with Sponge applications in 2005.

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NeoMedia completed the acquisitions of Mobot, Sponge, Gavitec, and 12Snap in an effort to gain entry into the rapidly evolving global mobile marketing industry.

The actual purchase price was based on cash paid, the fair value of NeoMedia stock around the date of the Sponge acquisition, and direct costs associated with the combination. The purchase price has been allocated as follows:

		(Dollars in Thousands)
Value of 33,097,135 shares issued at $0.395 per share (1)	$	13,073
Cash paid		6,141
Direct costs of acquisition		194
Total Fair Value of Purchase Price		19,408
Assets Purchased:		
Cash and cash equivalents	$	177
Accounts receivable		617
Other current assets		35
Property, plant & equipment		53
Customer contracts and relationships		400
Capitalized software platform		1,300
Brand name		800
Copyrighted materials		50
Goodwill		16,692
Total Assets Purchased		20,124
Less Liabilities Assumed:		
Accounts payable	$	190
Accrued liabilities		322
Other current liabilities		204
Total Liabilities Assumed		716

(1) - Shares were valued using the average stock price for two days before and two days after the measurement date, as defined in SFAS 141 and EITF 99-12

The combination is being accounted for as a purchase business combination as defined by Statement of Financial Accounting Standards No. 141, Business Combinations. The allocation of the purchase price to the assets acquired and liabilities assumed is based on an independent valuation report obtained by the Company. The allocation is subject to change resulting from the purchase price guarantee contingency described above.

The values assigned to intangible assets, aside from goodwill, are subject to amortization. The intangible assets were assigned the following lives for amortization purposes:

Intangible asset	Estimated useful life (in years)
Customer contracts and relationships	5
Copyrighted materials	5
Capitalized software platform	7
Brand name	10

Goodwill was not assigned a life and will be tested for impairment as defined by Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.

The purchase agreement calls for the management of Sponge to earn an additional £2,500,000 (approximately $4.4 million) in the form of NeoMedia common stock if, during the two-year period beginning on February 23, 2006, the Sponge business earns in excess of £1,300,000 (approximately $2.3 million) in net profits, plus £1 of NeoMedia common stock for each £1 that earnings exceed £1,300,000 during the two-year period. No shares are to be issued pro rata if the earnings target is not met.

At the end of the two-year measurement period (February 22, 2008), if the earnings target is met, the financial impact on NeoMedia of the issuance of additional shares would be a proportionate increase of approximately $4.4 million in the long-term assets acquired from Sponge, with a corresponding increase in depreciation expense from the point of issuance forward. If the earnings target is not met, no additional shares would be issued and there would be no financial impact to NeoMedia. Pursuant to SFAS 141, NeoMedia has not allocated a value to the contingent consideration in the initial purchase price. Accordingly the final purchase price will not be determined until the conclusion of this contingency.

The accompanying consolidated statement of operations presented herein for the nine months ended September 30, 2006, contains the results of operations for Sponge for the period from February 24, 2006, through September 30, 2006. The accompanying consolidated statement of operations presented herein for the three months ended September 30, 2006, contains the results of operations for Sponge for the entire three month period. Pro-forma results of operations for the three and nine months ended September 30, 2006 and 2005 are presented at the end of this Note 3.

Acquisition of Gavitec

On February 17, 2006, NeoMedia and Gavitec signed a definitive sale and purchase agreement, subject to closing conditions, under which NeoMedia acquired all of the outstanding shares of Gavitec in exchange for $1,800,000 cash and 13,660,511 shares of NeoMedia common stock (1,366,051 of which are being held in escrow until December 31, 2006 for the purpose of securing the indemnification obligations outlined in the purchase agreement). Pursuant to the terms of the merger agreement, the number of shares of NeoMedia common stock to be issued as consideration was calculated using a share price of $0.389, which was the volume-weighted average closing price of NeoMedia common stock for the ten days up to and including February 16, 2006. On February 23, 2006, NeoMedia and Gavitec completed the closing requirements and the acquisition became effective. In the event that NeoMedia's stock price (at the time the consideration shares are saleable) is less than $0.389, NeoMedia is obligated to compensate Gavitec shareholders in cash for the difference between the price at the time the shares become saleable and $0.389. Assuming a stock price at the time the shares become saleable of $0.10, which was the last sale price on October 23, 2006, NeoMedia would have a cash liability of $3.9 million resulting from this clause.

Gavitec was founded in 1997 as a specialized provider and manufacturer of products and solutions for mobile marketing and mobile information technology. As a technology leader in code-reading systems and software for mobile applications, Gavitec offers its clients standardized or individual solutions in the areas of mobile marketing, mobile ticketing, mobile couponing, and mobile payment systems. Gavitec has run an in-market pilot program in Switzerland for its mobile macro-payment system with the leading Swiss retail bank PostFinance, Unisys, seven selected retailers including Migros, CoOp and McDonald's and approximately a thousand consumers. Participants receive a personal Data Matrix code via text message to their mobile phone. Then to complete a purchase, participants hold their cell phone over Gavitec's EXIO code reader and enter their PIN code to debit their PostFinance account. Gavitec has also run trials with "Coast Mobile" in conjunction with the British Broadcasting Corporation (BBC) and News International's The Times newspaper, along with a number of other interactive mobile campaigns.

NeoMedia completed the acquisitions of Mobot, Sponge, Gavitec, and 12Snap in an effort to gain entry into the rapidly evolving global mobile marketing industry.

The actual purchase price was based on cash paid, the fair value of NeoMedia stock around the date of the Gavitec acquisition, and direct costs associated with the combination. The purchase price has been allocated as follows:

		(Dollars in Thousands)
Value of 13,660,511 shares issued at $0.386 per share (1)	$	5,273
Cash paid		1,800
Direct costs of acquisition		114
Total Fair Value of Purchase Price		7,187
Assets Purchased:		
Cash and cash equivalents	$	74
Accounts receivable		173
Inventory		106
Other current assets		53
Property, plant & equipment		15
Intangible assets		3
Capitalized software platform		4,600
Copyrighted materials		50
Goodwill		2,611
Total Assets Purchased		7,685
Less Liabilities Assumed:		
Accounts payable	$	113
Accrued liabilities		24
Deferred revenue		117
Other current liabilities		244
Total Liabilities Assumed		498

(1) - Shares were valued using the average stock price for two days before and two days after the measurement date, as defined in SFAS 141 and EITF 99-12

The combination is being accounted for as a purchase business combination as defined by Statement of Financial Accounting Standards No. 141, Business Combinations. The allocation of the purchase price to the assets acquired and liabilities assumed is based on an independent report obtained by the Company. The allocation is subject to change resulting from the purchase price guarantee contingency described above.

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The values assigned to intangible assets, aside from goodwill, are subject to amortization. The intangible assets were assigned the following lives for amortization purposes:

Intangible asset	Estimated useful life (in years)
Copyrighted materials	5
Capitalized software platform	7
Brand name	10

Goodwill was not assigned a life and will be tested for impairment as defined by Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.

The accompanying consolidated statement of operations presented herein for the nine months ended September 30, 2006, contains the results of operations for Gavitec for the period from February 24, 2006, through September 30, 2006. The accompanying consolidated statement of operations presented herein for the three months ended September 30, 2006, contains the results of operations for Gavitec for the entire three month period. Pro-forma results of operations for the three and nine months ended September 30, 2006 and 2005 are presented at the end of this Note 3.

Acquisition of 12Snap

On February 10, 2006, NeoMedia and 12Snap signed a definitive sale and purchase agreement, subject to closing conditions, under which NeoMedia acquired all of the outstanding shares of 12Snap in exchange for $2,500,000 cash and 49,294,581 shares of NeoMedia common stock. On February 28, 2006, NeoMedia and 12Snap completed the closing requirements and the acquisition became effective. Pursuant to the terms of the merger agreement, the number of shares of NeoMedia common stock to be issued as consideration was calculated using a share price of $0.3956, which was the volume-weighted average closing price of NeoMedia common stock for the ten days up to and including February 9, 2006. In the event that NeoMedia's stock price (at the time the consideration shares are saleable) is less than $0.3956, NeoMedia is obligated to compensate 12Snap shareholders in cash for the difference between the price at the time the shares become saleable and $0.3956. Assuming a stock price at the time the shares become saleable of $0.10, which was the last sale price on October 23, 2006, NeoMedia would have a cash liability of $14.6 million resulting from this clause.

12snap AG is headquartered in Munich with branches in Düsseldorf, New York, London, Milan, Stockholm and Vienna. As an expert in innovative marketing and entertainment for mobile phones, 12snap combines know-how in mobile applications, mobile loyalty and mobile marketing. In the mobile marketing space, 12snap creates and implements national and pan-European mobile marketing campaigns for international brands; its mobile loyalty business unit offers customer loyalty programs for companies and brands, and its mobile applications business unit is the center for development and software. 12snap sells and licenses a wide spectrum of mobile solutions to satisfy the demands of the current growing market and the new uses of the third mobile phone generation from dynamic video services and multiplayer games to personalized messaging applications. 12snap has 75 employees, and services to companies including McDonald's, MTV®, Coca-Cola, Ferrero, Wella, adidas, Unilever and Gillette®.

NeoMedia completed the acquisitions of Mobot, Sponge, Gavitec, and 12Snap in an effort to gain entry into the rapidly evolving global mobile marketing industry.

The actual purchase price was based on cash paid, the fair value of NeoMedia stock around the date of the 12 Snap acquisition, and direct costs associated with the combination. The purchase price has initially allocated as follows:

		(Dollars in Thousands)
Value of 49,294,581 shares issued at $0.394 per share (1)	$	19,422
Cash paid		2,500
Direct costs of acquisition		114
Total Fair Value of Purchase Price		22,036
Assets Purchased:		
Cash and cash equivalents	$	465
Investment in marketable securities		951
Accounts receivable		2,683
Other current assets		554
Property, plant & equipment		224
Intangible assets		93
Customer contracts and relationships		400
Capitalized software platform		4,400
Brand name		1,600
Copyrighted materials		50
Goodwill		19,391
Total Assets Purchased		30,811
Less Liabilities Assumed:		
Accounts payable	$	977
Accrued liabilities		1,990
Deferred revenue		1,434
Other current liabilities		225
Notes payable		4,149
Total Liabilities Assumed		8,775

(1) - Shares were valued using the average stock price for two days before and two days after the measurement date, as defined in SFAS 141 and EITF 99-12

The combination is being accounted for as a purchase business combination as defined by Statement of Financial Accounting Standards No. 141, Business Combinations. The allocation of the purchase price to the assets acquired and liabilities assumed is based on an independent valuation report obtained by the Company. The allocation is subject to change resulting from the purchase price guarantee contingency described above.

The values assigned to intangible assets, aside from goodwill, are subject to amortization. The intangible assets were assigned the following lives for amortization purposes:

Intangible asset	Estimated useful life (in years)
Customer contracts and relationships	5
Copyrighted materials	5
Capitalized software platform	7
Brand name	10

Goodwill was not assigned a life and will be tested for impairment as defined by Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.

The accompanying consolidated statement of operations presented herein for the nine months ended September 30, 2006, contains the results of operations for 12Snap for the period from March 1, 2006, through September 30, 2006. The accompanying consolidated statement of operations presented herein for the three months ended September 30, 2006, contains the results of operations for 12Snap for the entire three month period. Pro-forma results of operations for the three and nine months ended September 30, 2006 and 2005 are presented at the end of this Note 3.

Acquisition of BSD

On March 21, 2006, NeoMedia completed its acquisition of BSD Software, Inc. of Calgary, Alberta, Canada for 7,123,698 shares of NeoMedia common stock. Pursuant to the terms of the merger agreement, the number of shares of NeoMedia common stock to be issued as consideration was calculated using a share price of $0.3467, which was the volume-weighted average closing price of NeoMedia common stock for the five days preceding March 21, 2006. BSD owns 90% of the outstanding shares of Triton Global Business Services, Inc., a provider of live and automated operator calling services and e-business support, including billing, clearinghouse and information management services, to companies in the telecommunications industry.

NeoMedia completed the acquisitions of BSD for the purpose of increasing its revenue and profit through establishment of a Telecom Services business unit, as well as gaining access to the Canadian telecom industry in order to penetrate that market with the products of the NeoMedia Mobile division.

The actual purchase price was based on cash paid, the fair value of NeoMedia stock around the date of the BSD acquisition, and direct costs associated with the combination. The purchase price has been allocated as follows:

		(Dollars in Thousands)
Value of 7,123,698 shares issued at $0.352 per share (1)	$	2,508
Direct costs of acquisition		7
Total Fair Value of Purchase Price		2,515
Assets Purchased:		
Cash and cash equivalents	$	55
Accounts receivable		1,733
Other current assets		13
Property, plant & equipment		61
Customer contracts and relationships		1,300
Copyrighted materials		130
Goodwill		4,402
Total Assets Purchased		7,694
Less Liabilities Assumed:		
Accounts payable	$	2,424
Accrued liabilities		1,224
Notes payable		1,531
Total Liabilities Assumed		5,179

(1) - Shares were valued using the average stock price for two days before and two days after the measurement date, as defined in SFAS 141 and EITF 99-12

The combination is being accounted for as a purchase business combination as defined by Statement of Financial Accounting Standards No. 141, Business Combinations. The allocation of the purchase price to the assets acquired and liabilities assumed is based on an independent valuation report obtained by the Company.

The values assigned to intangible assets, aside from goodwill, are subject to amortization. The intangible assets were assigned the following lives for amortization purposes:

Intangible asset	Estimated useful life (in years)
Customer contracts and relationships	5
Copyrighted materials	5

Goodwill was not assigned a life and will be tested for impairment as defined by Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.

The accompanying consolidated statement of operations presented herein for the nine months ended September 30, 2006, contains the results of operations for BSD for the period from March 22, 2006, through September 30, 2006. The accompanying consolidated statement of operations presented herein for the three months ended September 30, 2006, contains the results of operations for BSD for the entire three month period. Pro-forma results of operations for the three and nine months ended September 30, 2006 and 2005 are presented at the end of this Note 3.

Pro Forma Financial Information

Pro-forma results of operations as if NeoMedia was combined with Mobot, Sponge, Gavitec, 12Snap and BSD as of January 1, 2006 are as follows:

	Three Months Ended September 30, 2006							
	NeoMedia	Mobot	Sponge	Gavitec	12Snap	BSD	Pro Forma Adjust-ments	Pro-forma Combined
Total net sales	$ 6,249	$ 125	$ 265	$ 246	$ 2,226	$ 3,205	($6,067)(A)	$ 6,249
Net income (loss)	($30,909)	($388)	($420)	($359)	($166)	$ 228	$ 1,105(A)	($30,909)
Net income (loss) per share-basic and diluted	($0.05)						—	($0.05)
Weighted average common shares outstanding	644,720,857						—	644,720,857

	Nine Months Ended September 30, 2006							
	NeoMedia	Mobot	Sponge	Gavitec	12Snap	BSD	Pro Forma Adjust-ments	Pro-forma Combined
Total net sales	$ 14,129	$ 344	$ 1,488	$ 953	$ 8,457	$ 8,479	($13,876)(B)	$ 19,974
Net income (loss)	($27,094)	($1,007)	($458)	($428)	($51)	$ 474	$ 1,305(B)	($27,259)
Net income (loss) per share-basic and diluted	($0.04)						$ —(B)(C)	($0.04)
Weighted average common shares outstanding	602,132,555						58,652,190(C)	660,784,745

(A) - Adjustment to back out the operations of each subsidiary, which were included in NeoMedia's consolidated operations for the entire three month period ended September 30, 2006

(B) - Adjustments are to reflect operations of each acquisition from the closing date through September 30, 2006 and amortization of intangible assets for the period January 1, 2006 through the respective closing dates. Results of operations for each acquisition from its respective closing date through September 30, 2006 are included in NeoMedia's operations for the nine months ended September 30, 2006. Closing dates for each acquisition were: Mobot (February 17, 2006); Sponge and Gavitec (February 23, 2006); 12Snap (February 28, 2006); and BSD (March 21, 2006).

(C) - Adjustment for shares that would have been issued in connection with acquisitions if they had occurred on January 1, 2006. Using the stock price around January 1, 2006, the pro forma number of shares that would have been issued was:

	Mobot	Sponge	Gavitec	12Snap	BSD	Total
Total stock consideration	$ 6,500,000	$ 11,400,000	$ 5,400,000	$ 19,500,000	$ 2,279,263	$ 45,079,263
NeoMedia stock price around January 1, 2006 (measurement date)	$ 0.290	$ 0.290	$ 0.290	$ 0.290	$ 0.290	
Pro forma number of shares of NeoMedia to be issued as purchase price consideration	22,413,793	39,310,345	18,620,690	67,241,379	7,859,527	155,445,734

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The adjustment between the reported and the pro forma number of weighted average shares outstanding is caused by (i) the weighting of the pro forma shares for the entire nine month period ended September 30, 2006, whereas in the reported number the shares were only outstanding from the closing date through September 30, 2006, and (ii) the number of pro forma shares being higher than the actual shares issued due to a lower stock price on the pro forma date of issuance.

Pro-forma results of operations as if NeoMedia was combined with Mobot, Sponge, Gavitec, 12Snap and BSD as of January 1, 2005 are as follows:

	Three Months Ended September 30, 2005							
	NeoMedia	**Mobot**	**Sponge**	**Gavitec**	**12Snap**	**(B) BSD**	**Pro Forma Adjust-ments**	**Pro-forma Combined**
Total net sales	$ 193	$ 56	$ 609	$ 198	$ 2,114	$ 2,273	—	$ 5,443
Net income (loss)	($1,950)	($818)	$ 53	($492)	($140)	($134)	($723)(A)	($4,204)
Net income (loss) per share-basic and diluted	($0.00)						($0.01)(A)(B)	($0.01)
Weighted average common shares outstanding	456,695,836						172,717,482(B)	629,413,318

Nine Months Ended September 30, 2005