

Edgar Filing: VFINANCE INC - Form 10KSB

VFINANCE INC
Form 10KSB
March 31, 2006

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-KSB

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2005

Commission File Number 1-11454-03

VFINANCE, INC.

(Name of Small Business Issuer in Its Charter)

Delaware

58-1974423

(State or Other Jurisdiction of
Incorporation or Organization)

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

3010 North Military Trail, Suite 300
Boca Raton, FL 33431

(561) 981-1000

(Address of Principal Executive Offices)

(Issuer'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, PAR VALUE \$0.01 PER SHARE

Check whether the issuer is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act. []

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended (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] No []

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. [X]

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

The issuer's revenues for the fiscal year ended December 31, 2005 were \$25,826,250

The aggregate market value of the voting stock held by non-affiliates of the

Edgar Filing: VFINANCE INC - Form 10KSB

issuer on March 27, 2006, based upon the average bid and ask prices of such stock on that date was \$5,915,912. The number of shares of Common Stock of the issuer outstanding as of March 28, 2006 was 40,126,133.

DOCUMENTS INCORPORATED BY
REFERENCE: NONE

TABLE OF CONTENTS

| | Page No. ----- |
|---|-------------------|
| Forward-Looking Statements | 3 |
| PART I. | |
| Item 1. Description of Business | 4 |
| Item 2. Description of Property | 19 |
| Item 3. Legal Proceedings | 19 |
| Item 4. Submission of Matters to a Vote of Security Holders | 21 |
| PART II. | |
| Item 5. Market for Common Equity, Related Stockholder Matters and Small Business Issuer Purchases of Equity Securities | 22 |
| Item 6. Management's Discussion and Analysis of Financial Condition or Plan of Operations | 22 |
| Item 7. Financial Statements | 30 |
| Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure | 55 |
| Item 8A. Controls and Procedures | 55 |
| Item 8B. Other Information | 55 |
| PART III. | |
| Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(a) of the Exchange Act | 56 |
| Item 10. Executive Compensation | 58 |
| Item 11. Security Ownership of Certain Beneficial Owners and Management And Related Stockholder Matters | 60 |

Edgar Filing: VFINANCE INC - Form 10KSB

| | | |
|----------|--|----|
| Item 12. | Certain Relationships and Related Transactions | 60 |
| Item 13. | Exhibits | 61 |
| Item 14. | Principal Accountant Fees and Services | 65 |

Signatures

- 2 -

FORWARD-LOOKING STATEMENTS

The following information provides cautionary statements under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 (the Reform Act). We identify important factors that could cause our actual results to differ materially from those projected in forward-looking statements we make in this report or in other documents that reference this report. All statements that express or involve discussions as to: expectations, beliefs, plans, objectives, assumptions or future events or performance (often, but not always, identified through the use of words or phrases such as we or our management believes, expects, anticipates or hopes and words or phrases such as will result, are expected to, will continue, is anticipated, estimated, projection and outlook, and words of similar import) are not statements of historical facts and may be forward-looking. These forward-looking statements are based largely on our expectations and are subject to a number of risks and uncertainties including, but not limited to, economic, competitive, regulatory, growth strategies, available financing and other factors discussed elsewhere in this report and in the documents filed by us with the Securities and Exchange Commission ("SEC"). Many of these factors are beyond our control. Actual results could differ materially from the forward-looking statements we make in this report or in other documents that reference this report. In light of these risks and uncertainties, there can be no assurance that the results anticipated in the forward-looking information contained in this report or other documents that

Edgar Filing: VFINANCE INC - Form 10KSB

reference this report will, in fact, occur.

These forward-looking statements involve estimates, assumptions and uncertainties, and, accordingly, actual results could differ materially from those expressed in the forward-looking statements. These uncertainties include, among others, the following: (i) the inability of our broker-dealer operations to operate profitably in the face of intense competition from larger full service and discount brokers; (ii) a general decrease in merger and acquisition activities and our potential inability to receive success fees as a result of transactions not being completed; (iii) increased competition from business development portals; (iv) technological changes; (v) our potential inability to implement our growth strategy through acquisitions or joint ventures; and (vi) our potential inability to secure additional debt or equity financing.

Any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time and it is not possible for our management to predict all of such factors, nor can our management assess the impact of each such factor on the business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

- 3 -

PART I

ITEM 1. DESCRIPTION OF BUSINESS.

BUSINESS DEVELOPMENT

vFinance, Inc. is a holding company engaged in the financial services business where our strategic focus is on servicing the needs of high net-worth and institutional investors and high growth companies. Through our principal

Edgar Filing: VFINANCE INC - Form 10KSB

operating subsidiary, vFinance Investments, Inc., a licensed broker-dealer, we provide investment banking, retail and institutional brokerage services in all 50 states and the District of Columbia. The Company also operates a second broker-dealer, EquityStation, Inc. ("EquityStation") which offers institutional traders, hedge funds and professional traders a suite of services designed to enhance their trading by offering services such as trading technology, routing software, hedge fund incubation, capital introduction and custodial services. Clients, investors, shareholders and other stakeholders may access vFinance through its website at www.vfinance.com.

OUR HISTORY. We were incorporated in the state of Delaware in February 1992 under the name Peachtree Fiberoptics, Inc., primarily to engage in the production and sale of plastic optical fiber. On October 27, 1993, we ceased all operations and subsequently sold certain assets relating to our machinery and optical fiber operations.

On November 8, 1999, we acquired vFinance Holdings, Inc., a Florida corporation, and Union Atlantic LC, a Florida limited liability company, through a Share Exchange Agreement. We received all the outstanding capital stock of vFinance Holdings, Inc. and all the outstanding membership interests of Union Atlantic LC in exchange for a total of 6,955,000 shares of our common stock.

On January 4, 2001, we closed the merger of NW Holdings, Inc. ("NWH"), a Florida corporation, with and into us with us as the surviving corporation. On the closing date of the merger, NWH was the parent company of and wholly owned First Level Capital, Inc., a Florida corporation. First Level Capital, Inc. is now known as vFinance Investments, Inc. which has offices in New York, New Jersey and Florida. In addition to these offices the Company has relationships with certain independent contractors located throughout the United States.

On January 4, 2001, we also completed the merger of Colonial Direct Financial Group, Inc., a Delaware corporation, with and into Colonial Acquisition Corp., our wholly owned subsidiary, with Colonial Direct Financial Group, Inc. as the surviving corporation and as our wholly owned subsidiary. At the time of the merger, Colonial Direct Financial Group, Inc. was a holding company comprised of two diversified financial services companies, including First Colonial Securities Group, Inc. and Colonial Direct Retirement Services, Inc., and a company that provides administrative support to these financial service companies, Colonial Direct Capital Management, Inc. On June 22, 2002, the Company's Board of Directors approved a dividend to the Company's Series A Preferred shareholders of all of the common stock of Colonial. Although Colonial is no longer a subsidiary of the Company, the majority of its personnel remained employed with vFinance Investments, Inc.

On August 20, 2001, we entered into a Securities Exchange Agreement by means of which we acquired the membership interests in two related companies, Critical Investments, LLC, a Delaware limited liability company ("Critical Investments"), and Critical Advisors, L.L.C., a Virginia limited liability company ("Critical Advisors"). Critical Investments manages Critical Infrastructure Fund, L.P. ("Critical Infrastructure LP"), a Delaware limited partnership. Critical Advisors manages Critical Infrastructure Fund, Ltd. ("Critical Infrastructure Ltd."), an international business company organized and existing under the laws of the British Virgin Islands and receives (i) a management fee equal to 1% of the net asset value of Critical Infrastructure Ltd. and (ii) a performance fee equal to 20% of the increase in net asset value of Critical Infrastructure Ltd. Critical Infrastructure LP and Critical Infrastructure Ltd. are the sole general partners in, owning 96% and 4%, respectively, and conduct their investment and trading activity through Critical Infrastructure Fund (BVI), LP, a limited partnership organized and existing under the laws of the British Virgin Islands, which holds a portfolio of securities. A determination has been made to liquidate the funds.

-4-

On May 29, 2002, the Company entered into a select asset purchase agreement (the "Agreement"), as amended on June 17, 2002 (the "Amendment"), with Somerset Financial Partners, Inc., ("Somerset") a Delaware corporation to acquire certain of its assets. Through its subsidiaries, Somerset acted as a registered broker dealer and was engaged in other financial services. Pursuant to the Agreement the Company received the transfer of all agreed upon brokerage customers and client accounts as well as the registration of approximately 25 registered personnel of Somerset. As of June 17, 2002, the Company began reflecting in its financial statements the applicable revenue production and other associated costs. Under the escrow agreement signed in conjunction with the Agreement and Amendment, the Company instructed its transfer agent to deliver to and in the name of its escrow agent a total of 3,000,000 shares of the Company's common stock (the "Escrowed Shares"). The Escrowed Shares were to be delivered to Somerset when Somerset achieves all the closing conditions. In August 2002, all of the closing conditions of the Agreement and Amendment were not met by Somerset and the Company issued a default letter to Somerset (the "Default Letter"). Among other things, the Default Letter provided formal notice to Somerset of its default under the Agreement and Amendment. In October 2002, a formal termination notice was executed by the Company and Somerset and the Escrowed Shares were returned to the Company and cancelled.

The Company, as part of its strategic focus to operate its retail brokerage business using an independent contractor (IC) model, on January 1, 2003, entered into a Joint Venture Agreement with JSM Capital Holding Corp. ("JSM"), a retail brokerage IC headquartered in New York and founded by John S. Matthews (who was also, at the same time, named the President of vFinance's Retail Brokerage Division). Effective May 1, 2003, vFinance merged its "company-owned" retail branches into JSM, in exchange for a 19% equity position in JSM's common stock. Effective upon such mergers JSM became an IC of the Company. This Joint venture was terminated for cause in July 2005, and the investment in JSM was fully impaired.

On November 2, 2004, vFinance, Inc.'s wholly-owned subsidiary, vFinance Investments Holdings, Inc completed its acquisition of certain assets of Global Partners Securities, Inc. ("Global") and 100% of the issued and outstanding equity securities of EquityStation, Inc. ("EquityStation"), all of which were owned by Level2.com, Inc. ("Level2"), a subsidiary of Global.

The assets acquired from Global included certain intellectual property, customer accounts, computer equipment, and certain clearance and trading agreements relating to emerging market debt trading, wholesale market-making in selected equities for institutional clients, and direct-access equity trading. vFinance Investments Holdings assumed no liabilities in connection with the acquisition of Global's assets. Two of the principals of Global and Equity each entered into employment agreements with the Company which provided an annual base salary of \$144,000, certain incentive bonuses, and options to purchase 350,000 shares of the Company's common stock, \$0.01 par value (the "Common Stock"). The options are exercisable at \$0.19 per share, and vest ratably over a three year period.

In accordance with the terms of the acquisition agreements of Global and EquityStation, the Company delivered into escrow 8,324,690 restricted shares (the "Shares") of the Common Stock, and warrants (the "Warrants") to purchase 3,299,728 shares of the Common Stock at a price of \$0.11 per share. All of the shares of EquityStation were also delivered into escrow. Subject to (a) any indemnification claims under the acquisition agreements and (b) the financial

Edgar Filing: VFINANCE INC - Form 10KSB

performance of EquityStation and the business of Global acquired by vFinance Investments over the periods specified in the escrow agreement, a portion of the Shares and the Warrants was distributed to Global and Level2. As determined pursuant to the financial performance calculation in the escrow agreement, 2,199,425 of the Shares and 871,805 of the Warrants are subject to cancellation in accordance with the terms of the escrow agreement. This is reflected in the purchase price and the associated goodwill recorded as of December 31, 2005. When the escrow agreement is terminated, all of the shares of EquityStation will be distributed to vFinance Investments Holdings, and the holders of the Shares and Warrants will be entitled to certain piggyback registration rights. The Company also entered into a standstill agreement with each of Marcos Konig, Harry Konig and Salomon Konig, to provide restrictions on certain actions for a defined time period.

EquityStation is a broker-dealer registered with the Securities and Exchange Commission ("SEC") and is a member of the National Association of Securities Dealers (NASD). The company is a Florida corporation incorporated on July 22, 1999. EquityStation offers institutional traders, hedge funds, and professional traders a suite of services designed to advance their trading through cutting-edge trading technologies and routing software, hedge fund incubation, capital introduction and custodial services.

-5-

OUR COMPANY. We are a diversified financial services company committed to meeting the financial needs of high net-worth investors, institutions focused on portfolio growth and management strategies, and high growth emerging companies seeking capital. The Company's principal activities are provided by four business units. Retail Brokerage offers securities brokerage services including the sale of equities, mutual funds and fixed income products. Investment Banking assists emerging growth private and public companies develop sound strategic plans and access capital. Wholesale Trading operations provide wholesale market-making services for over 2500 Over-the-Counter Bulletin Board and NASDAQ Small Cap stocks to national and regional full-service broker-dealers, electronic discount brokers, and institutional investors. Institutional Services provides investment, technology and research services to institutional fund managers and other institutional investors.

In the execution of our business strategy, the Company has created a Website, www.vfinance.com, that reaches a worldwide audience of individuals looking to create wealth through equity investments in both their personal portfolios and their businesses. Our Website is a leading destination for entrepreneurs, owners of small and medium businesses looking for capital, venture capitalists and private (i.e. Angel) and institutional investors seeking equity investments in high growth companies. Each month our Website attracts an estimated 80,000 business owners from over 100 countries and communicates to approximately 60,000 high net-worth individuals and institutional investors. Our Website is typically listed by search engines as one of the top sites for relevant content. In addition, over 5,000 Websites have links to our Website including Microsoft Network, Dow Jones, THE WALL STREET JOURNAL, ENTREPRENEUR MAGAZINE, INC., Stanford University, and Yahoo!. Our business model is scalable as a) the Website provides sales leads to our Retail Brokerage, Investment Banking, and Institutional Services Divisions and b) the firm has structured its Banking and Brokerage business to take advantage of an Independent Contractor model allowing the firm to expand and contract without the costs and liabilities associated with employees and offices. Due to the Website's large, global audience of entrepreneurs and venture investors, the Website serves as a vehicle to collect,

Edgar Filing: VFINANCE INC - Form 10KSB

measure and analyze data on entrepreneurial activity. See Internet Strategy.

RECENT FINANCINGS

The Company entered into agreements with two financial institutions to increase our resources. The discussion below is qualified in its entirety by reference to the copies of the agreements attached as exhibits to this filed report.

On November 28, 2001, we entered into a Note Purchase Agreement, as amended on November 30, December 14, December 28, 2001, February 13 and March 4, 2002 (collectively, the "Agreement"), with SBI Investments (USA) Inc. ("SBI"). Under the terms of the Agreement, SBI provided a loan to us in the amount of \$975,000 in the form of a 48-month non-interest bearing, convertible note (the SBI Note). The SBI Note is convertible at SBI's option into as many as 3,421,052 shares of our common stock at \$0.285 per share. During year 2002, the SBI Note was reduced by \$225,000 as a portion of the SBI Note was converted into 789,474 shares of the Company's common stock. During February and March of 2004, \$721,500 of the SBI Note was converted into 3,344,298 shares of the Company's common stock. Of this amount, \$545,000 was converted into 2,725,000 shares of the Company's common stock at a discounted rate of \$0.20 per share under a special arrangement offered by the Company to encourage further equity participation by SBI, which resulted in a \$231,625 conversion premium expense during the first quarter of 2004. The remainder, \$176,500, was converted into 619,298 shares at the stated conversion rate of \$0.285 per share. In April of 2004, the remaining balance was converted into 100,000 shares of common stock of the Company at the original stated conversion rate of \$.285 per share. The issuance of the common stock was exempt from registration pursuant to Section 4 (2) of the Securities Act of 1933, as amended, because the common stock was acquired in a privately negotiated transaction by sophisticated investors. Accordingly, the balance due SBI at December 31, 2003 was \$750,000 and 2004 was \$0.

On January 25, 2002, the Company entered into a Credit Agreement, as amended on April 12, 2002, with UBS Americas, Inc. ("UBS"). Under the terms of the Credit Agreement, UBS provided the Company with a revolving credit facility for up to \$3,000,000 for the purpose of supporting the expansion of our brokerage business or investments in infrastructure to expand our operations and our broker-dealer operations. The loan had a term of 4 years, was required to be repaid in full by January 2005, and accrued interest at LIBOR plus a LIBOR margin of 2% if the loan was repaid within a month or 5% if it was outstanding more than a month.

-6-

The Company borrowed \$1,500,000 under the credit facility on January 28, 2002 leaving an additional \$1,500,000 available. In June 2003, Fidelity Investments, on behalf of its clearing division, National Financial Services LLC, Member NYSE/SIPC, a Fidelity Investments company ("NFS"), announced that it had acquired Correspondent Services Clearing ("CSC"), an affiliate of UBS and vFinance Investments' clearing firm at the time. The credit facility stayed with UBS subsequent to the acquisition giving rise to potential breaches under such credit facility as well as precluding the Company from drawing an additional \$1,500,000 thereunder. During March 2004, NFS agreed to directly pay down the UBS credit facility in the amount of \$1,500,000 pursuant to a guaranty Fidelity Investments made to UBS as part of their original acquisition of the CSC clearing division. As a result, the Company was relieved from \$1,500,000 in debt but no longer had the ability to obtain an additional \$1,500,000 under the

Edgar Filing: VFINANCE INC - Form 10KSB

credit facility or assert any claims against UBS or NFS regarding this transaction and credit facility. During March 2004, the Company entered into a clearing agreement with NFS. The new clearing agreement required NFS to pay to vFinance, over a five year period beginning January 2004, a monthly incentive bonus not to exceed \$25,000 per month up to \$1,500,000, based on a formula that the Company believes is very achievable. Accordingly, NFS has been paying \$25,000 per month related to this incentive calculation and such amount, \$300,000 through December 31, 2005, has been included in the attached statements of operations as "other brokerage related income". The new clearing agreement also required NFS to provide the Company with \$200,000 to assist the Company with transition costs related to the conversion from CSC to NFS. This amount was paid to vFinance in March 2004 and was included in the first quarter 2004's statements of operations as a reduction to clearing and transaction costs. In consideration for these incentives, NFS required a termination fee of \$1,700,000 should vFinance discontinue using NFS' services. This fee is reduced, pro rata, annually over the five year term of the agreement. The Company began clearing through NFS during May 2004.

OUR BUSINESS

RETAIL AND TRADING BUSINESS. The largest portion of our revenues, 89% in 2005 and 85% in 2004 was attributable to commissions generated by our brokerage and trading activities through our wholly owned broker-dealer subsidiary, vFinance Investments. vFinance Investments' Retail Brokerage and Trading Divisions buys and sells securities for its customers from other dealers on an agency basis, and charges its customers a commission for its services. Such commission revenue is derived from brokerage transactions in listed and over-the-counter securities and mutual fund securities. vFinance Investments has agreements with numerous mutual fund management companies pursuant to which it sells shares in a variety of mutual funds. Mutual fund commissions are derived from standard dealers' discounts that are a small percentage of the purchase price of the shares depending upon the terms of the dealer agreement and the size of the transaction. In addition, most funds permit vFinance Investments to receive additional periodic fees based upon the customer's investments maintained in particular funds.

INVESTMENT BANKING. A significant portion of our revenues in our last fiscal year were derived from the success fees generated by our vFinance Investments' Investment Banking Division (8% in 2005) (12% in 2004). We assist emerging growth private and public companies by (i) developing sound strategic plans, (ii) obtaining equity, mezzanine, bridge, or acquisition capital, (iii) executing strategically sound acquisitions or divestiture strategies, (iv) raising capital in the public markets, and (v) maximizing shareholder value by conducting recapitalizations or other liquidity transactions. As consideration for such services, we are paid retainers and success fees, based on the percentage of the total value of a transaction, which are contingent on the successful completion of a specified transaction. As part of our success fees, we periodically receive equity instruments and stock purchase warrants from companies for which we perform services in addition to cash paid for such services.

In the area of corporate finance, vFinance Investments has been active as underwriters or selling group members in numerous public equity transactions. Participation as a managing underwriter or in an underwriting syndicate involves both economic and regulatory risks. An underwriter may incur losses if it is unable to resell the securities it is committed to purchase. In addition, under the federal securities laws, other laws and court decisions with respect to underwriters' liabilities and limitations on the indemnification of underwriters by issuers, an underwriter is subject to substantial potential liability for misstatements or omissions of material facts in prospectuses and other communications with respect to such offerings. Acting as a managing underwriter increases these risks. Underwriting commitments constitute a charge against net

Edgar Filing: VFINANCE INC - Form 10KSB

capital and our subsidiaries' ability to make underwriting commitments may be limited by the requirement that they must at all times be in compliance with regulations regarding their net capital.

-7-

WHOLESALE TRADING BUSINESS. In support of the firm's retail brokerage, banking and institutional services businesses, we offer wholesale market-making services. vFinance Investments makes markets in over 2500 Over-the-Counter Bulletin Board, National Market System, Pink Sheet, and NASDAQ Small Cap stocks. The Company's customers are national and regional full-service broker-dealers, electronic discount brokers and institutional investors that require fast and efficient executions for each security. This expertise supports the firm's investment banking strategy of servicing high growth public companies that are looking for a financial services firm that is capable of assisting them in building broad-based market support for their securities. Market makers use the firm's capital, retail and systems resources to represent a stock and compete with other market makers. Operated primarily by electronic execution, buyers and sellers meet via computer to make bids and offers. Each market maker competes for "customer order flow" by displaying buy and sell quotations for a guaranteed number of shares in a security. Once an order is received, the market maker will immediately purchase for or sell from its own inventory, or seek the other side of the trade until it is executed, often in a matter of seconds. The market maker generates all of its revenue from the difference between the price paid when a security is bought and price received when that security is sold or the price received when the security is shorted and the price received when the short is covered.

INSTITUTIONAL SERVICES. A critical element of the Company's business strategy is to identify institutional quality investments that offer above market returns. The Institutional Services Division ("ISD") supports that mission by providing institutional investment managers, primarily hedge fund managers, a complete array of services designed to enhance portfolio performance. Hedge funds represent the fastest growing segment of the money management market and by definition are focused on achieving positive returns for their investors while controlling risk. ISD accomplishes its mission by offering fund managers access to investment opportunities and independent research products that boost return on investment. Additionally, we offer fund managers the ability to reduce their transaction costs by offering them access to our trading desk for illiquid securities and automated trading systems for their liquid transactions. ISD has a mutually beneficial relationship with the Company's Investment Banking Division ("IBD") as fund managers looking for investment opportunities fund IBD's corporate clients and having relationships with fund managers creates opportunities to increase the number and quality of IBD clients.

INTERNET STRATEGY (www.vfinance.com). The Center for Innovative Entrepreneurship, a non-profit corporation, dedicated to providing research services to promote innovative entrepreneurship has been engaged by vFinance Holdings, Inc., by means of a licensing arrangement, to operate its financial services Website or "channel" on the World Wide Web located at <http://www.vfinance.com>. With an estimated 3.4 million visitors annually, the Website reaches a global audience of entrepreneurs, CEOs, and private and institutional investors in over 150 countries. The Website provides sales leads to our investment banking, brokerage and institutional services divisions. The Website is the premier destination for search phrase "venture capital" and "raising capital". Website visitors have convenient access to a variety of financial services, proprietary business development tools, searchable databases, and daily news. The website has over 80,000 "opted in" subscribers

Edgar Filing: VFINANCE INC - Form 10KSB

that receive a daily newsletter on private funding. The Website features our database of venture capital firms and angel investors accessible with vSearch, our proprietary Web-based data mining tool that allows entrepreneurs to search potential funding sources by different criteria, including, geography, amount of funds required, industry, stage of corporate development, or keyword. Much of the information on the website is provided free of charge, however, we do charge nominal fees for the use of proprietary search engines and premium services such as our business planning services.

ADMINISTRATION, OPERATIONS, SECURITIES TRANSACTIONS PROCESSING AND CUSTOMER ACCOUNTS

Our operating subsidiaries, vFinance Investments and EquityStation, do not hold any funds or securities for customers. Instead, they use the services of clearing agents on a fully disclosed basis. These clearing agents process all securities transactions and maintain customer accounts on a fee basis. Customer accounts are protected through the SIPC for up to \$500,000, of which coverage for cash balances is limited to \$100,000. In addition, all customer accounts of vFinance Investments are fully protected by an Excess Securities Bond providing protection for the account's entire net equity (both cash and securities). The services of our subsidiaries' clearing agents include billing and credit control as well as receipt, custody and delivery of securities. The clearing agents provide the operational support necessary to process, record, and maintain securities transactions for our subsidiary's brokerage activities. They provide these services to our subsidiary's customers at a total cost which we believe is less than it would cost us to process such transactions on our own. The clearing agents also lend funds to our subsidiaries' customers through the use of margin credit. These loans are made to customers on a secured basis, with the clearing agents maintaining collateral in the form of saleable securities, cash or cash equivalents. vFinance Investments and Equity Station have agreed to indemnify the clearing brokers for losses they incur on these credit arrangements.

-8-

COMPETITION

vFinance Investments and EquityStation, our subsidiaries, encounter competition in all aspects of their business. Many of their competitors have significantly greater financial, technical, marketing and other resources. National retail firms such as Merrill Lynch Pierce Fenner & Smith Incorporated, Salomon Smith Barney, Inc. and Morgan Stanley/Dean Witter dominate the industry. Our subsidiaries also compete with numerous regional and local firms. In addition, a number of firms offer discount brokerage services to retail customers and generally effect transactions at substantially lower commission rates on an "execution only" basis, without offering other services such as investment recommendations and research. Moreover, there is substantial commission discounting by full-service broker-dealers competing for institutional and retail brokerage business. The emergence of online trading has further intensified the competition for brokerage customers. With the exception of offering certain trading platforms to institutional clients and portfolio managers, our subsidiaries do not offer online trading services to retail customers. The continued expansion of discount brokerage firms and online trading could adversely affect our retail business. Other financial institutions, notably commercial banks and savings and loan associations, offer customers some of the same services and products presently provided by securities firms. While it is not possible to predict the type and extent of competing services which banks and other institutions ultimately may offer to customers, our subsidiaries may be adversely affected to the extent those services are offered on a large-scale basis. We compete through our advertising and recruiting programs for registered representatives interested in potentially

Edgar Filing: VFINANCE INC - Form 10KSB

joining our Company.

GOVERNMENT REGULATION

REGULATION OF THE SECURITIES INDUSTRY AND BROKER-DEALERS. Our business is subject to extensive regulation applicable to the securities industry in the United States and elsewhere. As a matter of public policy, regulatory bodies in the United States and the rest of the world are charged with safeguarding the integrity of the securities and other financial markets and with protecting the interests of customers participating in those markets. In the United States, the SEC is the federal agency responsible for the administration of the federal securities laws. In general, broker-dealers are required to register with the SEC under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Under the Exchange Act, every registered broker-dealer that does business with the public is required to be a member of and is subject to the rules of the NASD. The NASD administers qualification testing for all securities principals and registered representatives for its own account and on behalf of the state securities authorities. vFinance Investments and EquityStation are broker-dealers registered with the SEC and members of the NASD.

Our broker-dealers are also subject to regulation under state law. vFinance Investments and EquityStation are currently registered as broker-dealers in all 50 states and the District of Columbia. The NASD approved the change of ownership to us of (i) Union Atlantic Capital, L.C. from Pinnacle Capital Group, L.C., (ii) First Level Capital, Inc. from NW Holdings, Inc. and (iii) First Colonial Securities Group, Inc. A recent amendment to the federal securities laws prohibits the states from imposing substantive requirements on broker-dealers that exceed those imposed under federal law. The amendment, however, does not preclude the states from imposing registration requirements on broker-dealers that operate within their jurisdiction or from sanctioning these broker-dealers who have engaged in misconduct.

The SEC, self-regulatory organizations such as the NASD and state securities commissions may conduct administrative proceedings which can result in censure, fine, the issuance of cease-and-desist orders, or the suspension or expulsion of a broker-dealer, its officers, or its employees. The SEC and self-regulatory organization rules cover many aspects of a broker-dealer's business, including capital structure and withdrawals, sales methods, trade practices among broker-dealers, use, and safekeeping of customers' funds and securities, record-keeping, the financing of customers' purchases, broker-dealer and employee registration, and the conduct of directors, officers, and employees. Additional legislation, changes in rules promulgated by the Commission and self-regulatory organizations, or changes in the interpretation or enforcement of existing laws and rules, may directly affect the mode of operation and profitability of broker-dealers.

The Uniform Net Capital Rule and NASD rules require prior notice to the SEC and the NASD for certain withdrawals of capital and also provide that the SEC may restrict for up to 20 business days any withdrawal of equity capital, or unsecured loans or advances to shareholders, employees or affiliates if the capital withdrawal, together with all other net capital withdrawals during a 30-day period, exceeds 30% of excess net capital and the SEC concludes that the capital withdrawal may be detrimental to the financial integrity of the broker-dealer.

-9-

In addition, the Uniform Net Capital Rule provides that the total outstanding principal amount of a broker-dealer's indebtedness under certain subordination agreements, the proceeds of which are included in its net capital, may not

Edgar Filing: VFINANCE INC - Form 10KSB

exceed 70% of the sum of the outstanding principal amount of all subordinated indebtedness included in net capital, par or stated value of capital stock, paid in capital in excess of par, retained earnings and other capital accounts for a period in excess of 90 days. A change in the Uniform Net Capital Rule, the imposition of new rules or any unusually large charge against net capital could limit those parts of our operations that require the intensive use of capital and also could restrict our ability to pay dividends, repay debt and repurchase shares of our outstanding stock.

As of December 31, 2005, the minimum amount of net capital required to be maintained by vFinance Investments was \$1,000,000 and the minimum amount of net capital required to be maintained by our wholly owned subsidiary, EquityStation was \$100,000. A significant operating loss or any unusually large charge against net capital could adversely affect our ability to expand or even maintain our present levels of business, which could have a material adverse affect on our business and operations. vFinance Investments and EquityStation are members of Securities Investor Protection Corporation ("SIPC") which provides, in the event of the liquidation of a broker-dealer, protection for clients' accounts up to \$500,000, subject to a limitation of \$100,000 for claims for cash balances. vFinance Investments clients' accounts are carried on the books and records of NFS and Jefferies. NFS has obtained additional insurance from a private insurer in an amount equal to \$4,500,000 for the benefit of our clients' accounts with vFinance Investments that is supplemental to SIPC protection. The client accounts for Equity Station are carried on the books and records of Merrill Lynch, Pierce, Fenner & Smith ("Merrill Lynch").

APPLICATION OF LAWS AND RULES TO INTERNET BUSINESS AND OTHER ONLINE SERVICES.

Due to the increasing popularity and use of the Internet and other online services, various regulatory authorities are considering laws and/or regulations with respect to the Internet or other online services covering issues such as user privacy, pricing, content copyrights, and quality of services. In addition, the growth and development of the market for online commerce may prompt more stringent consumer protection laws that may impose additional burdens on those companies conducting business online. When the Securities Act of 1933, as amended (the "Securities Act"), which governs the offer and sale of securities, and the Exchange Act, which governs, among other things, the operation of the securities markets and broker-dealers, were enacted, such acts did not contemplate the conduct of a securities business through the Internet and other online services. The recent increase in the number of complaints by online traders could lead to more stringent regulations of online trading firms and their practices by the SEC, NASD and other regulatory agencies.

Although the SEC, in releases and no-action letters, has provided guidance on various issues related to the offer and sale of securities and the conduct of a securities business through the Internet, the application of the laws to the conduct of a securities business through the Internet continues to evolve. Furthermore, the applicability to the Internet and other online services of existing laws in various jurisdictions governing issues such as property ownership, sales and other taxes and personal privacy is uncertain and may take years to resolve. Uncertainty regarding these issues may adversely affect the viability and profitability of our business.

As our services, through our subsidiaries, are available over the Internet in multiple jurisdictions, and as we, through our subsidiaries, have numerous clients residing in these jurisdictions, these jurisdictions may claim that our subsidiaries are required to qualify to do business as a foreign corporation in each such jurisdiction. While vFinance Investments and EquityStation are currently registered as broker-dealers in the jurisdictions described in this report, vFinance Investments, EquityStation and our non-broker dealer subsidiaries are qualified to do business as a foreign corporation in only a few jurisdictions. Failure to qualify as an out-of-state or foreign corporation in a

Edgar Filing: VFINANCE INC - Form 10KSB

jurisdiction where it is required to do so could subject us to taxes and penalties for the failure to qualify.

INTELLECTUAL PROPERTY

We own the following federally registered marks: vFinance, Inc.(R), vFinance.com, Inc.(R), AngelSearch(R).

-10-

EMPLOYEES

At December 31, 2005, we employed the following personnel:

| Position | Salaried | Contract | Total |
|--------------------|----------|----------|-------|
| Officers | 11 | 0 | 11 |
| Administration | 21 | 14 | 35 |
| Brokers | 16 | 95 | 111 |
| Traders | 19 | 2 | 21 |
| Investment Bankers | 4 | 12 | 16 |
| Web Operations | 3 | 0 | 3 |
| ----- | | | |
| Totals | 74 | 123 | 197 |
| ===== | | | |

None of our personnel is covered by a collective bargaining agreement. We consider our relationships with our employees to be good. Any future increase in the number of employees will depend upon the growth of our business. Our registered representatives are required to take examinations administered by the NASD and state authorities in order to qualify to transact business and are required to enter into agreements with us obligating them, among other things, to adhere to industry rules and regulations, our supervisory procedures and not to solicit customers in the event of termination of employment.

RESEARCH AND DEVELOPMENT AND ENVIRONMENTAL MATTERS

We did not incur any research and development expenses. We do not incur any significant costs or experience any significant effects as a result of compliance with federal, state and local environmental laws.

RISKS RELATED TO OUR COMPANY

In addition to other information in this report, the following risks should be considered in evaluating our condition and prospects. These risks may have a material effect on our operating results.

WE HAVE A LIMITED OPERATING HISTORY. AS A RESULT, IT MAY BE DIFFICULT EVALUATING OUR BUSINESS AND PROSPECTS.

We have a limited operating history. We only commenced our broker-dealer operations in the middle of 2000. In addition, we completely restructured our broker-dealer operations in 2001 through the acquisition of two firms and their merger into a single operation. We purchased our hedge fund management business in mid-2001, but we decided to liquidate such funds. Our website has been in

Edgar Filing: VFINANCE INC - Form 10KSB

existence since 1995. In 2004, we acquired a second broker-dealer, EquityStation, which has been in operation since mid 1999. Our business and prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in the early stages of development. These risks are particularly severe among companies in new and rapidly evolving markets such as online business development services and those in regulated industries such as the securities industry. It may be difficult or impossible to accurately forecast our operating results and to evaluate our business and prospects based on our historical results.

WE HAVE HAD SUBSTANTIAL LOSSES SINCE INCEPTION

Prior to 2004, the Company had sustained substantial losses in each year since its inception due to ongoing operating expenses and a lack of revenues sufficient to offset those operating expenses. We have raised capital to fund ongoing operations by private sales of our securities, some of which sales have been highly dilutive and involved considerable expense. For the year ended December 31, 2004, the Company results amounted to net income of \$2,774,435, earning a substantial profit for the first time in its history. For the year ended December 31, 2005 however, results amounted to a net loss of \$1,137,398 .

The loss generated in 2005, was largely the result of higher administrative costs related to higher payroll and rent expense as a result of investment in upgrading talent in certain senior level staff functions, the expansion of leased facilities at the corporate headquarters in Boca Raton, Florida, and the addition of an office in Mt. Laurel, New Jersey. Further, a non-cash expense to impair goodwill and the impairment of an investment in an unrelated entity in the amount of \$420,000 and \$80,000, respectively with revenues that remained relatively flat year over year. As of December 31, 2005, we had an accumulated deficit of \$21,953,206. We expect to make significant capital expenditures to enhance our products and technologies, and to expand domestic and international sales and operations. As a result, we will need to continue to generate significant additional revenue to maintain our recent profitability and generate sufficient working capital to fund our planned

-11-

spending. Even if we do maintain profitability, we may not be able to increase profitability on a quarterly or annual basis. If we do not increase our profitability, the market price for our common stock may further decline.

Obtaining future financing may be costly and could be dilutive to existing stockholders. If we are not able to obtain financing when and in the amounts needed, and on terms that are acceptable, our operations, financial condition and prospects could be materially adversely affected, and we could be forced to curtail our operations or sell part or all of our assets.

WE MAY NEED TO RAISE ADDITIONAL FUNDS. THESE FUNDS MAY NOT BE AVAILABLE WHEN WE NEED THEM.

Based on our current spending plans and our projected working capital, we believe that our cash on hand and cash generated from our operations will be sufficient to fund our operations for at least the next 12 months. However, the Company may attempt to raise additional capital to operate the business, support expansion plans, develop new or enhanced services and products, respond to competitive pressures, acquire complementary businesses or technologies or respond to unanticipated events. We can provide no assurances that additional financing will be available when needed on favorable terms, if at all. If these funds are not available when we need them, we may need to change our business

Edgar Filing: VFINANCE INC - Form 10KSB

strategy or reduce our operations or investment activities. In addition, any issuance of additional equity securities will dilute the ownership interest of our existing stockholders and the issuance of additional debt securities may increase the perceived risk of investing in us.

WE ARE SUBJECT TO VARIOUS RISKS ASSOCIATED WITH THE SECURITIES INDUSTRY.

As securities broker-dealers, we are subject to uncertainties that are common in the securities industry. These uncertainties include:

- the volatility of domestic and international financial, bond and stock markets, as demonstrated by past disruptions in the financial markets;
- extensive governmental regulation;
- litigation;
- intense competition;
- substantial fluctuations in the volume and price level of securities; and
- dependence on the solvency of various third parties.

As a result of these risks, revenues and earnings may vary significantly from quarter to quarter and from year to year. We are much smaller and have much less capital than many of our competitors in the securities industry. Accordingly, we could be impacted by these risks to a larger degree. In the event of a market downturn our revenues would likely decline and, if we were unable to reduce expenses at the same pace, our profit margins would quickly erode. Our business could be adversely affected in many other ways, including those described below.

OUR BUSINESS COULD BE ADVERSELY AFFECTED BY A BREAKDOWN IN THE FINANCIAL MARKETS

As a securities broker-dealer, our business is materially affected by conditions in the financial markets and economic conditions in general, both in the United States and elsewhere around the world. Many factors or events could lead to a breakdown in the financial markets including war, terrorism, natural catastrophes and other types of disasters. These types of events could cause people to begin to lose confidence in the financial markets and their ability to function effectively. If the financial markets are unable to effectively prepare for these types of events and ease public concern over their ability to function, our revenues may decline and our operations could be adversely affected.

WE HAVE INCURRED, AND MAY IN THE FUTURE INCUR, SIGNIFICANT LOSSES FROM TRADING AND INVESTMENT ACTIVITIES DUE TO MARKET FLUCTUATIONS AND VOLATILITY.

We generally maintain trading and investment positions in the equity markets. To the extent that we own assets, i.e.: have long positions, a downturn in those markets could result in losses from a decline in the value of such long positions. Conversely, to the extent that we have sold assets that we do not own, i.e.: have short positions in any of those markets, an upturn could expose us to potentially unlimited losses as we attempt to cover our short positions by acquiring assets in a rising market.

We may, from time to time, have a trading strategy consisting of holding a long position in one asset and a short position in another from which we expect to earn revenues based on changes in the relative value of the two assets. If, however, the relative value of the two assets changes in a direction or manner that we did not anticipate or against which we are not hedged, we might realize a loss in those paired positions. In addition, we maintain trading positions that can be adversely affected by the level of volatility in the financial markets, i.e., the degree to which trading prices fluctuate over a particular period, in a particular market, regardless of market levels.

Edgar Filing: VFINANCE INC - Form 10KSB

OUR REVENUES MAY DECLINE IN ADVERSE MARKET OR ECONOMIC CONDITIONS.

Unfavorable financial or economic conditions may reduce the number and size of the transactions in which we provide underwriting services, merger and acquisition consulting and other services. Our investment banking revenues, in the form of financial advisory and underwriting fees, are directly related to the number and size of the transactions in which we participate and would therefore be adversely affected by a sustained market downturn. Additionally, a downturn in market conditions could lead to a decline in the volume of transactions that we execute for our customers and, therefore, to a decline in the revenues we receive from commissions and spreads.

OUR RISK MANAGEMENT POLICIES AND PROCEDURES MAY LEAVE US EXPOSED TO UNIDENTIFIED RISKS OR AN UNANTICIPATED LEVEL OF RISK.

The policies and procedures we employ to identify, monitor and manage risks may not be fully effective. Some methods of risk management are based on the use of observed historical market behavior. As a result, these methods may not accurately predict future risk exposures, which could be significantly greater than the historical measures indicate. Other risk management methods depend on evaluation of information regarding markets, clients or other matters that are publicly available or otherwise accessible by us. This information may not be accurate, complete, up-to-date or properly evaluated. Management of operational, legal and regulatory risks requires, among other things, policies and procedures to properly record and verify a large number of transactions and events. We cannot assure that our policies and procedures will effectively and accurately record and verify this information.

We seek to monitor and control our risk exposure through a variety of separate but complementary financial, credit, operational and legal reporting systems. We believe that we are able to evaluate and manage the market, credit and other risks to which we are exposed. Nonetheless, our ability to manage risk exposure can never be completely or accurately predicted or fully assured. For example, unexpectedly large or rapid movements or disruptions in one or more markets or other unforeseen developments can have a material adverse effect on our results of operations and financial condition. The consequences of these developments can include losses due to adverse changes in inventory values, decreases in the liquidity of trading positions, higher volatility in earnings, increases in our credit risk to customers as well as to third parties and increases in general systemic risk.

CREDIT RISK EXPOSES US TO LOSSES CAUSED BY FINANCIAL OR OTHER PROBLEMS EXPERIENCED BY THIRD PARTIES.

We are exposed to the risk that third parties which owe us money, securities or other assets will not perform their obligations. These parties include:

- trading counterparties;
- customers;
- clearing agents;
- exchanges;
- clearing houses; and
- other financial intermediaries as well as issuers whose securities we hold.

These parties may default on their obligations owed to us due to bankruptcy, lack of liquidity, operational failure or other reasons. This risk may arise, for example, from:

- holding securities of third parties;
- executing securities trades that fail to settle at the required time due to

Edgar Filing: VFINANCE INC - Form 10KSB

- non delivery by the counterparty or systems failure by clearing agents, exchanges, clearing houses or other financial intermediaries; and
- extending credit to clients through bridge or margin loans or other arrangements.

Significant failures by third parties to perform their obligations owed to us could adversely affect our revenues and perhaps our ability to borrow in the credit markets.

WE MAY HAVE DIFFICULTY RETAINING OR RECRUITING OUR INDEPENDENT CONTRACTORS

vFinance Investments is dependent upon the independent contractor model for our retail brokerage business. As such, approximately 85% of our retail registered representatives are independent contractors. We are exposed to the risk that a large group of independent contractors leave the firm or decide to affiliate with another firm and that we are unable to recruit suitable replacements. A loss of a large group of our independent contractors could have a material adverse impact on our ability to generate revenue in the retail brokerage business.

-13-

WE MAY HAVE DIFFICULTY EFFECTIVELY MANAGING OUR GROWTH.

Over the past several years, we have experienced significant growth in our business activities through a variety of transactions. We expect our business to continue to grow through similar transactions as well as organically. Future growth through mergers, acquisitions and other such transactions involves numerous risks such as:

- difficulties and expenses incurred in connection with the subsequent assimilation of the operations and services or products of the acquired company;
- the potential loss of key employees of the acquired company; and
- the diversion of management's attention from other business concerns.

If we are unable to effectively address these risks, we may be required to restructure the acquired business or write off the value of some or all of the assets of the acquired business. Further, this type of growth requires increased investments in management personnel, financial and management systems and controls as well as facilities. We cannot assure that we will experience parallel growth in these areas. If these areas do not grow at the same time, our operating margins may decline from current levels.

Additionally, as is common in the securities industry, we will continue to be highly dependent on the effective and reliable operation of our communications and information systems. We believe that our current and anticipated future growth will require implementation of new and enhanced communications and information systems and training of our personnel to operate such systems. Any difficulty or significant delay in the implementation or operation of existing or new systems or the training of personnel could adversely affect our ability to manage our growth.

INTENSE COMPETITION FROM EXISTING AND NEW ENTITIES MAY ADVERSELY AFFECT OUR REVENUES AND PROFITABILITY.

The securities industry is rapidly evolving, intensely competitive and has few barriers to entry. We expect competition to continue to intensify in the future. Many of our competitors have significantly greater financial, technical, marketing and other resources than we do. They may also offer a wider range of services and financial products than we do and have greater name recognition and

Edgar Filing: VFINANCE INC - Form 10KSB

a larger client base. These competitors may be able to respond more quickly to new or changing opportunities, technologies and client requirements. They may also be able to undertake more extensive promotional activities, offer more attractive terms to clients, and adopt more aggressive pricing policies. We may not be able to compete effectively with current or future competitors and competitive pressures faced by us may harm our business.

THE PRECAUTIONS WE TAKE TO PREVENT AND DETECT EMPLOYEE MISCONDUCT MAY NOT BE EFFECTIVE AND WE COULD BE EXPOSED TO UNKNOWN AND UNMANAGED RISKS OR LOSSES.

We run the risk that employee misconduct could occur. Misconduct by employees could include:

- employees binding us to transactions that exceed authorized limits or present unacceptable risks to us;
- employees hiding unauthorized or unsuccessful activities from us; or
- the improper use of confidential information.

These types of misconduct could result in unknown and unmanaged risks or losses to us including regulatory sanctions and serious harm to our reputation. The precautions we take to prevent and detect these activities may not be effective. If employee misconduct does occur, our business operations could be materially adversely affected.

RISK OF LOSSES ASSOCIATED WITH SECURITIES LAWS VIOLATIONS AND LITIGATION.

Many aspects of our business involve substantial risks of liability. An underwriter is exposed to substantial liability under federal and state securities laws, other federal and state laws, and court decisions, including decisions with respect to underwriters' liability and limitations on indemnification of underwriters by issuers. For example, a firm that acts as an underwriter may be held liable for material misstatements or omissions of fact in a prospectus used in connection with the securities being offered or for statements made by its securities analysts or other personnel. In recent years, there has been an increasing incidence of litigation involving the securities industry, including class actions that seek substantial damages. Our underwriting activities will usually involve offerings of the securities of smaller companies, which often involve a higher degree of risk and are more volatile than the securities of more established companies. In comparison with more established companies, smaller companies are also more likely to be the subject of securities class actions, not to carry directors and officer's

-14-

liability insurance or policies with lower limits, and to become insolvent. Each of these factors increases the likelihood that an underwriter of smaller companies' securities will be required to contribute to an adverse judgment or settlement of a securities lawsuit.

In the normal course of business, our operating subsidiaries have been and continue to be the subject of numerous civil actions and arbitrations arising out of customer complaints relating to our activities as a broker-dealer and as a result of other business activities. In general, the cases involve various allegations that our employees had mishandled customer accounts. We believe that, based on our historical experience and the reserves established by us, the resolution of the claims presently pending will not have a material adverse effect on our financial condition. However, although we typically reserve an amount we believe will be sufficient to cover any damages assessed against us, we have in the past been assessed damages that exceeded our reserves. If we

Edgar Filing: VFINANCE INC - Form 10KSB

misjudged the amount of damages that may be assessed against us from pending or threatened claims or if we are unable to adequately estimate the amount of damages that will be assessed against us from claims that arise in the future and fail to appropriately reserve, our financial condition may be materially adversely affected.

OUR DIRECTORS AND EXECUTIVE OFFICERS CONTROL APPROXIMATELY 30% OF OUR COMMON STOCK AND MAY HAVE INTERESTS DIFFERING FROM THOSE OF OTHER STOCKHOLDERS.

At December 31, 2005, our directors and executive officers controlled approximately 30% of our outstanding common stock, directly as stockholders and indirectly through control relationships with other stockholders. There is no supermajority vote in our Certificate of Incorporation. These directors and executive officers, if acting together, would be able to significantly influence all matters requiring approval by our stockholders, including the election of directors and approval of significant corporate transactions including mergers, consolidations and the sale of substantially all of our assets. This control could have the effect of delaying or preventing a third party from acquiring or merging with us, which could hinder shareholders' ability to receive a premium for their shares.

OUR VFINANCE BRAND MAY NOT ACHIEVE THE BROAD RECOGNITION NECESSARY TO SUCCEED.

We believe that broader recognition and positive perception of the "vFinance" brand is essential to our future success. Accordingly, we intend to continue to pursue an aggressive brand enhancement strategy, which will include multimedia advertising, promotional programs and public relations activities. These initiatives will require significant expenditures. If our brand enhancement strategy is unsuccessful, these expenses may never be recovered and we may be unable to increase future revenues. Successful positioning of our brand will depend in a large part on:

- The success of our advertising and promotional efforts;
- An increase in the number of users and page views of our website; and
- The ability to continue to provide a website and services useful to our clients.

IF WE DO NOT CONTINUE TO DEVELOP AND ENHANCE OUR SERVICES IN A TIMELY MANNER, OUR BUSINESS MAY BE HARMED.

Our future success will depend on our ability to develop and enhance our services and add new services. We operate in a very competitive industry in which the ability to develop and deliver advanced services through the Internet and other channels is a key competitive factor. There are significant risks in the development of new or enhanced services, including the risks that we will be unable to:

- Effectively use new technologies;
- Adapt our services to emerging industry or regulatory standards; or
- Market new or enhanced services.

If we are unable to develop and introduce new or enhanced services quickly enough to respond to market or customer requirements or to comply with emerging industry standards, or if these services do not achieve market acceptance, our business could be seriously harmed.

Edgar Filing: VFINANCE INC - Form 10KSB

INTERNET AND INTERNAL COMPUTER SYSTEM FAILURES OR COMPROMISES OF OUR SYSTEMS OR SECURITY COULD DAMAGE OUR REPUTATION AND HARM OUR BUSINESS.

Although a significant portion of our business is conducted using traditional methods of contact and communications such as face-to-face meetings, a portion of our business is conducted through the Internet. We could experience future system failures and degradations. We cannot assure you that we will be able to prevent an extended systems failure if any of the following events occur:

- Human error;
- Subsystem, component, or software failure;
- A power or telecommunications failure;
- An earthquake, fire, or other natural disaster or other act of God;
- Hacker attacks or other intentional acts of vandalism; or
- Terrorists acts or war.

Any such systems failure that interrupts our operations could seriously harm our business. We currently have limited off-site data storage and disaster recovery systems.

The secure transmission of confidential information over public networks is a critical element of our operations. We rely on encryption and authentication technology to provide the security and authentication necessary to effect secure transmission of confidential information over the Internet. To the best of our knowledge, to date, we have not experienced any security breaches in the transmission of confidential information. Moreover, we continually evaluate advanced encryption technology to ensure the continued integrity of our systems. However, we cannot assure that advances in computer capabilities, new discoveries in the field of cryptography or other events or developments will not result in a compromise of the technology or other algorithms used by our vendors and us to protect client transaction and other data. Any compromise of our systems or security could harm our business.

THERE ARE RISKS ASSOCIATED WITH OUR STOCK TRADING ON THE NASD OTC BULLETIN BOARD RATHER THAN A NATIONAL EXCHANGE.

There are significant consequences associated with our stock trading on the NASD OTC Bulletin Board rather than a national exchange. The effects of not being able to list our securities on a national exchange include:

- Limited release of the market prices of our securities;
- Limited news coverage;
- Limited interest by investors in our securities;
- Volatility of our stock price due to low trading volume;
- Increased difficulty in selling our securities in certain states due to "blue sky" restrictions; and
- Limited ability to issue additional securities or to secure additional financing.

IF OUR COMMON STOCK IS SUBJECT TO PENNY STOCK RULES, A STOCKHOLDER MAY HAVE GREATER DIFFICULTY SELLING SHARES.

The Securities Enforcement and Penny Stock Reform Act of 1990 applies to stocks characterized as "penny stocks," and requires additional disclosure relating to the market for penny stocks in connection with trades in any stock defined as a penny stock. The Securities and Exchange Commission has adopted regulations that generally define a penny stock to be any equity security that has a market price of less than \$5.00 per share, subject to certain exceptions.

Edgar Filing: VFINANCE INC - Form 10KSB

The exceptions include exchange-listed equity securities and any equity security issued by an issuer that has:

- net tangible assets of at least \$2,000,000, if the issuer has been in continuous operation for at least three years; - net tangible assets of at least \$5,000,000, if the issuer has been in continuous operation for less than three years; or - average annual revenue of at least \$6,000,000 for the last three years.

Unless an exception is available, the regulations require the delivery, prior to any transaction involving a penny stock, of a disclosure schedule explaining the penny stock market and the associated risks.

-16-

If our financial condition does not meet the above tests, then trading in the common stock will be covered by Rules 15g-1 through 15g-6 and 15g-9 promulgated under the Securities Exchange Act. Under those rules, broker-dealers who recommend such securities to persons other than their established customers and institutional accredited investors must make a special written suitability determination for the purchaser and must have received the purchaser's written agreement to a transaction prior to sale. These regulations would likely limit the ability of broker-dealers to trade in our common stock and thus would make it more difficult for purchasers of common stock to sell their securities in the secondary market. The market liquidity for the common stock could be severely affected.

WE DEPEND ON A LIMITED NUMBER OF KEY EXECUTIVES WHO WOULD BE DIFFICULT TO REPLACE.

Our success depends significantly on the continued services of our senior management, especially Leonard J. Sokolow, our Chief Executive Officer and President. Losing Mr. Sokolow or any of our subsidiaries' other key executives, including Timothy E. Mahoney, our Chairman and Chief Operating Officer, could seriously harm our business. We cannot assure you that we will be able to retain our key executives or that we would be able to replace any of our key executives if we were to lose their services for any reason. Competition for these executives is intense. If we had to replace any of these key executives, we would not be able to replace the significant amount of knowledge that these key executives have about our operations. We do not maintain "key person" insurance policies on any of our executives.

OUR OPERATING BROKER-DEALER SUBSIDIARIES EXTEND CREDIT TO THEIR CLIENTS AND ARE SUBJECT TO RISKS AS A RESULT.

Our broker dealers, vFinance Investments and EquityStation clear all transactions for customers on a fully disclosed basis with their clearing brokers, NFS, Jefferies, and Merrill Lynch. These clearing brokers carry and clear all customer securities accounts. A limited portion of the customer securities activities for both broker dealers are transacted on a "margin" basis, pursuant to which credit is extended to customers, which (a) is secured by cash and securities in customer accounts, or (b) involve (i) "short sales" (i.e., the sale of securities not yet purchased) or (ii) the purchase and sale of commodity futures contracts, substantially all of which are transacted on a

Edgar Filing: VFINANCE INC - Form 10KSB

margin basis. These risks are increased during periods of volatile markets in which the value of the collateral held could fall below the amount borrowed by clients. If margin requirements are not sufficient to cover losses, the broker dealers may be required to sell or buy securities at prevailing market prices and incur losses to satisfy its client obligations.

WE MAY UNDERWRITE SECURITIES THROUGH VFINANCE INVESTMENTS AND ARE SUBJECT TO LOSSES RELATING TO A DECLINE IN THE MARKET VALUE OF SECURITIES THAT WE HOLD IN INVENTORY AND TO POTENTIAL LIABILITY FOR ENGAGING IN UNDERWRITING ACTIVITIES.

The underwriting activities of vFinance Investments involve the purchase, sale or short sale of securities as a principal. As an underwriter, vFinance Investments agrees to purchase securities on a "firm commitment" basis and is subject to risk that it may be unable to resell securities or be required to dispose of securities at a loss. In connection with our investment-banking activities in which vFinance Investments acts as a manager or co-manager of public offerings of securities, we expect to make increased commitments through vFinance Investments of capital to market making activities in securities of those issuers. Any additional concentration of capital in the securities of those issuers held in inventory will increase the risk of loss from possible declines in the market price of those securities. In addition, under federal securities laws, other laws and court decisions with respect to underwriters' liabilities and limitations on the indemnification of underwriters by issuers, an underwriter is subject to substantial potential liability for misstatements or omissions of material facts in prospectuses and other communications with respect to securities offerings. Our potential liability through

vFinance

Investments as an underwriter is generally not covered by insurance. Moreover, underwriting commitments constitute a charge against net capital and the ability of vFinance Investments to make underwriting commitments may be limited by the requirement that it must at all times be in compliance with the net capital rule.

-17-

OUR SUCCESS AND ABILITY TO COMPETE DEPEND TO A SIGNIFICANT DEGREE ON OUR INTELLECTUAL PROPERTY

We rely on copyright and trademark law, as well as confidentiality arrangements, to protect our intellectual property. The Company owns the following federally registered marks: vFinance, Inc.(R), vFinance.com, Inc.(R), and AngelSearch(R). We currently do not have any patents. The concepts and technologies we use may not be patentable. Our competitors or others may adopt product or service names similar to "vFinance.com," thereby impeding our ability to build brand identity and possibly leading to client confusion. Our inability to adequately protect the name "vFinance.com" would seriously harm our business. Policing unauthorized use of our intellectual property is made especially difficult by the global nature of the Internet and the inherent difficulty in controlling the ultimate destination or security of software or other data transmitted on it.

The laws of other countries may afford us little or no effective protection for our intellectual property. We cannot assure you that the steps we take will prevent misappropriation of our intellectual property or that agreements entered into for that purpose will be enforceable. In addition, litigation may be necessary in the future to:

Edgar Filing: VFINANCE INC - Form 10KSB

- Enforce our intellectual property rights;
- Determine the validity and scope of the proprietary rights of others; or
- Defend against claims of infringement or invalidity.

Such litigation, whether successful or unsuccessful, could result in substantial costs and diversions of resources, either of which could seriously harm our business.

OUR BOARD OF DIRECTORS CAN ISSUE SHARES OF "BLANK CHECK" PREFERRED STOCK WITHOUT FURTHER ACTION BY OUR STOCKHOLDERS.

Our Board of Directors has the authority, without further action by the stockholders, to issue up to 2,500,000 shares of preferred stock in one or more series and to fix the rights, preferences, privileges and restrictions in each series of the preferred stock, including:

- Dividend rights;
- Conversion rights;
- Voting rights, which may be greater or lesser than the voting rights of the common stock;
- Rights and terms of redemption;
- Liquidation preferences; and
- Sinking fund terms.

The issuance of shares of preferred stock could adversely affect the voting power of holders of our common stock and the likelihood that these holders will receive dividends and payments upon liquidation of the Company and could have the effect of delaying, deferring or preventing a change in control of the Company. We have no current plans to issue any additional preferred stock in the next twelve months. Although the issuance of preferred stock may be necessary in order to raise additional capital.

-18-

ADDITIONAL DILUTION AS A RISK TO STOCKHOLDERS.

As of December 31, 2005, the Company had 40,126,133 shares of common stock outstanding, options to purchase a total of 14,614,839 shares of common stock and warrants to purchase a total of 7,659,589 shares of common stock. We are authorized to issue up to 75,000,000 shares of common stock and are therefore able to issue additional shares without being required to obtain shareholder approval. If we issue additional shares, or if our existing shareholders exercise or convert their outstanding options or notes, our other shareholders may find their holdings drastically diluted, which if it occurs, means that they will own a smaller percentage of the Company.

ITEM 2. DESCRIPTION OF PROPERTY.

The Company leases office space in three locations. The following chart provides information related to these lease obligations:

Edgar Filing: VFINANCE INC - Form 10KSB

| Office Location | Approximate Square Footage | Lease Rental | Expiration Date |
|-------------------------------------|-------------------------------|--------------|--------------------|
| 3010 N. Military, Boca Raton, FL | 15,756 | \$ 523,164 | 2/28/2009 |
| 880 Third Ave., New York, NY | 7,855 | \$ 188,520 | 6/30/2008 |
| 131 Gaither Drive, Mount Laurel, NJ | 1,400 | \$ 19,600 | 7/31/2006 |

Our corporate headquarters are located at 3010 North Military Trail, Boca Raton, Florida 33431, where we lease 15,756 square feet. The Company terminated the original lease and entered into a new lease in January 2003, as amended on October 31, 2003 and March 26, 2004. The January 2003 lease reduced the size of the leased space to approximately 9,877 square feet. On November 12, 2004, the Company entered into a new amendment in which the Company expanded the size of its premises to include an additional 5,879 rentable square feet of space effective January 1, 2005 (the "effective date"). As of the effective date, the lease was amended such that the premises shall be deemed to contain a total of 15,756 rentable square feet. The lease expiration date was also extended to February 28, 2009.

On December 15, 2004, we entered into a new lease at 880 Third Avenue, New York, New York to replace our two previous leases in the same building which expired on December 31, 2005. We now have offices on the twelfth floor with an annual rental of \$188,520 for approximately 7,855 square feet. The lease expires on June 30, 2008.

On August 1, 2004, the Company entered into a lease in Mt. Laurel, New Jersey. The opening of this office was part of the Company's disaster recovery plan implemented in order to be able to provide our clients with uninterrupted service. The lease is for approximately 1,400 square feet with an annual rental of \$19,600 and expires on July 31, 2006.

On September 4, 2003, we entered into a lease for our Shrewsbury, New Jersey office. The lease was for approximately 1,249 square feet with an annual rental of \$27,659 and expired October 31, 2005.

We consider the facilities of our company and our subsidiaries to be reasonably insured and adequate for the foreseeable needs of our company and its subsidiaries.

ITEM 3. LEGAL PROCEEDINGS.

From time to time the Company, and/or one of its subsidiaries, is named as a party to a lawsuit that has arisen in the ordinary course of business. Although it is possible that losses exceeding amounts already recorded may be incurred upon ultimate resolution of these existing legal proceedings, we believe that such losses, if any, will not have a material adverse effect on our business, results of operations or financial position; however, unfavorable resolution of each matter individually or in the aggregate could affect the consolidated results of operations for the quarterly and annual periods in which they are resolved.

The business of vFinance Investments and EquityStation involve substantial risks of liability, including exposure to liability under federal and state securities laws in connection with the underwriting or distribution of securities and claims by dissatisfied customers for fraud, unauthorized trading, churning, mismanagement and breach of fiduciary duty. In recent years, there has been an increasing incidence of litigation involving the securities industry, including class actions that generally seek rescission and substantial damages.

Edgar Filing: VFINANCE INC - Form 10KSB

In the ordinary course of business, the Company and/or its subsidiaries may be parties to other legal proceedings and regulatory inquiries, the outcome of which, either singularly or in the aggregate, is not expected to be material. There can be no assurance however that any sanctions will not have a material adverse effect on the financial condition or results of operations of the Company and/or its subsidiaries. The following is a brief summary of certain matters pending against or involving the Company and its subsidiaries.

On August 14, 2002, Henry S. Snow and Sandra L. Snow filed a complaint against Colonial Direct and vFinance, Inc. in the Circuit Court of the 15th Judicial Circuit in Palm Beach County, Florida. The claim alleges "Breach of Contract" and "Unjust Enrichment" and seeks damages of \$250,000 plus interest and court costs. It is alleged that Colonial Direct defaulted on a Promissory Note in the principal amount of \$250,000. The Company believes their claim is without merit and is vigorously defending the action.

On October 17, 2003, we were advised by the staff of the SEC that it intended to recommend that the SEC institute enforcement proceedings against vFinance Investments and one of its former employees. The SEC claims that vFinance Investments and its former employee failed reasonably to supervise the alleged illegal trading activities over a period of approximately two months of one of our broker/dealer's former securities traders with respect to one publicly traded security that resulted in vFinance Investments earning \$11,000 in commissions related to that one security over the two month period. As of December 31, 2005, the Company has included an accrual of \$50,000 for estimated expenses. On March 17, 2005 we were advised by a member of the staff of the SEC that the SEC had accepted our offer to settle the matter. Pursuant to the terms of the settlement, vFinance Investments paid amounts aggregating to \$50,000 by March 2006.

On or about February 28, 2005, Knight Equity Markets, LP ("Knight") filed an arbitration action (NASD Case No. 05-01069) against vFinance Investments, Inc. ("vFinance"), claiming that vFinance received roughly \$6.5 million in dividends that rightfully belong to Knight. vFinance asserts that the dividends actually went to two of its clients, Pearl Securities LLC ("Pearl Securities") and Michael Balog, and that vFinance has no liability. vFinance filed third party claims against Pearl Securities and Michael Balog to bring all of the parties into the action. vFinance's motion to amend the third party claim to include these two clients is currently pending. Pearl and Balog have filed motions to dismiss vFinance's claims and the motions are scheduled for hearing on April 17, 2006. Knight is seeking approximately \$6.5 million in damages plus costs, attorney fees and punitive damages. vFinance denies any liability to Knight and intends to vigorously defend against Knight's claims.

In June 2005, The Securities and Exchange Commission advised vFinance that the Division of Enforcement staff intended to recommend that the Commission take enforcement action against vFinance, Inc for various reasons. The SEC stated that it intends to file a civil action in Federal District Court seeking: a permanent injunction in connection with offers and sales of the securities of Sedona Software Solutions and SHEP Technologies, the imposition of civil penalties, and disgorgement of approximately \$40,000 in commissions. vFinance continues to engage in settlement discussions with the staff and, so far, has been unable to reach a resolution. While vFinance Investments, Inc. will continue to present a vigorous defense, a prediction of the likely outcome cannot be made.

On or about September 27, 2005, John S. Matthews filed an arbitration action (NASD Case No. 05-014991) against vFinance, claiming that vFinance wrongfully

Edgar Filing: VFINANCE INC - Form 10KSB

terminated his independent contact with vFinance and that vFinance "stole" his clients and brokers. Mr. Matthews has obtained a temporary restraining order and an agreed upon injunction was issued by the NASD panel. Matthews and JMS Capital Holding Corp., a plaintiff in the arbitration action also request unspecified damages resulting from vFinance's alleged improper activity. The full hearing on the merits is currently scheduled for August 30 through September 1, 2006. vFinance intends to vigorously defend this matter. In addition to contesting and defending against JSM's and Mr. Matthews claims, vFinance filed a counterclaim for indemnity based upon the contractual agreement between the parties.

-20-

We are engaged in a number of other legal proceedings incidental to the conduct of our business. These claims aggregate a range of \$17,500 to \$260,000.

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

No matters were submitted to a vote of stockholders during the fourth quarter of fiscal year 2005.

-21-

PART II

ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES.

Our common stock, par value \$0.01 per share, is traded on the OTC Bulletin Board of the National Association of Securities Dealers, Inc. under the symbol "VFIN."

The following table sets forth the closing high and low price information for our common stock for the periods indicated below, as reported by the National Quotation Bureau during such periods:

| | High | Low |
|-------------|------|------|
| 2004 | | |
| 1st Quarter | 0.45 | 0.22 |
| 2nd Quarter | 0.37 | 0.31 |
| 3rd Quarter | 0.21 | 0.19 |
| 4th Quarter | 0.34 | 0.17 |
| 2005 | | |
| 1st Quarter | 0.37 | 0.23 |
| 2nd Quarter | 0.33 | 0.17 |
| 3rd Quarter | 0.22 | 0.15 |
| 4th Quarter | 0.21 | 0.15 |

The foregoing quotations supplied by the National Quotations Bureau reflect inter-dealer prices, without retail mark-up, markdown or commission and may not represent actual transactions.

We are authorized to issue 75,000,000 shares of common stock, of which 40,126,133 shares were issued and outstanding as of March 28, 2006. We are authorized to issue up to 2,500,000 shares of preferred stock, none of which are currently issued or outstanding. The number of stockholders of record for the common stock as of March 28, 2005 is 309.

Edgar Filing: VFINANCE INC - Form 10KSB

We have not paid any cash dividends since inception, and we do not anticipate paying any cash dividends in the foreseeable future.

Our transfer agent is North American Transfer Co., Freeport, New York 11520.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION OR PLAN OF OPERATIONS

CRITICAL ACCOUNTING POLICIES

Financial Reporting Release No. 60, released by the SEC, requires all companies to include a discussion of critical accounting policies or methods used in the preparation of financial statements. Note 2 to our consolidated financial statements includes a summary of the significant accounting policies and methods used in the preparation of our consolidated financial statements. The following is a brief discussion of the more significant accounting policies and methods used by us.

GENERAL. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

REVENUE RECOGNITION

The Company earns revenue (commissions) from brokerage and trading which are recognized on the day of the trade - trade date basis. The Company also earns revenue from investment banking and consulting. Monthly retainer fees for investment banking and consulting are recognized as services are provided. Investment banking success fees are generally based on a percentage of the total value of a transaction and are recognized upon successful completion.

The Company does not require collateral from its customers. Revenues are not concentrated in any particular region of the country or with any individual or group.

-22-

The Company may receive equity instruments which include stock purchase warrants and common and preferred stock from companies as part of its compensation for investment-banking services that are classified as investments in trading securities on the balance sheet, if still held at the financial reporting date. Primarily all of the equity instruments are received from small public companies. The Company recognizes revenue for such stock purchase warrants when received based on the Black Scholes valuation model. On a monthly basis the Company recognizes unrealized gains or losses in the statement of operations based on the changes in value in the stock purchase warrants as determined by the Black Scholes valuation model. Realized gains or losses are recognized in the statement of operations when the related stock purchase warrant is exercised and sold. For the years ended December 31, 2005 and 2004, the Company recognized \$487,511 and \$419,365 of revenue in connection with the receipt of equity instruments.

Occasionally, the Company receives equity instruments in private companies with no readily available market value. Equity interests and warrants for which there is not a public market, are valued based on factors such as significant equity financing by sophisticated, unrelated new investors, history of positive cash flow from operations, the market value of comparable publicly traded companies (discounted for liquidity) and other pertinent factors. Management also

Edgar Filing: VFINANCE INC - Form 10KSB

considers recent offers to purchase a portfolio company's securities and the filings of registration statements in connection with a portfolio company's initial public offering when valuing warrants.

As of December 31, 2005, certain transactions in process may result in the Company receiving equity instruments or stock purchase warrants in subsequent periods as discussed above. In such event, the Company will recognize revenue related to the receipt of such equity instruments consistent with the aforementioned policies.

In 2004, the Company sold two types of listings through its website: (i) perpetual listings to venture capital vendors, who are interested in providing services to other companies or individuals; and (ii) three-month listings to entrepreneurs who have new business ideas to sell. Revenue related to the listings were generally recognized over the terms of such listings. Website revenues are concentrated primarily in the United States but are not concentrated in any particular region of the country or with any individual or group. Fees related to such listings are included in "other" in the statements of operations for the years ended December 31, 2004. In 2005, the Company entered into a licencing agreement with the Center for Innovative Entrepreneurship ("CIE") to operate it's website. The company also entered into a Management Agreement whereby it provides certain services to CIE in exchange for a servicing fee. The servicing fee is recorded as other income in the statement of operations. Also the company entered into a services contract to purchase certain services from CIE such as economic reports; the fees for these services are included in general and administrative expenses.

CLEARING ARRANGEMENT. We do not carry accounts for customers or perform custodial functions related to customers' securities. We introduce all of their customer transactions, which are not reflected in these financial statements, to their respective clearing brokers, which maintain the customers' accounts and clear such transactions. Additionally, our clearing firms provide the clearing and depository operations for our proprietary securities transactions. These activities may expose our broker dealer to off-balance-sheet risk in the event that customers do not fulfill their obligations with the clearing broker; in this event, our broker dealers have agreed to indemnify our clearing firms.

NET CAPITAL REQUIREMENT. As of December 31, 2005, the minimum amount of net capital required to be maintained by vFinance Investments was \$1,000,000. The minimum amount of capital required to be maintained by EquityStation was \$100,000 pursuant to NASD requirements. However, EquityStation has agreed to maintain a minimum of \$250,000 in net capital pursuant to its agreement with its clearing agent, Merrill Lynch.

CUSTOMER CLAIMS. In the normal course of business, our operating subsidiaries have been and continue to be the subject of numerous civil actions and arbitrations arising out of customer complaints relating to our activities as a broker-dealer, as an employer and as a result of other business activities. In general, the cases involve various allegations that our employees had mishandled customer accounts. Based on our historical experience and consultation with counsel, we typically reserve an amount we believe will be sufficient to cover any damages assessed against us. However, we have in the past been assessed damages that exceeded our reserves. If we misjudged the amount of damages that may be assessed against us from pending or threatened claims, or if we are unable to adequately estimate the amount of damages that will be assessed against us from claims that arise in the future and reserve accordingly, our operating income would be reduced.

STOCK BASED COMPENSATION. Upon the consummation of an advisory, consulting, capital or other similar transactions the Company may distribute equity instruments or proceeds from the sale of equity instruments to its employees. These distributions are made at the Company's discretion on a case by case basis as determined by the role of the employee and the nature of the transaction. At December 31, 2005 and 2004, no amounts were owed to employees of the Company in connection with equity investments received as compensation.

FAIR VALUE. "Trading securities owned" and "Securities sold, not yet purchased" on our consolidated statements of financial condition are carried at fair value or amounts that approximate fair value, with related unrealized gains and losses recognized in our results of operations. The determination of fair value is fundamental to our financial condition and results of operations and, in certain circumstances, it requires management to make complex judgments.

Fair values are based on listed market prices, where possible. If listed market prices are not available or if the liquidation of our positions would reasonably be expected to impact market prices, fair value is determined based on other relevant factors, including dealer price quotations. Fair values for certain derivative contracts are derived from pricing models that consider current market and contractual prices for the underlying financial instruments or commodities, as well as time value and yield curve or volatility factors underlying the positions.

Pricing models and their underlying assumptions impact the amount and timing of unrealized gains and losses recognized, and the use of different pricing models or assumptions could produce different financial results. Changes in the fixed income and equity markets will impact our estimates of fair value in the future, potentially affecting principal trading revenues. The illiquid nature of certain securities or debt instruments also requires a high degree of judgment in determining fair value due to the lack of listed market prices and the potential impact of the liquidation of our position on market prices, among other factors.

YEAR ENDED DECEMBER 31, 2005 COMPARED TO THE YEAR ENDED DECEMBER 31, 2004

STATEMENTS OF OPERATIONS

Business Environment

The securities industry is highly competitive and sensitive to many factors and is directly affected by general economic and market conditions, including the volatility and price level of securities markets; the trading volume, size, and timing of securities transactions; the demand for investment banking services and changes in interest rates. All such conditions have an impact on commissions, trading and investment income as well as on liquidity. In addition, a significant portion of the Company's expenses are relatively fixed and do not vary with market activity. Consequently, substantial fluctuations can occur in the Company's revenues and net income from period to period due to these and other factors.

In addition, the Company continues to face increasing competition from commercial banks and other large financial services firms as they begin to offer more investment banking and financial services traditionally provided by securities firms. The effect of the consolidation of the securities industry of recent years means that a variety of financial services companies have merged to offer a broader spectrum of investment products and such competitors have substantially greater financial resources than the Company. The Company is incurring additional expenses to comply with increased regulation from the the

Edgar Filing: VFINANCE INC - Form 10KSB

securities industry, particularly in the over-the-counter markets. At present, the Company is unable to predict the extent of the changes, or their potential effect on the Company's business.

Outlook

The Company will continue executing its plan for growth and profitability by investing in its core businesses and through mergers and acquisitions. Due to the many complexities of purchasing companies, the Company cannot predict its success in executing this strategy. The Company will leverage the substantial investments in technology and infrastructure made in 2004 and 2005 by adding independent contractors to its retail brokerage and investment banking businesses. The Company will expand its institutional sales business by focusing on providing a full range of investment, research and trading services to the Hedge Fund Industry. Furthermore, the Company plans to find opportunities to expand its newly acquired emerging markets fixed income securities trading business. In January 2006, the Company entered into an Asset Purchase Agreement whereby it agreed to purchase certain select assets of the Sterling Financial Investment Group and the Group of Companies of Sterling. The Company also entered into a management agreement whereby it agreed to provide certain management services to Sterling until such time as the Asset Purchase could be completed or April 24th whichever occurred first. In connection with this acquisition, the Company will add a fixed income proprietary trading business and an Independent Contractor arrangement with a Panamanian group.

-24-

Results of Operations

During 2005, the Company's revenues declined by \$502,901 or 1.9% and the company incurred losses in each fiscal quarter and a total net loss of \$1,137,398 for the year. In the final quarter of 2005, the Company's loss amounted to \$780,664 or roughly 69% of the total loss for the year. In the final quarter, the Company incurred an impairment charge of \$420,000 related to the write-off of goodwill and \$80,000 related to the impairment of an investment. The Company increased revenue by 9.4% in its retail brokerage business, which represents 62% of total revenues. This was offset by declines of 19.0% in its trading business and a 29.4% in investment banking which represent 16% and 10% of total revenue for 2005, respectively. Other brokerage related income increased \$270,100 or 10.5% and other revenues which consist primarily of management fee revenue related to the Center for Innovative Entrepreneurship decreased by \$106,762 or 24.4%. In 2004, other revenue was produced from sales through the company's website.

-25-

Edgar Filing: VFINANCE INC - Form 10KSB

The following table and discussion summarizes the changes in the major revenue and expense categories for the past two years.

| | For Years ended December 31, | | |
|---|------------------------------|------------------|--------------------|
| | 2005 | % of Revenues | 2004 |
| Revenues: | | | |
| Commissions - agency | \$ 15,941,221 | 62% | \$14,571,878 |
| Trading Profits | 4,177,402 | 16% | 5,156,842 |
| Success fees | 2,006,016 | 8% | 3,224,973 |
| Consulting and retainers | 533,644 | 2% | 370,829 |
| Other brokerage related income | 2,837,589 | 11% | 2,567,489 |
| Other | 330,378 | 1% | 437,140 |
| Total revenues | 25,826,250 | 100% | 26,329,151 |
| Cost of revenues: | | | |
| Commissions | 14,187,765 | 55% | 14,624,914 |
| Clearing and transaction costs | 1,905,215 | 7% | 1,030,114 |
| Success | 1,099,519 | 4% | 1,346,272 |
| Consulting and retainers | 377,585 | 2% | 224,916 |
| Other | 100 | 0% | 4,581 |
| Total cost of revenues | 17,570,184 | 68% | 17,230,797 |
| Gross profit | 8,256,066 | 32% | 9,098,354 |
| Other expenses: | | | |
| General and administrative | 8,479,910 | 34% | 6,686,372 |
| Professional fees | 262,607 | 1% | 157,370 |
| Provision for bad debts | 70,990 | 0% | 85,567 |
| Legal litigation | 312,155 | 1% | 399,647 |
| Depreciation and amortization | 299,604 | 1% | 147,804 |
| Amounts forgiven under forgivable loans | 6,597 | 0% | 80,161 |
| Stock based compensation | 19,412 | 0% | 5,294 |
| Total other expenses | 9,451,275 | 37% | 7,562,215 |
| Income (loss) from operations | (1,195,209) | (5%) | 1,536,139 |
| Gain on forgiveness of debt | 0 | 0% | 1,500,000 |
| Interest and dividend income (Expense) | 57,811 | 0% | (221,704) |
| Pre-tax net (loss) profit | (1,137,398) | (4%) | 2,814,435 |
| Income taxes | 0 | 0% | (40,000) |
| Net (loss) profit | \$ (1,137,398) | (4%) | \$2,774,435 |

-26-

Total revenues were \$25,826,250 for the year ended December 31, 2005 as compared to \$26,329,151 for the year ended December 31, 2004, a decrease of \$502,901, or 1.9%. The decrease in revenues was primarily related to Trading Profits and Success Fees which decreased by \$979,440, or 19.0% and \$1,218,957 or 37.8%, respectively, from the prior year, partially offset by an increase in retail agency commissions which increased \$1,369,343 or 9.4%, from the prior year along with an increase in consulting fees of \$162,815 or 43.9%. Overall, the Company attributes the decrease in its operating revenues to less favorable market conditions than in the prior year for the investment banking and trading businesses offset by an increase in its clearing revenue and retail agency commission revenue. Revenues in 2005 also benefited from having a full year of operations for the acquired businesses of Global Partners Securities.

Cost of revenues was \$17,570,184 for the year ended December 31, 2005 as compared to \$17,230,797 for the year ended December 31, 2004, an increase of \$339,387, or 2.0%. The increase was primarily due to an increase in the clearing and transaction costs of \$875,101, resulting from the addition of the EquityStation trading platform business and increases in execution fees for wholesale trading. This was offset by decreases in commissions and related fees of \$535,714 due to having lower revenues in principal trading and investment banking.

Gross profit was \$8,256,066 for the year ended December 31, 2005 as compared to \$9,098,354 for the year ended December 31, 2004, an decrease of \$842,288, or 9.3%. Gross profit margin for the year ended December 31, 2005 was 32.0% as compared to 34.6% for the year ended December 31, 2004, a decrease of 2.6% percentage points. The decrease in gross profit and gross profit margin was mostly due to profit of \$602,440 realized in 2004 from the sale of securities with no corresponding expense and the \$200,000 provided by NFS to assist the Company with transition costs related to the conversion from CSC to NFS which materially benefited the gross margin percentage in 2004.

General and administrative expenses were \$8,479,910 for the year ended December 31, 2005 as compared to \$6,686,372 for the year ended December 31, 2004, an increase of \$1,793,538, or 26.8%. This increase was mostly due to an investment in talent at the senior management level, higher health benefit costs, and increased rent expense due to expansion of our leased facilities at the corporate offices in Boca Raton and New York City and the addition of the disaster recovery sight in Mt. Laurel, New Jersey. In addition, the Company incurred a non-cash expense of \$500,000, for the impairment of goodwill associated with a prior acquisition and the write-down of an investment in one of its independent contractor entities which amounted to about one-third of the increase in G&A expense.

Professional fees were \$262,607 for the year ended December 31, 2005 as compared to \$157,370 for the year ended December 31, 2004, an increase of \$105,237, or 66.9%. The increase was primarily due to legal fees associated with the management agreements for Sterling, other acquisition activities that have not yet resulted in any definitive agreements and slightly higher fees from our independent accounting firm.

Provision for bad debts was \$70,990 for the year ended December 31, 2005 as compared to \$85,567 for the year ended December 31, 2004, a decrease of

Edgar Filing: VFINANCE INC - Form 10KSB

\$14,577, or 17.0%. The decrease was due to a more proactive approach by management to collect aged accounts.

Legal litigation was \$312,155 for the year ended December 31, 2005 as compared to \$399,647 for the year ended December 31, 2004, a decrease of \$87,492, or 21.9%. As is typical in the industry, customers make claims regarding the Company's actions and the Company defends itself vigorously against such claims. The Company's cost of defending itself varies year-to-year depending on the volume of claims which are in process at any given time.

Depreciation and amortization was \$299,604 for the year ended December 31, 2005 as compared to \$147,804 for the year ended December 31, 2004, an increase of \$151,800 or 103.7%. The increase is primarily due to the Company's investment in new systems and technologies as a strategy to introduce new services that exceed compliance requirements and offer a comprehensive business solution thereby increasing productivity while reducing regulatory risk.

The amount forgiven under forgivable loans was \$6,597 for the year ended December 31, 2005 as compared to \$80,161 for the year ended December 31, 2004, a decrease of \$73,564, or 91.8%. This decrease was attributable to the fact that several years ago the Company discontinued its practice of providing forgivable loans to brokers as part of its recruitment efforts. Accordingly, there have been no additions to the outstanding balance and the remaining balance was fully amortized in 2005.

Stock based compensation was \$19,412 for the year ended December 31, 2005 as compared to \$5,294 for the year ended December 31, 2004 an increase of \$14,118, or 266.7%. This amount primarily represents the amortization of deferred compensation to an outside consultant who was granted options from the Company in return for his services. The amount related to this consultant was fully recognized as of March 31, 2003. In addition, during January 2003, the Company granted warrants to its landlord related to the renegotiation of its lease and this amount was fully amortized in 2005 as a result of a change in ownership of the building leased as the company headquarters.

Net loss amounted to \$1,137,398 for the year ended December 31, 2005 as compared to Income of \$2,774,435 for the year ended December 31, 2004. The change was primarily due to the higher general and administrative costs and higher cost of revenue.

-27-

Income from forgiveness of indebtedness amounted to \$0 for the year ended December 31, 2005, as compared to \$1,500,000 as of December 31, 2004 which was the result of NFS agreeing to pay down the UBS credit facility, pursuant to a guaranty Fidelity Investments made to UBS as part of their original acquisition of the CSC clearing division.

Interest and dividend income, net of interest expense, was \$57,811 for the year ended December 31, 2005 as compared to interest expense net of interest and dividend income of \$221,704 for the year ended December 31, 2004, an increase of \$279,515. This increase in income was primarily attributable forgiveness of debt and less interest expense being paid as a result of this forgiveness.

We do not believe our operations are materially affected by inflation and or by seasonal fluctuations. Our main lines of business are directly affected by higher interest rates, the volatility and volume of the stock market and the capital markets.

LIQUIDITY AND CAPITAL RESOURCES

Net cash used by operating activities for the year ended December 31, 2005

Edgar Filing: VFINANCE INC - Form 10KSB

was \$673,187 compared to net cash provided of \$1,678,281 for the year ended December 31, 2004 a decrease of \$2,351,468. The decrease in cash provided from operating activities is primarily attributable to a decline in net income offset by changes in working capital. The Company's net loss for fiscal year 2004 was \$1,137,398 versus a profit of \$2,774,435 for fiscal year 2004. Net loss in 2005 included a non-cash loss of \$500,000 for impairment of goodwill and an investment.

Net cash used in investing activities for the year ended December 31, 2005 was \$493,804 as opposed to \$394,090 for the year ended December 31, 2004. The primary reason for the increase is due to investments in technology the Company made to introduce new services to our existing clients and our affiliates and to ensure that the firm was positioned to continuously service clients in the event of either a manmade or natural disaster. As part of that investment, the Company revamped its entire data and communications infrastructure. The Company has implemented a fully operational disaster recovery plan that features fully redundant data center in Mt. Laurel, New Jersey. In order to finance these capital expenditures, the Company entered into lease agreements (discussed below under cash provided by financing).

Net cash provided by financing activities for the year ended December 31, 2005 was \$338,089 as opposed to \$188,303 for the year ended December 31, 2004. The increase is primarily due to the Company entering into certain capital lease agreements to finance its investment in information technology equipment.

The Company believes that its cash on hand is sufficient to meet its working capital requirements over the next 12 months. However, the Company may seek additional debt or equity financing in order to carry out its long-term business strategy. Such funding may be a result of bank borrowings, public offerings, private placements of equity or debt securities, or a combination thereof.

FUTURE AND CONTINGENT LIABILITIES:

The following statements are made in consideration of Financial Reporting Release (FR-61), LIQUIDITY AND OFF-BALANCE SHEET ARRANGEMENTS, CERTAIN TRADING ACTIVITIES, & TRANSACTIONS WITH RELATED AND CERTAIN OTHER PARTIES. We do not have "off-balance sheet arrangements."

We lease office space under the terms of operating leases. The following chart shows lease obligations including rental of real property and equipment.

| YEAR | AMOUNT |
|-------|-------------|
| 2006 | 966,808 |
| 2007 | 934,118 |
| 2008 | 666,674 |
| 2009 | 89,569 |
| 2010 | 0 |
| | ----- |
| TOTAL | \$2,657,169 |
| | ===== |

Total rent expense under operating leases, including space rental, totaled approximately \$726,290 and \$690,414 for the years ended December 31, 2005 and 2004.

Edgar Filing: VFINANCE INC - Form 10KSB

Litigation:

From time to time we are a party to various lawsuits that have arisen in the ordinary course of business. The amounts asserted in these matters are material to our financial statements. While any litigation contains an element of uncertainty and although it is possible that losses exceeding amounts already recorded may be incurred upon ultimate resolution of these existing legal proceedings, management believes that such losses, if any, will not have a material adverse effect on our business, results of operations or financial position. However, unfavorable resolution of each matter individually or in the aggregate could affect the consolidated results of operations for the quarterly and annual periods in which they are resolved.

For a description of this litigation, see Part I, Item 3 of this Annual Report.

SUBSEQUENT EVENTS

On January 10, 2006, vFinance, Inc.'s (the "Company") wholly-owned subsidiary, vFinance Investments, Inc. ("vFinance Investments"), entered into an agreement to acquire certain assets of Sterling Financial Investment Group, Inc. ("SFIG") and Sterling Financial Group of Companies, Inc. ("SFGC" and together with SFIG, "Sterling Financial"). These transactions are subject to the approval of the National Association of Securities Dealers, Inc.

The assets to be acquired from Sterling Financial include Sterling Financial's businesses as a going concern, certain intellectual property, client accounts and revenues, computer equipment, and a certain real property lease. On the closing date, vFinance Investments will not assume any liabilities of Sterling Financial except an office lease and select office services contracts directly relating to the operation of the business that arise and are to be paid, performed or discharged from and after the closing date. One of the principals of Sterling Financial will enter into an employment agreement with vFinance Investments that provides for an annual base salary of \$262,000 and certain performance bonuses and options to be granted in the sole discretion of vFinance Investments.

In accordance with the terms of the asset purchase agreement, vFinance Investments will deliver to SFGC 17,500,000 shares of the Company's common stock and approximately \$26,800, for certain prepaid expenses. Subject to the financial performance of the business of Sterling Financial acquired by vFinance Investments over the period specified in the asset purchase agreement, up to 4,500,000 of such shares may be cancelled. The Company has granted SFGC certain registration rights with respect to the shares. The Company and vFinance Investments will enter into a standstill agreement with each of SFGC, SFIG, Charles Garcia and Alexis Korybut to provide restrictions on certain actions for a defined time period. The Company and vFinance Investments also will enter into a voting and lockup agreement with each of SFIG, SFGC, Charles Garcia, Leonard Sokolow and Timothy Mahoney to provide certain rights and obligations with respect to the Company's common stock.

vFinance Investments and Sterling Financial also entered into a management agreement, pursuant to which certain designated principals of vFinance Investments will provide risk management of, and operational and back office support for, the branch offices of SFIG from January 10, 2005 until the closing of the acquisition transactions. In addition, such principals will assist SFIG with the supervision of SFIG's registered representatives in accordance with applicable rules and regulations.

-29-

ITEM 7. FINANCIAL STATEMENTS.

vFinance, Inc.

Consolidated Financial Statements

Years ended December 31, 2005 and 2004

CONTENTS

| | |
|--|-----|
| Report of Independent Registered Public Accounting Firm..... | F-1 |
| Audited Financial Statements | |
| Consolidated Balance Sheet..... | F-2 |
| Consolidated Statements of Operations | F-3 |
| Consolidated Statements of Shareholders' Equity..... | F-4 |
| Consolidated Statements of Cash Flows..... | F-5 |
| Notes to Consolidated Financial Statements..... | F-6 |

-30-

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
vFinance Inc., & Subsidiaries

We have audited the accompanying balance sheet of vFinance Inc., & Subsidiaries, as of December 31, 2005 and the related statements of operations, shareholders' equity and cash flows for the years ended December 31, 2005 and 2004. These financial statements are the responsibility of the Company's management. 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

Edgar Filing: VFINANCE INC - Form 10KSB

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 vFinance Inc., & Subsidiaries, at December 31, 2005, and the results of its operations and its cash flows for the years ended December 31, 2005 and 2004, in conformity with accounting principles generally accepted in the United States.

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

Boca Raton, Florida
March 29, 2006

F-1

vFINANCE, INC. CONSOLIDATED BALANCE SHEET

December 31,

Assets:

Current Assets:

| | | |
|-----------------------------------|----|-----------|
| Cash and cash equivalents | \$ | 4,427,406 |
| Due from clearing broker | | 705,097 |
| Investments in trading securities | | 870,306 |
| Accounts receivable | | 408,841 |

Edgar Filing: VFINANCE INC - Form 10KSB

| | |
|---|--------------|
| Notes receivable-employees | 67,588 |
| Prepaid expenses and other current assets | 130,033 |
| | ----- |
| Total current assets | 6,609,271 |
| Furniture and equipment, at cost: | |
| Furniture and equipment | 1,383,878 |
| Internal use software | 173,890 |
| | ----- |
| | 1,557,768 |
| Less accumulated depreciation | (865,130) |
| | ----- |
| Net furniture and equipment | 692,638 |
| Intangible asset, net | 1,446,848 |
| Other assets | 313,327 |
| | ----- |
| Total Assets | \$ 9,062,084 |
| | ===== |
| Liabilities and Shareholders' Equity: | |
| Current liabilities: | |
| Accounts payable | \$ 714,197 |
| Accrued payroll | 1,678,632 |
| Other accrued liabilities | 825,594 |
| Securities sold, not yet purchased | 42,421 |
| Capital lease obligations | 187,775 |
| Other | 118,781 |
| | ----- |
| Total current liabilities | 3,567,400 |
| Capital lease obligations, long term | 225,067 |
| Shareholders' Equity: | |
| Series A Convertible Preferred Stock \$0.01 par value, 122,500 shares authorized, 0 shares issued and outstanding | - |
| Series B Convertible Preferred Stock \$0.01 par value, 50,000 shares authorized, 0 shares issued and outstanding | - |
| Common stock \$0.01 par value, 75,000,000 shares authorized, 40,126,133 issued and outstanding | 401,266 |
| Additional paid-in-capital | 26,821,557 |
| Accumulated deficit | (21,953,206) |
| | ----- |
| Total Shareholders' Equity | 5,269,617 |
| | ----- |
| Total Liabilities and Shareholders' Equity | \$ 9,062,084 |
| | ===== |

See Accompanying Notes
F-2

Edgar Filing: VFINANCE INC - Form 10KSB

vFINANCE, INC. CONSOLIDATED STATEMENTS OF OPERATIONS

| | Years Ended December 31, | |
|---|--------------------------|--------------|
| | 2005 | 2004 |
| Revenues: | | |
| Commissions - agency | \$15,941,221 | \$14,571,878 |
| Trading profits | 4,177,402 | 5,156,842 |
| Success Fees | 2,006,016 | 3,224,973 |
| Consulting and retainers | 533,644 | 370,829 |
| Other brokerage related income | 2,837,589 | 2,567,489 |
| Other | 330,378 | 437,140 |
| | 25,826,250 | 26,329,151 |
| Cost of revenues: | | |
| Commissions | 14,187,765 | 14,624,914 |
| Clearing and transaction costs | 1,905,215 | 1,030,114 |
| Success | 1,099,519 | 1,346,272 |
| Consulting and retainers | 377,585 | 224,916 |
| Other | 100 | 4,581 |
| | 17,570,184 | 17,230,797 |
| Gross profit | 8,256,066 | 9,098,354 |
| Other expenses: | | |
| General and administrative | 8,479,910 | 6,686,372 |
| Professional fees | 262,607 | 157,370 |
| Provision for bad debt | 70,990 | 85,567 |
| Legal litigation | 312,155 | 399,647 |
| Depreciation and amortization | 299,604 | 147,804 |
| Amounts forgiven under forgivable loans | 6,597 | 80,161 |
| Stock based compensation | 19,412 | 5,294 |
| | 9,451,275 | 7,562,215 |
| Income (Loss) from operations | (1,195,209) | 1,536,139 |
| Gain on forgiveness of debt | - | 1,500,000 |
| Interest and dividend income (expense) | 57,811 | (221,704) |
| | (1,137,398) | 2,814,435 |
| Pre-tax Net Income (Loss) | (1,137,398) | 2,814,435 |
| Federal income tax | - | (40,000) |
| | (1,137,398) | 2,774,435 |
| Net Income (Loss) available to common shareholders | \$ (1,137,398) | \$ 2,774,435 |
| Net Income (Loss) per share: | | |
| Basic | (0.03) | 0.08 |
| Weighted average number of common shares used in computing basic net income per share | 40,049,654 | 33,773,336 |

Edgar Filing: VFINANCE INC - Form 10KSB

| | | |
|---|------------|------------|
| Diluted | ===== | ===== |
| | (0.03) | 0.08 |
| | ===== | ===== |
| Weighted average number of common shares used in computing diluted net income per share | 40,049,654 | 35,840,248 |
| | ===== | ===== |

See Accompanying Notes
F-3

vFinance, Inc.
Consolidated Statements of Shareholders' Equity

| | Preferred Stock Shares | Preferred Stock Amount | Common Stock Shares | Common Stock Amount | Additional Paid-in Capital Common | Defer Compen |
|--|---------------------------|---------------------------|------------------------|------------------------|---|-----------------|
| Balance at December 31, 2003 | - | - | 29,851,570 | \$ 298,520 | \$ 24,376,798 | \$ (24, |
| Partial conversion of promissory note | | | 3,344,298 | 33,443 | 688,057 | |
| Conversion Premium on promissory note | | | - | - | 231,625 | |
| Imputed Interest write off | | | - | - | (128,438) | |
| Amortization of Deferred Compensation | | | - | - | - | 5, |
| Partial conversion of promissory note | | | 100,000 | 1,000 | 27,500 | |
| Issuance of shares in conjunction with acquisition of EquityStation Inc. and Global Partners | | | 6,275,265 | 62,753 | 1,518,015 | |
| Net Income | | | - | - | - | |
| Balance at December 31, 2004 | - | - | 39,571,133 | 395,716 | 26,713,557 | (19, |
| Exercise of Stock Options | | | 555,000 | 5,550 | 108,000 | |
| Amortization of Deferred Compensation | | | - | - | - | 19, |
| Net Loss | | | - | - | - | |
| Balance at December 31, 2005 | - | - | 40,126,133 | \$ 401,266 | \$ 26,821,557 | \$ |

Edgar Filing: VFINANCE INC - Form 10KSB

See Accompanying Notes

F-4

vFINANCE, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Years ended December 31 | |
|---|-------------------------|-----------|
| | 2005 | 2004 |
| | ----- | ----- |
| OPERATING ACTIVITIES | | |
| Net (loss) income | \$ (1,137,398) | \$ 2,774, |
| Adjustments to reconcile net income/(loss) to | | |
| Net cash used (provided) by operating activities: | | |
| Non-cash fees received | (487,511) | (419, |
| Gain on forgiveness of debt | - | (1,500, |
| Depreciation and amortization | 299,604 | 147, |
| Impairment of goodwill | 420,000 | |
| Loss on investment in other companies | 80,000 | |
| Provision for doubtful accounts | 69,657 | 79, |
| Non-cash compensation | - | 5, |
| Conversion premium expense | - | 231, |
| Accretion of debt discount | - | 18, |
| Unrealized loss on investments, net | 131,386 | 211, |
| Unrealized loss (gain) on warrants | 108,040 | (41, |
| Amount forgiven under forgivable loans | - | 80, |
| Stock based compensation | 19,412 | 5, |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (480,154) | 26, |
| Forgivable Loans | 6,597 | |
| Due from clearing broker | 13,394 | (297, |
| Notes receivable - employees | 101,113 | 14, |
| Investments in trading securities | 294,142 | 328, |
| Other assets and liabilities | (32,045) | (39, |
| Accounts payable and accrued liabilities | (54,375) | 68, |
| Securities, sold not yet purchased | (25,049) | (16, |
| | ----- | ----- |
| Net cash (used in) provided by operating activities | (673,187) | 1,678, |
| INVESTING ACTIVITIES | | |
| Cash acquired in acquisition | - | 56, |
| Purchase of capital lease equipment | (367,952) | (204, |
| Purchase of equipment | (125,852) | (245, |
| | ----- | ----- |
| Net cash used in investing activities | (493,804) | (394, |
| FINANCING ACTIVITIES | | |
| Proceeds from capital lease | 246,088 | 204, |
| Payments of capital lease | (21,550) | (16, |

Edgar Filing: VFINANCE INC - Form 10KSB

| | | |
|--|--------------|----------|
| Proceeds from issuance of common stock | 113,551 | |
| | | |
| Net cash provided by financing activities | 338,089 | 188, |
| Decrease (increase) in cash and cash equivalents | (828,902) | 1,472, |
| Cash and cash equivalents at beginning of year | 5,256,308 | 3,783, |
| | | |
| Cash and cash equivalents at end of year | \$ 4,427,406 | \$5,256, |
| | | |

See accompanying notes.

F-5

vFinance, Inc.

Notes to the Consolidated Financial Statements

1. DESCRIPTION OF BUSINESS

vFinance, Inc. is a holding company engaged in the financial services business where our strategic focus is on servicing the needs of high net-worth and institutional investors and high growth companies. Through our principal operating subsidiary, vFinance Investments, Inc., a licensed broker-dealer, we provide investment banking, retail and institutional brokerage services in all 50 states and the District of Columbia. The Company also operates a second broker-dealer, EquityStation, Inc. ("EquityStation") which offers institutional traders, hedge funds and professional traders a suite of services designed to enhance their trading by offering services such as trading technology, routing software, hedge fund incubation, capital introduction and custodial services. The Company, through its website www.vfinance.com, provides financial information services to entrepreneurs and venture investors.

2. SIGNIFICANT ACCOUNTING POLICIES AND OTHER MATTERS

Basis of Presentation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All inter-company accounts have been eliminated in consolidation.

Revenue Recognition

The Company earns revenue (commissions) from brokerage and trading which are recognized on the day of the trade - trade date basis. The Company also earns revenue from investment banking and consulting. Monthly retainer fees for investment banking and consulting are recognized as services are provided. Investment banking success fees are generally based on a percentage of the total value of a transaction and are recognized upon successful completion.

The Company does not require collateral from its customers. Revenues are not concentrated in any particular region of the country or with any individual or group.

The Company may receive equity instruments which include stock purchase warrants and common and preferred stock from companies as part of its compensation for investment-banking services that are classified as investments in trading

Edgar Filing: VFINANCE INC - Form 10KSB

securities on the balance sheet, if still held at the financial reporting date. These instruments are stated at fair value in accordance with SFAS #115 "Accounting for certain investments in debt and equity securities". Primarily all of the equity instruments are received from small public companies. The Company recognizes revenue for such stock purchase warrants, when received, based on the Black Scholes valuation model. The revenue recognized related to the other equity instruments is determined based on available market information, discounted by a factor reflective of the expected holding period for those particular equity instruments. For the years ended December 31, 2005 and 2004, the Company recognized \$487,511 and \$419,365, respectively, of revenue in connection with the receipt of equity instruments. On a monthly basis the Company recognizes unrealized gains or losses in its statement of operations based on the changes in value of equity instruments. Realized gains or losses are recognized in the statement of operations when the related equity instrument is sold.

Occasionally, the Company receives equity instruments in private companies with no readily available market value. Equity interests and warrants for which there is not a public market are valued based on factors such as significant equity financing by sophisticated, unrelated new investors, history of positive cash flow from operations, the market value of comparable publicly traded companies (discounted for liquidity) and other pertinent factors. Management also considers recent offers to purchase a portfolio company's securities and the filings of registration statements in connection with a portfolio company's initial public offering when valuing equity instruments received from a private company.

Upon the consummation of an advisory, consulting, capital or other similar transactions the Company may distribute equity instruments or proceeds from the sale of equity instruments to its employees. These distributions are made at the Company's discretion on a case by case basis as determined by the role of the employee and the nature of the transaction. At December 31, 2005 and 2004, no amounts were owed to current employees of the Company in connection with equity investments received as compensation.

As of December 31, 2005, certain transactions in process may result in the Company receiving equity instruments or stock purchase warrants in subsequent periods as discussed above. In such event, the Company will recognize revenue related to the receipt of such equity instruments consistent with the aforementioned policies.

F-6

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

2. SIGNIFICANT ACCOUNTING POLICIES AND OTHER MATTERS (CONTINUED)

Revenue Recognition (continued)

The Company sells two types of listings through its website: (i) perpetual listings to venture capital vendors, who are interested in providing services to other companies or individuals; and (ii) three-month listings to entrepreneurs who have new business ideas to sell. Revenue related to the listings is generally recognized over the terms of such listings. Website revenues are concentrated primarily in the United States but are not concentrated in any particular region of the country or with any individual or group. Fees related to such listings are included in "other" in the statements of operations for the years ended December 31, 2004. In May 2005, the Company entered into an

Edgar Filing: VFINANCE INC - Form 10KSB

agreement with The Center for Innovative Entrepreneurship ("CIE"), a nonprofit organization, to develop www.vfinance.com as a platform for academic-quality research on entrepreneurial activities and to produce the Company's proprietary vFinance Entrepreneurial Confidence Index ("VECI") and sector research reports, and to provide educational and informational services to entrepreneurs with start-ups and other early-stage firms. The Company also agreed to enter into a management services agreement to provide management, administrative and technical support services for CIE. These agreements became effective beginning in January 2005 and no revenue from website operations is shown in 2005 in other income. The fee income obtained from the management services agreement is shown as revenue under Other revenue in 2005.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. Furthermore, the Company, including its wholly owned subsidiary vFinance Investments, Inc., has been named as a defendant in various customer arbitrations. These claims result from the actions of brokers affiliated with vFinance Investments, Inc. In addition, under the vFinance Investments, Inc. registered representatives contract, each registered representative has indemnified the Company for these claims. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 5 "Accounting for Contingencies," the Company has established liabilities for potential losses from such complaints, legal actions, investigations and proceedings. In establishing these liabilities, the Company's management uses its judgment to determine the probability that losses have been incurred and a reasonable estimate of the amount of losses. In making these decisions, we base our judgments on our knowledge of the situations, consultations with legal counsel and our historical experience in resolving similar matters. In many lawsuits, arbitrations and regulatory proceedings, it is not possible to determine whether a liability has been incurred or to estimate the amount of that liability until the matter is close to resolution. However, accruals are reviewed regularly and are adjusted to reflect our estimates of the impact of developments, rulings, advice of counsel and any other information pertinent to a particular matter. Because of the inherent difficulty in predicting the ultimate outcome of legal and regulatory actions, we cannot predict with certainty the eventual loss or range of loss related to such matters. If our judgments prove to be incorrect, our liability for losses and contingencies may not accurately reflect actual losses that result from these actions, which could materially affect results in the period other expenses are ultimately determined. As of December 31, 2005, the Company has accrued approximately \$ 220,000 for these matters. As the Company has recently acquired an errors and omissions policy, future claims will be covered in excess of the policies \$75,000 per claim deductible. While the Company will vigorously defend itself in these matters, and will assert insurance coverage and indemnification to the maximum extent possible, there can be no assurance that these lawsuits and arbitrations will not have a material adverse impact on its financial position.

Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid investments with maturities of three months or less when purchased.

Accounts and Notes Receivable

Accounts and notes receivable balances are reviewed monthly to determine the Company's ability to collect such receivables. The Company records both a

Edgar Filing: VFINANCE INC - Form 10KSB

specific and general reserve on such balances as deemed appropriate.

F-7

Investments

Investments are classified as investments in trading securities and are held for resale in anticipation of short-term market movements or until such securities are registered or are otherwise unrestricted. Investments in trading securities include both trading account assets and equity instruments which the Company has received as part of its compensation for investment banking services. At December 31, 2005, investments consisted of common stock, corporate bonds and common stock purchase warrants held for resale.

Trading account assets, consisting of marketable equity securities, are stated at fair value. Unrealized gains or losses are recognized in the statement of operations on a monthly basis based on changes in the fair value of the security as quoted on national or inter-dealer stock exchanges. Realized gains or losses are recognized in the statement of operations as trading profits when the equity instruments are sold.

As mentioned above, the Company periodically receives equity instruments which include stock purchase warrants and common and preferred stock from companies as part of its compensation for investment-banking services. These instruments are stated at fair value in accordance with SFAS #115 "Accounting for certain investments in debt and equity securities" and EITF 00-8 "Accounting by a grantee for an equity instrument to be received in conjunction with providing goods or services." Primarily all of the equity instruments are received from small public companies. The stock and the stock purchase warrants received are typically restricted as to resale, although, the Company generally receives a registration right within one year. Company policy is to resell these securities in anticipation of short-term market movements. The Company recognizes revenue for such equity instruments based on the fair value of the stock at the time equity instruments are granted and for stock purchase warrants based on the Black-Scholes valuation model. Unrealized gains or losses are recognized in the statement of operations on a monthly basis based on changes in the fair value of the security as quoted on national or inter-dealer stock exchanges, discounted by a factor to address the remaining period which the equity instrument is restricted as to resale.

Net unrealized (losses)gains related to investments in trading securities as of December 31, 2005, and 2004, aggregated \$(244,447) and \$170,660, respectively. Net realized gains related to investments in trading securities as of December 31, 2005 and 2004 aggregated \$174,775 and \$1,087,741, respectively.

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

2. SIGNIFICANT ACCOUNTING POLICIES AND OTHER MATTERS (CONTINUED)

Investments in trading securities and securities sold, not yet purchased, consist of trading and investment securities at market values at December 31, 2005, as follows:

| | Owned | Sold, not yet purchased |
|------------------|------------|-------------------------|
| Corporate Stocks | \$ 849,858 | \$ 42,421 |
| Warrants | 20,448 | |
| Total | \$ 870,306 | \$ 42,421 |

At December 31, 2005, restricted equity securities had an aggregate fair value of \$253,841.

Securities Transactions

Proprietary securities transactions in regular-way trades are accrued and recorded on the trade date, as if they had settled. Profit and loss arising from all securities and commodities transactions entered into for the account and risk of the Company are recorded on a trade date basis. Customers' securities and commodities transactions are reported on a settlement date basis with related commission income and expense reported on a trade date basis.

Amounts receivable and payable for securities transactions that have not reached their contractual settlement date are recorded net on the balance sheet.

Financial Instruments with Off-Balance Sheet Risk

The securities transactions of the Company's customers are introduced on a fully disclosed basis with a clearing broker-dealer. The Company holds no customer funds or securities. The clearing broker-dealer is responsible for execution, collection of and payment of funds, and receipt and delivery of securities relative to customer transactions. Off-balance sheet risk exists with respect to these transactions due to the possibility that customers may be unable to fulfill their contractual commitments wherein the clearing broker-dealer may charge any related losses to the Company. The Company seeks to minimize this risk through procedures designed to monitor the creditworthiness of its customers and to ensure that customer transactions are executed properly by the clearing broker-dealer.

Stock Based Compensation

The Company has elected to follow Accounting Principles Board Opinion No. 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES ("APB 25"), and related interpretations

Edgar Filing: VFINANCE INC - Form 10KSB

in accounting for its employee stock options and employee stock purchase warrants because the alternative fair value accounting provided for under Statement of Financial Accounting Standards No. 123, ACCOUNTING FOR STOCK BASED COMPENSATION ("SFAS 123") and SFAS 148 ACCOUNTING FOR STOCK BASED COMPENSATION TRANSITION AND DISCLOSURE, AN AMENDMENT OF SFAS 123, requires the use of option valuation models that were not developed for use in valuing employee stock options. Under APB 25, if the exercise price of the Company's employee stock options or stock purchase warrants equals or exceeds the market price of the underlying stock on the date of grant no compensation expense is recognized.

Fair Value of Financial Instruments

The fair values of the Company's financial instruments, which includes cash and cash equivalents, accounts and notes receivable, investments, accounts payable, and accrued expenses approximate their carrying values.

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. The Company places its cash with high quality insured financial institutions.

F-9

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

2. SIGNIFICANT ACCOUNTING POLICIES AND OTHER MATTERS (CONTINUED)

Furniture and Equipment

Furniture and equipment are stated on the basis of cost less accumulated depreciation and consists primarily of computer equipment. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, 2-5 years, for financial reporting purposes. Depreciation expense for the years ended December 31, 2005 and 2004, totaled \$299,604 and \$147,804 respectively. Included in Furniture and Equipment is approximately \$573,000 of equipment acquired under capital leases.

Intangible Asset

The carrying value of intangible assets as well as other long-lived assets are reviewed if the facts and circumstances suggest that they may be impaired. If this review indicates that the assets will not be recoverable, as determined based on the undiscounted estimated cash flows of the Company over the remaining amortization period, the Company's carrying values of the assets would be reduced to their estimated fair values in accordance with Statement of Financial Accounting Standards No. 144, ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS ("FAS 144"). Among other factors considered in such evaluation is the historical and projected operating performance of business operations, the operating environment and business strategy, competitive information and market trends. As a result of the acquisition of EquityStation and certain assets of Global in November 2004, the Company recorded goodwill in the amount of \$1,446,848. The Company had goodwill of \$1,866,848 as of December 31, 2004, which constituted approximately 19% of our total assets. In November 2005, the Company reassessed the allocation of the original purchase price of Equity Station and Global and re-classed the goodwill to customer relationships. The customer relationships will be amortized over 5 years. No amortization expense has been recorded through December 31, 2005. Management evaluates this balance on an ongoing basis and as a result of this evaluation, has impaired the goodwill by \$420,000 against its First Level acquisition. Management believes

Edgar Filing: VFINANCE INC - Form 10KSB

that there has not been an impairment of its remaining long-lived assets as of December 31, 2005. The Company no longer has goodwill recorded on its books at December 31, 2005.

Income Taxes

The Company accounts for income taxes under the liability method in accordance with Statement of Financial Accounting Standards No. 109, ACCOUNTING FOR INCOME TAXES. Under this method, deferred income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Statement of Cash Flows

Supplemental disclosure of cash flow information:

Non-cash items affecting the statement of cash flows are as follows:

| | 2005 | 2004 |
|--|-----------|--------------|
| | ----- | ----- |
| Cash paid for interest during the year | \$ 30,710 | \$ 34,008 |
| Non-cash items affecting investing and financing activities: | | |
| Conversion Premium expense | \$ 0 | \$ 231,625 |
| | ===== | ===== |
| Imputed Interest | \$ 0 | \$ 18,349 |
| | ===== | ===== |
| Common Stock issued for payment of Note | \$ 0 | \$ 750,000 |
| | ===== | ===== |
| Common Stock issued for Acquisition | \$ 0 | \$ 1,580,768 |
| | ===== | ===== |

F-10

Earnings per Share

The Company calculates earnings per share in accordance with Statement of Financial Accounting Standards No. 128, EARNINGS PER SHARE ("SFAS No. 128"). In accordance with SFAS No. 128, basic earnings per share is computed using the weighted average number of shares of common stock outstanding and diluted earnings per share is computed using the weighted average number of shares of common stock and the dilutive effect of options and warrants outstanding, using the "treasury stock" method. The company had 658,701 options and warrants at December 31, 2005, not included in diluted earnings per share because the options and warrants would have been anti-dilutive because the company had a net loss.

Forgivable Loans

In order to remain competitive in the marketplace, the Company previously granted forgivable loans to certain employees. The terms of the loans ranged from two to five years with scheduled maturity dates from 2002 to 2005. For each year the employee is in good standing with the Company, the Company forgives a ratable portion of the loan and charges this amount to compensation expense. If the employee is terminated, the principal balance is due and payable within 120

Edgar Filing: VFINANCE INC - Form 10KSB

days. The loans do not bear interest and interest is not imputed as the Company's ability to collect such interest would not be probable. As of December 31, 2005, the balance of the forgivable loans was \$0, as the balance was fully amortized in 2005.

Other Accrued Liabilities

Other accrued liabilities is primarily comprised of \$280,000 in settlement reserves for open litigation and \$185,000 in accrued bonus payable and \$93,620 in accrued audit fees related to the 2005 audit as of December 31, 2005.

F-11

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

2. SIGNIFICANT ACCOUNTING POLICIES AND OTHER MATTERS (CONTINUED)

Due from Clearing Broker

Receivables from brokers and dealers consist primarily of amounts due from the Company's clearing organization, which provides clearing and depository services for brokerage transactions on a fully disclosed basis.

3. ACQUISITIONS

On November 2, 2004, vFinance's wholly-owned subsidiary, vFinance Investments completed its acquisition of certain assets of Global and 100% of the issued and outstanding equity securities of EquityStation, all of which were owned by Level2, a subsidiary of Global. These transactions are subject to the approval of the National Association of Securities Dealers, Inc.

Edgar Filing: VFINANCE INC - Form 10KSB

In accordance with the terms of the acquisition agreements, the Company delivered into escrow 8,324,690 restricted shares of the Company's common stock, and warrants to purchase 3,299,728 shares of the Common Stock at a price of \$0.11 per share. All of the shares of EquityStation were also delivered into escrow. Subject to (a) any indemnification claims under the acquisition agreements and (b) the financial performance of EquityStation and the business of Global acquired by vFinance Investments over the periods specified in the escrow agreement, all or a portion of the Shares and the Warrants will be distributed to Global and Level2. As determined pursuant to the financial performance calculation in the escrow agreement, 2,199,425 of the Shares and 871,805 of the Warrants are subject to cancellation in accordance with the terms of the escrow agreement. When the escrow agreement is terminated, all of the shares of EquityStation will be distributed to vFinance Investments, and the holders of the Shares and Warrants will be entitled to certain piggyback registration rights. The Company also entered into a standstill agreement with each of Marcos Konig, Harry Konig and Salomon Konig, to provide restrictions on certain actions for a defined time period.

As remuneration for providing advisory services to Global in connection with the acquisitions, Scott J. Saunders ("Saunders") received 150,000 restricted shares of the Common Stock. The shares received by Saunders are not subject to the escrow agreement, registration rights agreement or standstill agreement.

Goodwill was determined as follows; 6,125,265 common shares issued to Global and EquityStation, 150,000 common shares issued to Saunders valued at \$1,192,300 or \$0.19 per share, 2,427,923 warrants valued at \$0.16 per warrant or \$388,468 using the Black-Scholes valuation model, and legal fees in the amount of \$47,863 for a total purchase price of \$1,628,631. The Company acquired net assets of \$181,783 and allocated the difference between the purchase price and the net assets acquired of \$1,446,848 as goodwill. See note 2 for description of the reclassification of goodwill to the intangible asset Customer Relationships.

In accordance with Financial Interpretation No. 44 "Accounting for Certain Transactions Involving Stock Compensation" we have included all vested stock options issued by the Company in exchange for outstanding awards held by employees of the acquired company as part of the purchase price.

The following Pro Forma Combined Financial Statements of Global, EquityStation and vFinance gives effect to the acquisition of certain assets of Global and 100% of the issued and outstanding equity securities of EquityStation, under the purchase method of accounting prescribed by Accounting Principles Board Opinion No. 16, Business Combinations. These pro forma statements are presented for illustrative purposes only. The pro forma adjustments are based upon available information and assumptions that management believes are reasonable.

F-12

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

3. ACQUISITIONS (CONTINUED)

Edgar Filing: VFINANCE INC - Form 10KSB

VFINANCE, INC.
Pro Forma Combined Statement of Operations
For the Year Ended December 31, 2004

| | vFinance | Global Partners | EquityStation | Pro Forma Adjustments | Pro Forma |
|--|--------------|--------------------|---------------|--------------------------|---------------|
| REVENUE | | | | | |
| Commissions | \$14,571,878 | \$ 186,402 | \$1,764,299 | \$ - | \$ 16,522,579 |
| Trading Profits | 5,156,842 | 2,868,675 | 2,489 | - | 8,028,006 |
| Success Fees | 3,224,973 | - | - | - | 3,224,973 |
| Consulting and Retainers | 370,829 | - | - | - | 370,829 |
| Other Brokerage Related Income | 2,567,489 | - | - | - | 2,567,489 |
| Other Income | 437,140 | 388,714 | 2 | - | 825,856 |
| | ----- | ----- | ----- | ----- | ----- |
| | 26,329,151 | 3,443,791 | 1,766,790 | - | 31,539,732 |
| | ===== | ===== | ===== | ===== | ===== |
| COST OF REVENUES | | | | | |
| Commissions | 14,624,914 | 1,675,493 | 456,037 | - | 16,756,444 |
| Clearing and Transaction Costs | 1,030,114 | 674,469 | 665,853 | - | 2,370,436 |
| Success | 1,346,272 | - | - | - | 1,346,272 |
| Consulting and Retainers | 224,916 | 2,760 | - | - | 227,676 |
| Other | 4,581 | 2,363 | 1,278 | - | 8,222 |
| | ----- | ----- | ----- | ----- | ----- |
| | 17,230,797 | 2,355,085 | 1,123,168 | - | 20,709,050 |
| | ===== | ===== | ===== | ===== | ===== |
| GROSS PROFIT | 9,098,354 | 1,088,707 | 643,621 | - | 10,830,682 |
| | ----- | ----- | ----- | ----- | ----- |
| EXPENSES | | | | | |
| General and Administrative | 6,686,372 | 1,808,585 | 802,936 | - | 9,297,893 |
| Professional Fees | 157,370 | 6,635 | 260 | - | 164,265 |
| Provision for Bad Debt | 85,567 | - | - | - | 85,567 |
| Legal litigation | 399,647 | 94,921 | 18,414 | - | 512,982 |
| Depreciation and Amortization | 147,804 | 18,869 | - | - | 166,673 |
| Amounts Forgiven under Forgivable Loans | 80,161 | - | - | - | 80,161 |
| Stock Based Compensation | 5,294 | - | - | - | 5,294 |
| | ----- | ----- | ----- | ----- | ----- |
| | 7,562,215 | 1,929,010 | 821,610 | - | 10,312,834 |
| | ----- | ----- | ----- | ----- | ----- |
| INCOME (LOSS) From Operations | 1,536,139 | (840,303) | (177,988) | - | 517,848 |
| | ----- | ----- | ----- | ----- | ----- |
| Gain on Forgiveness of Debt | 1,500,000 | - | - | - | 1,500,000 |
| Interest and Dividend Income (Expense) | (221,704) | 3,131 | 7,520 | - | (211,053) |
| | ----- | ----- | ----- | ----- | ----- |
| PRE TAX NET INCOME (LOSS) | 2,814,435 | (837,172) | (170,468) | - | 1,806,795 |
| | ----- | ----- | ----- | ----- | ----- |
| Federal Income Tax | (40,000) | - | - | - | (40,000) |

Edgar Filing: VFINANCE INC - Form 10KSB

| | | | | | |
|--|--------------|--------------|--------------|-------|--------------|
| NET INCOME (LOSS) Available to Shareholders | \$ 2,774,435 | \$ (837,172) | \$ (170,469) | \$ - | \$ 1,766,795 |
| | ===== | ===== | ===== | ===== | ===== |

F-13

4. NET CAPITAL REQUIREMENT

Both vFinance Investments and EquityStation are subject to the Securities and Exchange Commission Uniform Net Capital Rule (rule 15c3-1), which requires the maintenance of minimum net capital and requires that the ratio of aggregate indebtedness to net capital, both as defined, shall not exceed 15 to 1 (and the rule of the "applicable" exchange also provides that equity capital may not be withdrawn or cash dividends paid if the resulting net capital ratio would exceed 10 to 1). At December 31, 2005, vFinance Investments had net capital of \$2,030,784, which was \$1,030,784 in excess of its required net capital of \$1,000,000. EquityStation had net capital of \$583,430 that was \$483,430 in excess of its required net capital of \$100,000.

vFinance Investments' aggregate indebtedness to net capital ratio was to 1.28 to 1 in 2005. Equity Station's aggregate indebtedness to net capital ratio was 0.33 to 1. vFinance Investments and EquityStation qualify under the exemptive provisions of Rule 15c3-3 under Section (k)(2)(ii) of the Rule, in that they do not carry security accounts of customers or perform custodial functions related to customer securities.

5. RELATED PARTY TRANSACTIONS

On November 16, 2004, the Company entered into new agreements ("Primary Employment Agreements") to amend and restate certain employment agreements dated November 8, 1999 between the Company's Chief Executive Officer and President, who is the beneficial owner of 15% and 19.7% of the total outstanding common shares of the Company at December 31, 2005 and 2003, respectively, and the Company's Chief Operating Officer and Chairman, who is the beneficial owner of 15% and 19.7% of the total outstanding common shares of the Company at December 31, 2004 and 2003, respectively (collectively the "Primary Shareholders"), as amended on January 5, 2001, July 2, 2001 and January 7, 2002 (the "Previous Employment Agreement"). Under the terms of the Primary Employment Agreements, which shall be for a three year period and shall automatically extend for a one year period on each anniversary date thereafter unless the Company has provided a non-renewal notice thirty (30) days prior to an anniversary date as directed by a majority vote of the board of directors, each individual shall receive (i) an initial base salary of \$257,000 per annum which shall increase 5% per annum beginning January 1, 2005 and each year thereafter and will be reviewed by the Board at least annually and may be increased (but not decreased) from time to time as Board may determine; (ii) discretionary bonuses and/or interim cash bonuses and/or other bonuses when and in such amounts as may be determined by the Company's board of directors based on each individuals performance, the Company's performance and/or other factors; provided that the Board shall meet at least annually to review employees' bonus entitlements; and (iii) incentive compensation paid quarterly no later than the 45th day following the end of quarter primarily based on performance of the Company and its respective subsidiaries. The Primary Employment Agreements also contain provisions related to change of control.

On January 1, 2003, the Company entered into a Joint Venture Agreement with JSM

Edgar Filing: VFINANCE INC - Form 10KSB

Capital Holding Corp. ("JSM"), a retail brokerage operations headquartered in New York and founded by John S. Matthews. The Company issued JSM 1,000,000 warrants to purchase its common stock at an exercise price of \$0.20 in exchange for a 19% equity position in JSM. The warrants were valued using the Black-Scholes valuation method which calculated the value to be \$0.08 per warrant, or \$80,000. The Company accounts for this investment using the cost method. Effective May 1, 2003, vFinance merged its "company-owned" retail branches into JSM. Effective upon such merger JSM became an independent contractor of the Company. In August 2005, the relationship between the Company and JSM was terminated, and management impaired the asset fully.

F-14

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

6. INCOME TAXES

The components of the Company's tax provision for the years ended December 31, 2005 and 2004 were as follows:

| | Year Ended December 31, | |
|-------------------------------|-------------------------|-----------|
| | 2005 | 2004 |
| Current income tax expense | \$ - | \$ 40,000 |
| Deferred income tax (benefit) | - | (40,000) |
| | \$ - | \$ - |

Deferred income taxes reflect the net income tax effect of temporary differences between the carrying amounts of the assets and liabilities for financial reporting purposes and amounts used for income taxes. The Company's deferred income tax assets and liabilities consist of the following:

| | Year Ended December 31, | |
|---|-------------------------|-----------|
| | 2005 | 2004 |
| Net operating loss carryforwards | \$ 4,587,563 | \$ 3,282, |
| Unrealized losses | 158,079 | 65, |
| Impairment of Investment in JSM | 30,860 | |
| Allowance for doubtful accounts | - | 2, |
| Depreciation | (154,250) | 11, |
| | 4,622,252 | 3,362, |
| Gross deferred income tax assets | | |
| Deferred income tax asset valuation allowance | (4,622,252) | (3,322, |
| | | |

Edgar Filing: VFINANCE INC - Form 10KSB

November 30, December 14 and December 28, 2001 and February 13 and March 4, 2002 (collectively, the "Agreement"), with SBI Investments (USA) Inc. ("SBI"). Under the terms of the Agreement, SBI provided a loan to us in the amount of \$975,000 in the form of a 48-month non-interest bearing, convertible note (the SBI Note"). The SBI Note is convertible at SBI's option into as many as 3,421,052 shares of our common stock at \$0.285 per share.

In accordance with EITF Issue No. 00-27, (APPLICATION OF ISSUE NO. 98-5), ACCOUNTING FOR CONVERTIBLE SECURITIES WITH BENEFICIAL CONVERSION FEATURES OF CONTINGENTLY ADJUSTABLE CONVERSION RATIOS, IN CERTAIN CONVERTIBLE INSTRUMENTS, and APB # 21 (INTEREST ON RECEIVABLES AND PAYABLES) the Company recorded an imputed interest factor related to the Note Purchase Agreement of \$563,000. The Company fully expensed the beneficial conversion factor due to the fact that the SBI Note was immediately convertible. The net one time charge to the financial statements was \$412,000.

The imputed interest was accreted ratably over the term of the loan as additional interest expense. Amortization of the imputed interest began in January 2002.

During year 2002, the SBI Note was reduced by \$225,000 as a portion of the SBI Note was converted into 789,474 shares of the Company's common stock.

As of December 31, 2003 the SBI note payable balance was \$750,000 and was netted against the \$146,787 corresponding asset imputed interest.

During February and March of 2004, \$721,500 of the SBI Note was converted into 3,344,298 shares of the Company's common stock. Of this amount, \$545,000 was converted into 2,725,000 shares of the Company's common stock at a discounted rate of \$0.20 per share under a special arrangement offered by the Company to encourage further equity participation by SBI, which resulted in a \$231,625 conversion premium expense during the first quarter of 2004. The remainder, \$176,500, was converted into 619,298 shares at the stated conversion rate of \$0.285 per share. In April of 2004, the remaining balance was converted into 100,000 shares of common stock of the Company at the original stated conversion rate of \$.285 per share. The issuance of the common stock was exempt from registration pursuant to Section 4 (2) of the Securities Act of 1933, as amended, because the common stock was acquired in a privately negotiated transaction by sophisticated investors. Accordingly, the balance due SBI at December 31, 2003 was \$750,000 and 2004 and 2005 was \$0.

F-16

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

7. SHAREHOLDERS' EQUITY (CONTINUED)

During the first quarter of 2005, the Company granted stock options to purchase an aggregate of 1,277,500 shares of the Company's common stock to certain employees of the Company. The exercise prices of these options range from \$.25 to \$.35. During the second quarter of 2005, the Company granted stock options to purchase an aggregate of 1,177,500 shares of the Company's common stock to certain employees of the Company. The exercise prices of these options range from \$.17 to \$.35. During the third quarter of 2005, the Company granted stock options to purchase an aggregate of 1,616,250 shares of the Company's common stock to certain employees of the Company. The exercise prices of these options range from \$0.17 to \$0.26. During the fourth quarter of 2005, the Company

Edgar Filing: VFINANCE INC - Form 10KSB

granted stock options to purchase an aggregate of 5,870,000 shares of the Company 's common stock to certain employees of the Company. The exercise prices of these options range from \$0.155 to \$0.21. The option grants were exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended, because the individuals receiving the options are sophisticated investors who have knowledge of all material information about the Company.

On January 31, 2005, The Company issued 300,000 common shares in connection with the exercise of options. The Company received \$60,000. The exercise price of these options was \$0.20.

On March 14, 2005, The Company issued 255,000 common shares in connection with the exercise of options. The Company received \$53,550. The exercise price of these options was \$0.21.

F-17

A summary of the stock option activity for the years ended December 31, 2005 and 2004 is as follows:

| | Weighted Average Exercise Price | Number of Shares | Exercise Price Per Option |
|--|--|---------------------|------------------------------|
| | ----- | ----- | ----- |
| Outstanding Options at December 31, 2003 | 0.29 | 10,346,211 | 0.15 - 6.00 |
| Granted | 0.21 | 4,137,502 | 0.19 - 0.36 |
| Forfeited | 0.23 | (3,945,500) | 0.15 - 0.35 |
| | | ----- | |
| Outstanding Options at December 31, 2004 | 0.28 | 10,538,213 | 0.15 - 2.25 |
| Granted | 0.19 | 9,941,250 | 0.16 - 0.35 |
| Forfeited | 0.30 | (5,309,624) | 0.15 - 2.25 |
| Exercised | 0.21 | (555,000) | 0.20 - 0.21 |
| | | ----- | |
| Outstanding Options at December 31, 2005 | 0.23 | 14,614,839 | 0.15 - 2.25 |
| | | ===== | |

Stock Options Outstanding

| Range of Exercise Prices | Number of Shares | Weighted Avg Remaining Contractual Life in Years | Weighted Average Exercise Price |
|-----------------------------|------------------|---|--|
| ----- | ----- | ----- | ----- |
| \$ 0.15 - 2.25 | 14,614,839 | 4.18 | \$ 0.23 |
| | ===== | ===== | ===== |

The following table summarizes information concerning stock options outstanding at December 31, 2005

| Weighted Average Exercise | Number |
|---------------------------------|--------|
|---------------------------------|--------|

Edgar Filing: VFINANCE INC - Form 10KSB

| Price | Outstanding |
|---------|-------------|
| ----- | ----- |
| \$0.150 | 260,000 |
| 0.155 | 4,500,000 |
| 0.170 | 885,000 |
| 0.180 | 180,000 |
| 0.190 | 1,662,502 |
| 0.200 | 485,000 |
| 0.205 | 400,000 |
| 0.210 | 2,064,497 |
| 0.220 | 60,000 |
| 0.230 | 902,500 |
| 0.245 | 750,000 |
| 0.250 | 43,750 |
| 0.270 | 5,000 |
| 0.280 | 597,500 |
| 0.320 | 310,000 |
| 0.330 | 2,500 |
| 0.350 | 484,215 |
| 0.363 | 120,000 |
| 0.500 | 100,000 |
| 0.550 | 69,000 |
| 0.625 | 642,500 |
| 0.700 | 39,000 |
| 1.000 | 18,000 |
| 2.250 | 33,875 |
| | ----- |
| | 14,614,839 |
| | ===== |

F-18

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

7. SHAREHOLDERS' EQUITY (CONTINUED)

A summary of the warrant activity for the years ended December 31, 2005 and 2004 is as follows:

| | Weighted Average Exercise Price | Number of Shares | Exercise Price Per Option |
|---|--|---------------------|------------------------------|
| | ----- | ----- | ----- |
| Outstanding Warrants at December 31, 2003 | 1.70 | 5,398,499 | 0.35 - 7.20 |
| Granted | 0.16 | 2,927,923 | 0.15 - 0.16 |
| Forfeited | 0.44 | (230,000) | 0.35 - 2.50 |
| | | ----- | |
| Outstanding Warrants at December 31, 2004 | 1.18 | 8,096,422 | 0.15 - 7.20 |
| Granted | - | - | 0.00 - 0.00 |
| Forfeited | 2.21 | (436,833) | 0.35 - 6.00 |
| | | ----- | |
| Outstanding Warrants at December 31, 2005 | 1.12 | 7,659,589 | 0.15 - 7.20 |
| | | ===== | |

The following table summarizes information concerning warrants outstanding at December 31, 2005.

Edgar Filing: VFINANCE INC - Form 10KSB

| Weighted Average Exercise Price | Number Outstanding |
|--|-----------------------|
| ----- | ----- |
| 0.15 | 750,000 |
| 0.16 | 2,427,923 |
| 0.20 | 1,000,000 |
| 0.35 | 1,673,500 |
| 0.63 | 400,000 |
| 2.25 | 605,000 |
| 6.00 | 103,166 |
| 7.20 | 700,000 |
| | ----- |
| | 7,659,589 |
| | ===== |

There were no warrants granted for the year ended December 31, 2005. The weighted average grant-date fair value of warrants granted equaled \$0.16 for the year ended December 31, 2004. The weighted average grant-date fair value of options granted during the year equaled \$0.19 and \$0.21 for the years ended December 31, 2005 and 2004, respectively. For purposes of pro forma disclosures, the estimated fair value of the options and warrants is amortized to expense over their respective vesting periods.

Options granted to employees are exercisable according to the terms of each agreement, ranging from one month to four years. At December 31, 2005 and 2004, 3,926,421 and 5,779,766 options outstanding were exercisable with weighted average exercise prices of \$.33 and \$.35, respectively. At December 31, 2005 and 2004, 7,639,589 and 7,920,172 warrants outstanding were exercisable with weighted average exercises prices of \$1.11 and \$1.15, respectively.

Pro forma information regarding net loss is required by SFAS 123, which also requires that the information be determined as if the Company has accounted for its employee stock options under the fair value method. The fair value for options and warrants granted was estimated at the date of grant using the Black Scholes option pricing model with the following weighted-average assumptions: for 2005 risk free interest rates of 4.25%; expected dividends of zero; volatility factor of the expected market price of the Company's common stock of 0.723 for options and warrants and an expected life of the options and warrants of 4-5 years; for 2004 risk free interest rates of 3.31%; expected dividends of zero; volatility factor of the expected market price of the Company's common stock of 1.12 for options and warrants and an expected life of the options and warrants of 4-5 years. The Company's pro forma net loss for the year ended December 31, 2005 was \$1,543,569 and the pro forma net income for the year ended December 31, 2004 was \$2,287,230. The Company's pro forma basic and diluted net loss per share for the year ended December 31, 2005 was \$(0.04) and the Company's pro forma basic and diluted income per share for December 31, 2004 were \$0.07 and \$0.06, respectively. The impact of the Company's pro forma net loss and loss per share of the SFAS 123 pro forma requirements are not likely to be representative of future pro forma results.

F-19

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

Edgar Filing: VFINANCE INC - Form 10KSB

7. SHAREHOLDERS' EQUITY (CONTINUED)

The Company recorded deferred compensation of \$19,412 and \$5,294 during the years ended December 31, 2005 and 2004, respectively, in connection with the grants of stock options, primarily to outside consultants, with exercise prices lower than the deemed fair value per share of the Company's common stock on the date of the grants. The Company had an unamortized balance of \$ 12,420 at December 31, 2002 fully amortized during 2003. In addition, during 2003 the Company granted 250,000 warrants, valued at \$30,000, to its landlord in relation to the renegotiation of the lease on its headquarters. This balance was to be amortized over the term of the lease. At December 31, 2005 the remaining unamortized balance was \$0.

8. DEBT

On January 25, 2002, the Company entered into a Credit Agreement, as amended on April 12, 2002, with UBS Americas, Inc. ("UBS"). Under the terms of the Credit Agreement, UBS provided the Company with a revolving credit facility for up to \$3,000,000 for the purpose of supporting the expansion of our brokerage business or investments in infrastructure to expand our operations and our broker-dealer operations. The loan had a term of 4 years, was required to be repaid in full by January 2005, and accrued interest at LIBOR plus a LIBOR margin of 2% if the loan was repaid within a month or 5% if it was outstanding more than a month. The Company borrowed \$1,500,000 under the credit facility on January 28, 2002 leaving an additional \$1,500,000 available. In June 2003, Fidelity Investments, on behalf of its clearing division, National Financial Services LLC, Member NYSE/SIPC, a Fidelity Investments company ("NFS"), announced that it had acquired Correspondent Services Clearing ("CSC"), an affiliate of UBS and vFinance Investments' clearing firm at the time. The credit facility stayed with UBS subsequent to the acquisition giving rise to potential breaches under such credit facility as well as precluding the Company from drawing an additional \$1,500,000 thereunder. During March 2004, NFS agreed to directly pay down the UBS credit facility in the amount of \$1,500,000 pursuant to a guaranty Fidelity Investments made to UBS as part of their original acquisition of the CSC clearing division. As a result, the Company was relieved from \$1,500,000 in debt but no longer had the ability to obtain an additional \$1,500,000 under the credit facility or assert any claims against UBS or NFS regarding this transaction and credit facility. During March 2004, the Company entered into a clearing agreement with NFS. The new clearing agreement required NFS to pay to vFinance, over a five year period beginning January 2004, a monthly incentive bonus not to exceed \$25,000 per month up to \$1,500,000, based on a formula that the Company believes is very achievable. Accordingly, NFS has been paying \$25,000 per month related to this incentive calculation and such amount, \$300,000 through December 31, 2005, has been included in the attached statements of operations as "other brokerage related income". The new clearing agreement also required NFS to provide the Company with \$200,000 to assist the company with transition costs related to the conversion from CSC to NFS. This amount was paid to vFinance in March 2004 and was included in the first quarter's statements of operations as a reduction to clearing and transaction costs. In consideration for these incentives, NFS required a termination fee of \$1,700,000 should vFinance discontinue using NFS' services. This fee is reduced, pro rata, annually over the five year term of the agreement. The Company began clearing through NFS during May 2004.

F-20

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

Edgar Filing: VFINANCE INC - Form 10KSB

9. COMMITMENTS AND CONTINGENCIES

The Company leases office space under the terms of operating leases. The following chart shows lease obligations including rental of real property and equipment.

| YEAR | AMOUNT |
|-------|-------------|
| 2006 | 966,808 |
| 2007 | 934,118 |
| 2008 | 666,674 |
| 2009 | 87,194 |
| 2010 | - |
| | ----- |
| TOTAL | \$2,654,794 |
| | ===== |

Total rent expense under operating leases, including space rental, totaled \$726,290 and \$690,415 for the years ended December 31, 2005 and 2004.

Capital lease obligations at December 31, 2005 consisted of the following:

| | 2005 |
|--------------------------------|------------|
| | ----- |
| Obligation under capital lease | \$ 412,842 |
| Less current maturities | (187,775) |
| | ----- |
| | \$ 225,067 |
| | ===== |

Future minimum lease payments for equipment under capital leases at December 31, 2005 are as follows:

| | |
|------------------------------------|------------|
| 2006 | \$ 215,996 |
| 2007 | 196,589 |
| 2008 | 41,986 |
| 2009 | - |
| | ----- |
| Total minimum lease payments | 454,571 |
| Less amount representing interest | (41,729) |
| | ----- |
| Present value of net minimum lease | 412,842 |
| Less current portion | (187,775) |
| | ----- |
| | \$ 225,067 |
| | ===== |

F-21

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

9. COMMITMENTS AND CONTINGENCIES (CONTINUED)

From time to time the Company, and/or one of its subsidiaries, is named as a party to a lawsuit that has arisen in the ordinary course of business. Although

Edgar Filing: VFINANCE INC - Form 10KSB

it is possible that losses exceeding amounts already recorded may be incurred upon ultimate resolution of these existing legal proceedings, we believe that such losses, if any, will not have a material adverse effect on our business, results of operations or financial position; however, unfavorable resolution of each matter individually or in the aggregate could affect the consolidated results of operations for the quarterly and annual periods in which they are resolved.

The business of vFinance Investments and EquityStation involve substantial risks of liability, including exposure to liability under federal and state securities laws in connection with the underwriting or distribution of securities and claims by dissatisfied customers for fraud, unauthorized trading, churning, mismanagement and breach of fiduciary duty. In recent years, there has been an increasing incidence of litigation involving the securities industry, including class actions that generally seek rescission and substantial damages.

In the ordinary course of business, the Company and/or its subsidiaries may be parties to other legal proceedings and regulatory inquiries, the outcome of which, either singularly or in the aggregate, is not expected to be material. There can be no assurance however that any sanctions will not have a material adverse effect on the financial condition or results of operations of the Company and/or its subsidiaries. The following is a brief summary of certain matters pending against or involving the Company and its subsidiaries.

On August 20, 2001, we entered into a Securities Exchange Agreement by means of which we acquired the membership interests in two related companies, Critical Investments, LLC, a Delaware limited liability company ("Critical Investments"), and Critical Advisors, L.L.C., a Virginia limited liability company ("Critical Advisors"). Critical Investments manages Critical Infrastructure Fund, L.P. ("Critical Infrastructure LP"), a Delaware limited partnership. Critical Advisors manages Critical Infrastructure Fund, Ltd. ("Critical Infrastructure Ltd."), an international business company organized and existing under the laws of the British Virgin Islands and receives (i) a management fee equal to 1% of the net asset value of Critical Infrastructure Ltd. and (ii) a performance fee equal to 20% of the increase in net asset value of Critical Infrastructure Ltd. Critical Infrastructure LP and Critical Infrastructure Ltd. are the sole general partners in, owning 96% and 4%, respectively, and conduct their investment and trading activity through Critical Infrastructure Fund (BVI), LP, a limited partnership organized and existing under the laws of the British Virgin Islands, which holds a portfolio of securities. A determination has been made to liquidate the funds

On August 14, 2002, Henry S. Snow and Sandra L. Snow filed a complaint against Colonial Direct and vFinance, Inc. in the Circuit Court of the 15th Judicial Circuit in Palm Beach County, Florida. The claim alleges "Breach of Contract" and "Unjust Enrichment" and seeks damages of \$250,000 plus interest and court costs. It is alleged that Colonial Direct defaulted on a Promissory Note in the principal amount of \$250,000. The Company believes their claim is without merit and is vigorously defending the action.

F-22

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

9. COMMITMENTS AND CONTINGENCIES (CONTINUED)

On October 17, 2003, we were advised by the staff of the SEC that it intended to recommend that the SEC institute enforcement proceedings against vFinance Investments and one of its former employees. The SEC claims that vFinance

Edgar Filing: VFINANCE INC - Form 10KSB

Investments and its former employee failed reasonably to supervise the alleged illegal trading activities over a period of approximately two months of one of our broker/dealer's former securities traders with respect to one publicly traded security that resulted in vFinance Investments earning \$11,000 in commissions related to that one security over the two month period. As of December 31, 2005, the Company has included an accrual of \$50,000 for estimated expenses. On March 17, 2005 we were advised by a member of the staff of the SEC that the SEC had accepted our offer to settle the matter. Pursuant to the terms of the settlement, vFinance Investments paid amounts aggregating to \$50,000 by March 2006.

On or about February 28, 2005, Knight Equity Markets, LP ("Knight") filed an arbitration action (NASD Case No. 05-01069) against vFinance Investments, Inc. ("vFinance"), claiming that vFinance received roughly \$6.5 million in dividends that rightfully belong to Knight. vFinance asserts that the dividends actually went to two of its clients, Pearl Securities LLC ("Pearl Securities") and Michael Balog, and that vFinance has no liability. vFinance filed third party claims against Pearl Securities and Michael Balog to bring all of the parties into the action. vFinance's motion to amend the third party claim to include these two clients is currently pending. Pearl and Balog have filed motions to dismiss vFinance's claims and the motions are scheduled for hearing on April 17, 2006. Knight is seeking approximately \$6.5 million in damages plus costs, attorney fees and punitive damages. vFinance denies any liability to Knight and intends to vigorously defend against Knight's claims.

On or about September 27, 2005, John S. Matthews filed an arbitration action (NASD Case No. 05-014991) against vFinance, claiming that vFinance wrongfully terminated his independent contact with vFinance and that vFinance "stole" his clients and brokers. Mr. Matthews has obtained a temporary restraining order and an agreed upon injunction was issued by the NASD panel. Matthews and JMS Capital Holding Corp., a plaintiff in the arbitration action also request unspecified damages resulting from vFinance's alleged improper activity. The full hearing on the merits is currently scheduled for August 30 through September 1, 2006. vFinance intends to vigorously defend this matter. In addition to contesting and defending against JSM's and Mr. Matthews claims, vFinance filed a counterclaim for indemnity based upon the contractual agreement between the parties.

We are engaged in a number of other legal proceedings incidental to the conduct of our business. These claims aggregate a range of \$28,000 to \$260,000.

F-23

vFinance, Inc.

Notes to Consolidated Financial Statements (continued)

10. DEFINED CONTRIBUTION PLAN

The Company maintains a defined contribution savings plan in which substantially all employees are eligible to participate. The Company may match up to 25% of the employee's salary. The Company made no contributions to the plan for the years ended December 31, 2005 and 2004, respectively.

11. SUBSEQUENT EVENTS

On January 10, 2006, vFinance, Inc.'s (the "Company") wholly-owned subsidiary, vFinance Investments, Inc. ("vFinance Investments"), entered into an agreement to acquire certain assets of Sterling Financial Investment Group, Inc. ("SFIG") and Sterling Financial Group of Companies, Inc. ("SFGC" and together with SFIG, "Sterling Financial"). These transactions are subject to the approval of the

Edgar Filing: VFINANCE INC - Form 10KSB

National Association of Securities Dealers, Inc.

The assets to be acquired from Sterling Financial include Sterling Financial's businesses as a going concern, certain intellectual property, client accounts and revenues, computer equipment, and a certain real property lease. On the closing date, vFinance Investments will not assume any liabilities of Sterling Financial except an office lease and select office services contracts directly relating to the operation of the business that arise and are to be paid, performed or discharged from and after the closing date. One of the principals of Sterling Financial will enter into an employment agreement with vFinance Investments that provides for an annual base salary of \$262,000 and certain performance bonuses and options to be granted in the sole discretion of vFinance Investments.

In accordance with the terms of the asset purchase agreement, vFinance Investments will deliver to SFGC 17,500,000 shares of the Company's common stock and approximately \$26,800, for certain prepaid expenses. Subject to the financial performance of the business of Sterling Financial acquired by vFinance Investments over the period specified in the asset purchase agreement, up to 4,500,000 of such shares may be cancelled. The Company has granted SFGC certain registration rights with respect to the shares. The Company and vFinance Investments will enter into a standstill agreement with each of SFGC, SFIG, Charles Garcia and Alexis Korybut to provide restrictions on certain actions for a defined time period. The Company and vFinance Investments also will enter into a voting and lockup agreement with each of SFIG, SFGC, Charles Garcia, Leonard Sokolow and Timothy Mahoney to provide certain rights and obligations with respect to the Company's common stock.

vFinance Investments and Sterling Financial also entered into a management agreement, pursuant to which certain designated principals of vFinance Investments will provide risk management of, and operational and back office support for, the branch offices of SFIG from January 10, 2005 until the closing of the acquisition transactions. In addition, such principals will assist SFIG with the supervision of SFIG's registered representatives in accordance with applicable rules and regulations.

F-24

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

None.

ITEM 8A. CONTROLS AND PROCEDURES.

Our Chief Executive Officer and Chief Financial Officer (collectively, the "Certifying Officers") are responsible for establishing and maintaining disclosure controls and procedures for us. Such officers have concluded (based upon such officers' evaluation of these controls and procedures as of the end of the period covered by this report) that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in this report is accumulated and communicated to management, including our principal executive officers as appropriate, to allow timely decisions regarding required disclosure.

The Certifying Officers have also indicated that there were no significant changes in our internal controls or other factors that could significantly affect such controls subsequent to the date of their evaluation, and there were no corrective actions with regard to significant deficiencies and material

Edgar Filing: VFINANCE INC - Form 10KSB

weaknesses.

Our management, including each of the Certifying Officers, does not expect that our disclosure controls or our internal controls will prevent all error and fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. In addition, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. 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 control. The design of any systems 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. Because of these inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

ITEM 8B. OTHER INFORMATION.

Not Applicable

-55-

PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT.

The following table sets forth the names, ages and positions of our executive officers and directors as of March 28, 2005. Under our bylaws, each director holds office until the election and qualification of his successor or until his earlier resignation or removal.

| Name | Age | Position |
|--------------------|-----|---|
| Leonard J. Sokolow | 49 | Director, Chief Executive Officer and President |
| Timothy E. Mahoney | 49 | Director, Chief Operating Officer and Chairman |
| Sheila C. Reinken | 45 | Chief Financial Officer and Chief Administrative Officer |
| Richard Campanella | 55 | Secretary |

LEONARD J. SOKOLOW has been a director since November 8, 1997, our Chief Executive Officer since November 8, 1999, and our President since January 5, 2001. From November 8, 1999 through January 4, 2001, Mr. Sokolow was Vice Chairman of the Board. Since September 1996, Mr. Sokolow has been President of Union Atlantic LC, a merchant, banking and strategic consulting firm specializing domestically and internationally in technology industries that is a wholly-owned subsidiary of our company. Since August 1993, Mr. Sokolow has been President of Genesis Partners, Inc., a private financial business-consulting

Edgar Filing: VFINANCE INC - Form 10KSB

firm. Genesis Partners, Inc. has been inactive since December 31, 2002. From August 1994 through December 1998, Mr. Sokolow was the Chairman and Chief Executive Officer of the Americas Growth Fund, Inc., a public closed-end management investment company. Mr. Sokolow received a B.A. degree with majors in Economics and Accounting from the University of Florida in 1977, a J.D. degree from the University of Florida School of Law in 1980 and an LL.M. (Taxation) degree from the New York University Graduate School of Law in 1982. Mr. Sokolow is a Certified Public Accountant.

TIMOTHY E. MAHONEY has been a director since November 8, 1999 and since November 8, 1999, Chairman of the Board and our Chief Operating Officer. Since September 1996, Mr. Mahoney has been a partner of Union Atlantic LC. From 1994 through 1995, Mr. Mahoney was President of the Highlands Group. Mr. Mahoney was a founder of the consumer products business for SyQuest Technology. In 1986, Mr. Mahoney founded and was the President of Rodime Systems, a computer disk drive sub-system manufacturer. In addition, Mr. Mahoney was the Vice President of Marketing and Sales for Tecmar, the first PC add-in board company and spent eight years in marketing and sales management in the computer timesharing business with Computer Sciences Corporation, Automatic Data Processing and General Electric Information Services. Mr. Mahoney received a B.A. degree with majors in Computer Science and Business from the West Virginia University in 1978. Mr. Mahoney received a Master of Business Administration from George Washington University in 1983.

SHEILA C. REINKEN has been the Chief Financial Officer and Chief Administrative Officer of the Company since January 2005. Ms. Reinken was vice president, finance for Burger King Corporation from March 2002 through November 2004. Prior to that Ms. Reinken was vice president, finance for American Eagle Outfitters and from January 2001 until February 2002. Prior to that Ms. Reinken was vice president, treasurer of Ames Department Stores, Inc. from August 1999 until January 2001. She holds a Master of Business Administration from Florida Atlantic University and a Bachelor of Science degree from Florida State University.

RICHARD CAMPANELLA has been Secretary of the Company since December 18, 2001. Mr. Campanella currently serves as the President, Chief Operating Officer and Chief Compliance Officer of vFinance Investments, Inc. He assumed the role of President of vFinance Investments, Inc. as of July 2005. From February 1994 until April 2001, Mr. Campanella was a partner of Commonwealth Associates, a registered broker dealer where he served as the director of Compliance. He has a degree in Business Administration from the College of Staten Island.

-56-

AUDIT COMMITTEE

The Company's board of directors serves as the audit committee. Leonard J. Sokolow has been designated as an "audit committee financial expert" as such term is defined in the SEC's rules.

CODE OF ETHICS

The Company has adopted a Code of Ethics for the Chief Executive Officer and Chief Financial Officer, which was filed as Exhibit 14 to the Annual Report on Form 10-KSB for the fiscal year ended December 31, 2003, and is herein incorporated by reference. If the Company makes any substantive amendments to its code of ethics or grants any waiver, including any implicit waiver, from a provision of the code to the Chief Executive Officer or Chief Financial Officer, the Company will disclose the nature of such amendment or waiver in a report on

Edgar Filing: VFINANCE INC - Form 10KSB

Form 8-K.

SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Exchange Act requires our directors and executive officers, and persons who beneficially own more than ten percent (10%) of a registered class of our company's equity securities, to file with the Securities and Exchange Commission (SEC) initial reports of ownership and reports of changes in ownership of Common Stock and the other equity securities of the Company. Officers, directors and persons who beneficially own more than ten percent (10%) of a registered class of our company's equity securities are required by the regulations of the SEC to furnish the Company with copies of all Section 16(a) forms they file.

To our knowledge, based solely on review of these filings and written representations from the directors and officers, we believe that during the fiscal year ended December 31, 2005, our officers, directors and significant stockholders have timely filed the appropriate form under Section 16(a) of the Exchange Act, except a Form 4 for Sheila C. Reinken (one filing).

-57-

ITEM 10. EXECUTIVE COMPENSATION.

The following table provides information concerning the annual and long term compensation earned by our chief executive officer and each of the other most highly compensated executive officers of the Company (collectively, the "Named Executive Officers") during the fiscal years ended December 31, 2005, 2004 and 2003:

| Name/Position ----- | SUMMARY COMPENSATION TABLE | | | | Long-Term Compensation |
|--|----------------------------|-----------|-----------|-----------------------|-------------------------------------|
| | Year | Salary | Bonus | Other Compensation | Securities Underlying Options |
| | ----- | ----- | ----- | ----- | ----- |
| Leonard J. Sokolow CEO, President (1) (2) (3) | 2005 | \$270,375 | \$145,000 | \$0 | 1,500,000 (1) |
| | 2004 | \$236,265 | \$180,000 | \$0 | 0 |
| | 2003 | \$230,265 | \$0 | \$18,900 (2) | 734,802 (3) |
| Timothy E. Mahoney COO, Chairman (1) (2) (3) | 2005 | \$270,375 | \$130,000 | \$0 | 1,500,000 (1) |
| | 2004 | \$236,265 | \$175,000 | \$0 | 0 |
| | 2003 | \$230,265 | \$0 | \$18,900 (2) | 734,802 (3) |
| Sheila C. Reinken Chief Financial Officer (4) | 2005 | \$175,000 | \$38,000 | \$0 | 1,250,000 |
| Richard Campanella President Chief Operating Officer | 2005 | \$130,000 | \$0 | \$0 | 600,000 |
| | 2004 | \$125,000 | \$10,000 | \$0 | 0 |
| | 2003 | \$125,000 | \$0 | \$0 | 75,000 |

Edgar Filing: VFINANCE INC - Form 10KSB

vFinance Investments, Inc.

| | | | | | |
|--|------|-----------|----------|-----|---------|
| Kathleen Kennedy Vice President (5) | 2005 | \$128,154 | \$10,000 | \$0 | 500,000 |
|--|------|-----------|----------|-----|---------|

(1) Messrs. Sokolow and Mahoney earned \$145,000 and 130,000, respectively, in 2005, \$180,000 and \$175,000 in 2004, and \$0 in 2003 of annual incentive compensation based on the performance of the Company during the respective years. These amounts are reflected in the corresponding table as bonuses.

(2) Messrs. Sokolow and Mahoney each received a car allowance of \$18,900 during 2003.

(3) Options that were issued in prior years were cancelled in 2002. During 2003, they were each granted 734,802 options. In 2005, 500,000 of the options for both Mr. Sokolow and Mr. Mahoney expired.

(4) Mrs. Reinken's employment with the Company began in January 2005.

(5) Mrs. Kennedy's employment with the Company began in January 2005.

-58-

OPTION GRANTS IN LAST FISCAL YEAR

Options were granted to the Chief Executive Officer and other Named Executive Officers of the Company in the amounts noted in the following table. No options were exercised during 2005.

| Year-End (1) | Number of Securities Underlying Options Granted | % of Total Options Granted to Employees in Fiscal Year | Exercise or Base Price (\$/Share) | Expiration Date |
|--------------------|--|--|---|--------------------|
| Name | ----- | ----- | ----- | ----- |
| Leonard J. Sokolow | 1,500,000 | 15.1% | \$0.155 | 12/29/2010 |
| Timothy E. Mahoney | 1,500,000 | 15.1% | \$0.155 | 12/29/2010 |
| Sheila C. Reinken | 750,000 | 7.5% | \$0.245 | 01/14/2010 |
| Sheila C. Reinken | 500,000 | 5.0% | \$0.155 | 12/29/2010 |
| Richard Campanella | 600,000 | 6.0% | \$0.170 | 06/30/2010 |
| Kathleen Kennedy | 500,000 | 5.0% | \$0.280 | 01/19/2010 |

Fiscal Year-End Option Table

The following table provides information on the total number of exercisable and unexercisable stock options held at December 31, 2005 by the Named Executive Officers. None of the Named Executive Officers exercised any options during fiscal year 2005.

Edgar Filing: VFINANCE INC - Form 10KSB

| Name | Number of Securities Underlying Unexercised Options at Fiscal Year-End | | Value of Unexercised In-the-Money Options at Fiscal Year-End (1) | |
|--------------------|---|---------------|---|---------------|
| | Exercisable | Unexercisable | Exercisable | Unexercisable |
| Leonard J. Sokolow | 234,802 | 1,500,000 | \$ - | \$ - |
| Timothy E. Mahoney | 234,802 | 1,500,000 | - | - |
| Sheila C. Reinken | 93,750 | 1,156,250 | - | - |
| Richard Campanella | 100,000 | 600,000 | - | - |
| Kathleen Kennedy | - | 500,000 | - | - |

(1) Based on the difference between the option's exercise price and a closing price of \$0.17 for the underlying common stock on December 30, 2005 (our last business day of fiscal year 2005) as reported by the National Quotation Bureau.

COMPENSATION OF DIRECTORS

Directors do not receive any compensation for serving on our Board of Directors.

EMPLOYMENT AGREEMENTS

On November 16, 2004, the Company entered into new agreements ("Primary Employment Agreements") to amend and restate certain employment agreements dated November 8, 1999 between the Company's Chief Executive Officer and President, who is the beneficial owner of 15% and 19.7% of the total outstanding common shares of the Company at December 31, 2005 and 2003, respectively, and the Company's Chief Operating Officer and Chairman, who is the beneficial owner of 15% and 19.7% of the total outstanding common shares of the Company at December 31, 2004 and 2003, respectively (collectively the "Primary Shareholders"), as amended on January 5, 2001, July 2, 2001 and January 7, 2002 (the "Previous Employment Agreement"). Under the terms of the Primary Employment Agreements, which shall be for a three year period and shall automatically extended for a one year period on each anniversary date thereafter unless the Company has provided a non-renewal notice thirty (30) days prior to an anniversary date as directed by a majority vote of the board of directors, each individual shall receive (i) an initial base salary of \$257,000 per annum which shall be increase 5% per annum beginning January 1, 2005 and each year thereafter and will be reviewed by the Board at least annually and may be increased (but not decreased) from time to time as Board may determine; (ii) discretionary bonuses and/or interim cash bonuses and/or other bonuses when and in such amounts as may be determined by the Company's board of directors based on each individuals performance, the Company's performance and/or other factors; provided that the Board shall meet at least annually to review employees' bonus entitlements; and (iii) incentive compensation paid quarterly no later than the 45th day following the end of quarter primarily based on performance of the Company and its respective subsidiaries. The Primary Employment Agreements also contain provisions related to change of control.

-59-

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

The following table sets forth common stock ownership information as of March 28, 2005 with respect to:

Edgar Filing: VFINANCE INC - Form 10KSB

- Each person known to us to be the beneficial owner of more than 5% of our common stock;
- Each of our Named Executive Officers and directors; and
- All directors and officers as a group.

This information as to beneficial ownership was furnished to us by or on behalf of the persons named. Unless otherwise indicated, the business address of each person listed is 3010 North Military Trail, Suite 300, Boca Raton, Florida. Information with respect to the percent of class is based on outstanding shares of common stock as of March 28, 2005. Except as otherwise indicated, to our knowledge, each stockholder has sole power to vote and dispose of all the shares of common stock listed opposite his name.

For purposes of this table, each person is deemed to have beneficial ownership of any shares of our common stock such person has the right to acquire on or within 60 days after March 28, 2006.

| Name of Beneficial Owner ----- | Amount of Shares Beneficially Owned ----- | Percent of Class ----- |
|--|---|---------------------------|
| Leonard J. Sokolow(1) | 6,617,812 | 16.72% |
| Timothy E. Mahoney(2) | 6,617,811 | 16.72% |
| Highlands Group Holdings, Inc. (3) | 2,175,000 | 5.42% |
| Richard Campanella (5) | 406,250 | * |
| All executive officers and directors as a group (5 persons) | 13,941,873 | 34.70% |

* Denotes less than 1% ownership.

(1) Includes 5,883,010 shares of common stock issued in the names of Mr. Sokolow and his wife.

(2) Includes 2,175,000 shares of common stock issued in the name of Highlands Group Holdings, Inc., 3,708,009 shares of common stock issued in the name of Mr. Mahoney.

(3) Highlands Group Holdings, Inc., whose address is 68 Cayman Place, Palm Beach Gardens, Florida 33418, is wholly owned by Mr. Timothy Mahoney, Chairman and Chief Operating Officer. Mr. Mahoney, as the owner of Highlands Group Holdings, Inc., is deemed to beneficially own the 2,175,000 shares held by Highlands Group Holdings, Inc.

(4) Includes 25,000 shares of common stock issued in the name of Mr. Campanella.

The following table sets forth certain information as of December 31, 2005, with respect to compensation plans (including individual compensation arrangements) under which our equity securities are authorized for issuance under:

- all compensation plans previously approved by our security holders; and
- all compensation plans not previously approved by our security holders.

| | | |
|---|---|--|
| Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted average exercise price of outstanding options, and rights | remaining available for future issuance under equity compensation plans (excluding securities Plan category warrants reflected in column (a)) |
|---|---|--|

(a)

(b)

(c)

Edgar Filing: VFINANCE INC - Form 10KSB

| | | | |
|--|------------|------|---|
| Equity compensation plans approved by security holders | - | - | - |
| Equity compensation plans not approved by security holders * | 22,274,428 | 0.53 | - |
| Total | 22,274,428 | 0.53 | - |

* For a description of the individual compensation arrangements in 2005 See Note 7 to the Consolidated Financial Statements included elsewhere herein.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

None.

-60-

ITEM 13. EXHIBITS

| Number of Exhibit | Exhibit Description |
|-------------------|--|
| 2.1 | Share Exchange Agreement among the Company, vFinance Holdings, Inc., certain shareholders of vFinance Holdings, Inc. and Union Atlantic, dated November 8, 1999 (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on November 8, 1999). |
| 2.2 | Amendment to Share Exchange Agreement dated November 29, 1999 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000). |
| 2.3 | Agreement and Plan of Merger dated as of December 22, 2000, by and among the Company, NW Holdings, Inc., and Alvin S. Mirman, Ilene Mirman, Marc N. Siegel, Richard L. Galterio, Vincent W. Labarbara, Eric M. Rand, and Mario Marsillo, Jr. (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on January 17, 2001). |
| 2.4 | Agreement and Plan of Merger, dated as of January 3, 2001, by and among the Company, Colonial Acquisition Corp., Colonial Direct Financial Group, Inc., and Michael Golden and Ben Lichtenberg (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on January 17, 2001). |
| 3.1 | Certificate of Incorporation as filed with the Delaware Secretary of State on February 12, 1992 (incorporated by reference to the Company's Registration Statement on Form S-18 filed with the SEC on July 24, 1992). |
| 3.2 | Certificate of Renewal and Revival of Certificate of Incorporation as filed with the Delaware Secretary of State on March 15, 1996 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000). |
| 3.3 | Certificate of Amendment to the Certificate of Incorporation as filed with the Delaware Secretary of State on April 28, 1999 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000). |

Edgar Filing: VFINANCE INC - Form 10KSB

- 3.4 Certificate of Amendment to Certificate of Incorporation as filed with the Delaware Secretary of State on March 13, 2000 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000).
- 3.5 Certificate of Amendment to Certificate of Incorporation as filed with the Delaware Secretary of State on November 28, 2001.
- 3.6 Certificate of Designation of Series A Convertible Preferred Stock of the Company as filed with the Delaware Secretary of State on January 3, 2001 (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on January 17, 2001).
- 3.7 Certificate of Designation of Series B Convertible Preferred Stock of the Company as filed with the Delaware Secretary of State on January 3, 2001 (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on January 17, 2001).
- 3.8 Bylaws of the Company (incorporated by reference to the Company's Registration Statement on Form S-18 filed with the SEC on July 24, 1992).
- 3.9 Unanimous Written Consent of the Company's Board of Directors dated January 24, 1994, amending the Bylaws (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000).
- 3.10 Unanimous Written Consent of the Company's Board of Directors, effective as of January 24, 1994, amending the Bylaws (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000).

-61-

- 10.1 Purchase Agreement between the Company and Steven Jacobs and Mauricio Borgonovo, dated December 24, 1999, for the purchase of Pinnacle Capital Group, LLC (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000).
- 10.2 Asset Purchase Agreement among the Company, Steven Jacobs and Mauricio Borgonovo dated January 3, 2000 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000).
- 10.3 Stock Purchase Agreement between the Company and River Rapids Ltd., dated September 27, 1999 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000).
- 10.4 Amendment to Stock Purchase Agreement between the Company and River Rapids Ltd. dated December 22, 1999 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 30, 2000).
- 10.5 Common Stock and Warrants Purchase Agreement among the Company, AMRO International, S.A., CALP II Limited Partnership, a Bermuda Limited partnership, Celeste Trust Reg, Balmore SA, Sallee

Edgar Filing: VFINANCE INC - Form 10KSB

Investments LLLP, worldVentures Fund I, LLC and RBB Bank Aktiengesellschaft, dated March 31, 2000 (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on April 13, 2000).

- 10.6 Registration Rights Agreement among the Company, AMRO International, S.A., CALP II Limited Partnership, a Bermuda limited partnership, Celeste Trust Reg, Balmore SA, Sallee Investments LLLP, worldVentures Fund I, LLC, RBB Bank Aktiengesellschaft and Thomas Kernaghan & Co., Ltd., dated March 31, 2000 (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on April 13, 2000).
- 10.7 Form of Warrant issued to AMRO International, S.A. (to purchase 100,000 shares), CALP II Limited Partnership, a Bermuda limited partnership (to purchase 350,000 shares), Celeste Trust Reg (to purchase 5,000 shares), Balmore SA (to purchase 35,000 shares), Sallee Investments LLLP (to purchase 25,000 shares), worldVentures Fund I, LLC (to purchase 25,000 shares), RBB Bank Aktiengesellschaft (to purchase 130,000 shares) and Thomas Kernaghan & Co., Ltd. (to purchase 58,333 shares) (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on April 13, 2000).
- 10.8 Escrow Agreement among the Company, AMRO International, S.A., CALP II Limited Partnership, a Bermuda limited partnership, Celeste Trust Reg, Balmore SA, Sallee Investments LLLP, worldVentures Fund I, LLC, RBB Bank Aktiengesellschaft and Epstein Becker & Green, P.C., dated March 31, 2000 (incorporated by reference to Amendment No. 1 to the Company's Registration (Statement on Form SB-2 filed with the SEC on July 14, 2000)).
- 10.9* Amended and Restated Employment Letter Agreement dated December 18, 2000, between the Company and David Spector (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC on March 20, 2001).
- 10.10 Securities Exchange Agreement, dated as of August 15, 2001, among Kathleen Wallman, Steven Wallman, Joseph Daniel and vFinance.com, Inc. (n/k/a vFinance, Inc.) (Incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed with the SEC on August 14, 2001).
- 10.11 Registration Rights Agreement, dated as of August 15, 2001, among Kathleen Wallman, Joseph Daniel and vFinance.com, Inc. (n/k/a vFinance, Inc.) (Incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed with the SEC on August 14, 2001).
- 10.12 Stock Purchase Warrant, dated August 15, 2001, issued to Kathleen Wallman (incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed with the SEC on August 14, 2001).
- 10.13 Note Purchase Agreement by and between vFinance.com, Inc. d/b/a vFinance, Inc. (n/k/a vFinance, Inc.) and Best Finance Investments Limited (n/k/a SBI Investments (USA), Inc.) dated November 28, 2001 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).

Edgar Filing: VFINANCE INC - Form 10KSB

- 10.14 Letter Agreement dated November 30, 2001 amending Note Purchase Agreement (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.15 Letter Agreement dated December 14, 2001 amending Note Purchase Agreement (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.16 Letter Agreement dated December 28, 2001 amending Note Purchase Agreement (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.17 Letter Agreement dated February 13, 2002 amending Note Purchase Agreement (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.18 Letter Agreement dated March 4, 2002 amending Note Purchase Agreement (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.19 Credit Facility by and between the Company and UBS Americas, Inc. dated as of January 25, 2002 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.20 Subordination Agreement by and among the Company, UBS Americas, Inc., and SBI Investments (USA), Inc. dated as of January 25, 2002 (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.21 Consulting Agreement effective as of August 20, 2001 by and between vFinance.com, Inc. and Insight Capital Consultants Corporation (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.22 Amendment to Credit Agreement dated April 12, 2002 by and between the Company and UBS Americas Inc. (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC April 16, 2002).
- 10.23 Selected Asset Purchase Agreement dated as of May 29, 2002 among vFinance Investments, Inc., Somerset Financial Partners, Inc., Somerset Financial Group, Inc., Douglas Toth and Nicholas Thompson (the "Select Asset Purchase Agreement") (incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed with the SEC August 14, 2002).
- 10.24 Amendment to Select Asset Purchase Agreement dated June 17, 2002 (the "Amendment") (incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed with the SEC August 14, 2002).
- 10.25 Escrow Agreement executed in conjunction with the Amendment (incorporated by reference to the Company's Quarterly Report on Form 10-QSB filed with the SEC August 14, 2002).
- 10.26 Termination Agreement (incorporated by reference to the Company's Quarterly Report on Form 10-QSB/A filed with the SEC November 14, 2002).

Edgar Filing: VFINANCE INC - Form 10KSB

- 10.27 Branch Agreement between the Company and JSM Holding Corp (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC March 31, 2003).
- 10.28 Lease agreement on the Company's headquarters in Boca Raton, FL. dated January 1, 2003 between the Company and Zenith Professional Center, LTD. (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC March 30, 2004).
- 10.29 Stock warrant agreement between the Company and Zenith Professional Center, LTD. (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC March 30, 2004).
- 10.30 Asset Purchase Agreement, dated November 2, 2004, by and between vFinance Investments Holdings, Inc. and Global Partners Securities, Inc. (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC November 8, 2004).
- 63-
- 10.31 Stock Purchase Agreement, dated November 2, 2004, by and between vFinance Investments Holdings, Inc. and Level2.com, Inc. (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC November 8, 2004).
- 10.32 Registration Rights Agreement, dated November 2, 2004, by and among vFinance, Inc., Global Partners Securities, Inc. and Level2.com, Inc. (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC November 8, 2004).
- 10.33 Form of Common Stock Purchase Warrant (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC November 8, 2004).
- 10.34 Stock Escrow Agreement, dated November 2, 2004, by and among vFinance Investments Holdings, Inc., the Company, Global Partners Securities, Inc., Level2.com, Inc., and Edwards & Angell, LLP (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC November 8, 2004).
- 10.35 Standstill Agreement, dated November 2, 2004, by and among vFinance, Inc. and each of Marcus Konig, Harry Konig and Salomon Konig (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC November 8, 2004).
- 10.38* Amended and Restated Letter Agreement dated January 14, 2005 between the Company and Sheila C. Reinken (incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC January 21, 2005).
- 14 Code of Ethics (incorporated by reference to the Company's Annual Report on Form 10-KSB filed with the SEC March 30, 2004).
- 21 List of Subsidiaries
- 31.1 Certification by Chief Executive Officer pursuant to Section 302

Edgar Filing: VFINANCE INC - Form 10KSB

of the Sarbanes-Oxley Act of 2002.

31.2 Certification by Chief Financial Officer pursuant to Section 1350 of the Sarbanes-Oxley Act of 2002.

32.1 Certification by Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification by Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley act of 2002.

* Management contract or compensatory plan or arrangement

-64-

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

During 2005 and 2004, the Company incurred the following fees for professional services rendered by our principal accountant Sherb & Co., LLP:

| | 2005 | 2004 |
|--------------------|------------|-----------|
| Audit Fees (1) | \$ 107,985 | \$101,000 |
| Audit-related Fees | - | - |
| Tax Fees (2) | \$ 27,500 | \$ 10,000 |
| All Other Fees | - | - |

(1) Audit Services for 2005 included the annual audit, the reviews of the Company's quarterly reports on Form 10-QSB, fees related to filings with the Securities and Exchange Commission ("SEC") and accounting consultations. Before any audit or non-audit services are performed by any independent accountant, such services must be approved in advance by the Company's board of directors.

(2) Fees for tax services for 2005 and 2004 included the preparation of federal income tax returns and other tax related matters.

Edgar Filing: VFINANCE INC - Form 10KSB

-65-

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

vFinance, Inc.

By: /s/ Leonard J. Sokolow

LEONARD J. SOKOLOW, DIRECTOR,
CHIEF EXECUTIVE OFFICER AND PRESIDENT

Date: March 31, 2006

In accordance with the Exchange Act, 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 | Capacity | Date |
|---|--|----------|
| ----- | ----- | ----- |
| /s/ Leonard J. Sokolow ----- Leonard J. Sokolow | Director, Chief Executive Officer and President (Principal Executive Officer) | March 31 |
| /s/ Sheila C. Reinken ----- Sheila C. Reinken | Chief Financial Officer and (Principal Financial and Accounting Officer) | March 31 |
| /s/ Timothy E. Mahoney ----- Timothy E. Mahoney | Director, Chairman of the Board and Chief Operating Officer | March 31 |

Edgar Filing: VFINANCE INC - Form 10KSB

INDEX OF DOCUMENTS FILED WITH THIS ANNUAL REPORT

| Number of Exhibit ----- | Exhibit Description ----- |
|----------------------------|---|
| 21 | List of Subsidiaries |
| 31.1 | Certification by Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification by Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification by Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification by Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley act of 2002. |