MOBIVITY HOLDINGS CORP.
Form 10-Q
November 14, 2013

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

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

For the transition period from ___________ to __________

Commission file number 000-53851

Mobivity Holdings Corp.
(Exact Name of Registrant as Specified in Its Charter)

Nevada	26-3439095
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

58 W. Buffalo St. #200
Chandler, AZ 85225
(Address of Principal Executive Offices & Zip Code)

(866) 622-4261
(Registrant's Telephone Number)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

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

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

Large accelerated filer	[ ]	Accelerated filer	[ ]
Non-accelerated filer	[ ]	Smaller reporting company	[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]

As of November 8, 2013, the registrant had 97,900,105 shares of common stock issued and outstanding.

MOBIVITY HOLDINGS CORP.

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Explanatory Note

On November 12, 2013, Mobivity Holdings Corp. (the "Company") filed an amendment to its articles of incorporation on file with the Nevada Secretary of State for purposes of (i) effecting a reverse split of the issued and outstanding shares of its common stock at a ratio of one share for every six shares outstanding prior to November 12, 2013 and (ii) decreasing the authorized shares of its common stock to 50,000,000 shares. The reverse stock split was effective as of November 12, 2013. The reverse stock split effected a proportional decrease in the number of shares of common stock issuable upon the exercise of the Company's stock options and warrants outstanding immediately prior to the effective date of the reverse stock split, with a proportional increase in the exercise price. No fractional shares were issued as a result of the reverse stock split. In lieu of issuing fractional shares, the Company rounded all fractional interests resulting from the split up to the nearest whole number. The share information contained in this Quarterly Report on Form 10-Q does not give any effect to the reverse stock split.

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Part I - Financial Information

Item 1. Financial Statements

Mobivity Holdings Corp.
Condensed Consolidated Balance Sheets

ASSETS	September 30, 2013 (Unaudited)	December 31, 2012 (Audited)
Current assets		
Cash	$ 3,500,245	$ 363
Accounts receivable, net	502,420	414,671
Other current assets	123,600	30,009
Total current assets	4,126,265	445,043
Goodwill	4,175,032	2,259,624
Intangible assets, net	1,651,692	444,112
Other assets	16,869	201,228
TOTAL ASSETS	$ 9,969,858	$ 3,350,007
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities		
Accounts payable	$ 561,792	$ 514,949
Accrued interest	16,117	321,368
Accrued and deferred personnel compensation	171,739	299,534
Deferred revenue - related party	-	35,262
Deferred revenue and customer deposits	173,422	181,731
Convertible notes payable, net of discount	-	2,857,669
Notes payable	20,000	171,984
Derivative liabilities	237,098	3,074,504
Other current liabilities	109,181	250,144
Earn-out payable	80,369	2,032,881
Total current liabilities	1,369,718	9,740,026
Non-current liabilities		
Earn-out payable	143,631	-
Total non-current liabilities	143,631	-
Total liabilities	1,513,349	9,740,026
Commitments and Contingencies (See Note 9)		
Stockholders' equity (deficit)		
Common stock, $0.001 par value; 150,000,000 shares authorized; 97,811,977 and 23,218,117 shares issued and outstanding	97,812	23,218
Equity payable	100,862	-
Additional paid-in capital	54,786,355	25,412,932
Accumulated deficit	(46,528,520)	(31,826,169)
Total stockholders' equity (deficit)	8,456,509	(6,390,019)
	$ 9,969,858	$ 3,350,007

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)

See accompanying notes to condensed consolidated financial statements (unaudited).

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Mobivity Holdings Corp.
Condensed Consolidated Statements of Operations
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Revenues				
Revenues	$ 1,035,952	$ 1,006,262	$ 3,149,555	$ 3,028,866
Cost of revenues	268,507	307,061	864,519	1,007,288
Gross margin	767,445	699,201	2,285,036	2,021,578
Operating expenses				
General and administrative	1,324,355	636,322	2,644,677	2,350,850
Sales and marketing	1,491,563	406,815	3,289,904	1,135,934
Engineering, research, and development	214,374	156,156	465,614	452,129
Depreciation and amortization	89,133	130,579	181,262	431,962
Total operating expenses	3,119,425	1,329,872	6,581,457	4,370,875
Loss from operations	(2,351,980)	(630,671)	(4,296,421)	(2,349,297)
Other income/(expense)				
Interest income	385	252	406	2,821
Interest expense	(807)	(1,781,125)	(6,347,360)	(3,019,625)
Change in fair value of derivative liabilities	(51,913)	213,089	(3,865,511)	407,079
Gain (loss) on adjustment in contingent consideration	-	(157,943)	(193,465)	(81,161)
Total other income/(expense)	(52,335)	(1,725,727)	(10,405,930)	(2,690,886)
Loss before income taxes	(2,404,315)	(2,356,398)	(14,702,351)	(5,040,183)
Income tax expense	-	-	-	-
Net loss	$ (2,404,315)	$ (2,356,398)	$ (14,702,351)	$ (5,040,183)
Net loss per share - basic and diluted	$ (0.02)	$ (0.10)	$ (0.28)	$ (0.22)
Weighted average number of shares during the period - basic and diluted	97,290,179	23,215,481	52,247,033	23,019,643

See accompanying notes to condensed consolidated financial statements (unaudited).

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Mobivity Holdings Corp.
Condensed Consolidated Statement of Stockholders' Equity (Deficit)
(Unaudited)

	Common Stock Shares	Common Stock Dollars	Equity Payable	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity (Deficit)
Balance, December 31, 2012	23,218,117	$ 23,218	$ -	$ 25,412,932	$ (31,826,169)	$ (6,390,019)
Shares issued for Boomtext earn-out payment	1,483,669	1,484	-	2,209,183	-	2,210,667
Issuance of common stock for acquisitions	7,750,000	7,750	-	1,288,310	-	1,296,060
Issuance of common stock for cash, net of transaction costs of $602,823	37,500,000	37,500	-	6,859,677	-	6,897,177
Issuance of common stock for conversion of note principal and interest	26,772,532	26,773	-	5,327,733	-	5,354,506
Issuance of common stock and warrants for services	165,252	165	-	85,841	-	86,006
Issuance of common stock for allonge	527,679	528	-	130,720	-	131,248
Adjustment of derivative liability for note conversion	-	-	218,446	10,726,967	-	10,945,413
Adjustment of derivative liability for note repayment	-	-	-	40,511	-	40,511
Adjustment of derivative liability for non-employee warrant conversion	-	-	-	176,555	-	176,555
	236,292	236	(117,584)	117,348	-	-

Issuance of common stock and warrants for equity payable						
Issuance of common stock for accrued bonuses	115,625	116	-	36,884	-	37,000
Issuance of common stock for cashless exercise of warrants	42,811	42	-	23,862	-	23,904
Stock based compensation	-	-	-	2,349,832	-	2,349,832
Net loss	-	-	-	-	(14,702,351)	(14,702,351)
Balance, September 30, 2013	97,811,977	$ 97,812	$ 100,862	$ 54,786,355	$ (46,528,520)	$ 8,456,509

See accompanying notes to condensed consolidated financial statements (unaudited).

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Mobivity Holdings Corp.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Nine months ended September 30, 2013	2012
OPERATING ACTIVITIES		
Net loss	$ (14,702,351)	$ (5,040,183)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Bad debt expense	10,843	104,484
Common stock and warrants issued for services	86,006	270,000
Common stock issued for late payment	-	160,468
Stock-based compensation	2,349,832	314,990
Depreciation and amortization expense	181,262	431,962
Loss on adjustment in contingent consideration	193,465	81,161
Change in fair value of derivative liabilities	3,865,511	(407,079)
Amortization of deferred financing costs	-	239,943
Amortization of note discounts	6,134,367	2,551,161
Loss on sale of assets	-	164
Increase (decrease) in cash resulting from changes in:		
Accounts receivable	(71,125)	(208,898)
Other current assets	(88,091)	(200,915)
Other assets	27,999	1,540
Accounts payable	624	(432,694)
Accrued interest	64,535	195,225
Accrued and deferred personnel compensation	(90,795)	(25,312)
Deferred revenue - related party	(35,262)	(157,538)
Deferred revenue and customer deposits	(8,309)	12,984
Other liabilities	(3,325)	42,594
Net cash used in operating activities	(2,084,814)	(2,065,943)
INVESTING ACTIVITIES		
Purchases of equipment	(2,799)	(9,732)
Acquisitions	(400,000)	-
Net cash used in investing activities	(402,799)	(9,732)
FINANCING ACTIVITIES		
Proceeds from issuance of notes payable, net of finance offering costs	700,000	3,148,470
Payments on notes payable	(1,609,682)	(819,300)
Payments on cash payment obligation	-	(87,500)
Proceeds from issuance of common stock, net of issuance costs	6,897,177	-

Net cash provided by financing activities		5,987,495		2,241,670
Net change in cash		3,499,882		165,995
Cash at beginning of period		363		396
Cash at end of period	$	3,500,245	$	166,391
Supplemental disclosures:				
Cash paid during period for :				
Interest	$	146,973	$	33,108
Non-cash investing and financing activities:				
Debt discount from derivatives	$	4,614,714	$	2,733,412
Adjustment to derivative liability due to note repayment	$	40,511	$	69,332
Adjustment to derivative liability due to note conversion	$	10,726,967	$	1,020,859
Adjustment to derivative liability due to Allonge / ASID conversion	$	349,694	$	-
Adjustment to derivative liability due to non-employee warrant conversion	$	176,555	$	-
Issuance of common stock for cashless exercise of warrants	$	23,904	$	-
Issuance of common stock for Boomtext earn-out	$	2,210,667	$	-
Issuance of common stock for acquisitions	$	1,296,060	$	-
Issuance of common stock for accrued bonuses	$	37,000	$	-
Issuance of note payable for acquisition	$	1,365,096	$	-
Earn-out payable recorded for acquisition	$	224,000	$	-
Conversion of accrued interest into notes payable	$	-	$	137,649
Conversion of notes payable into common stock	$	4,984,720	$	-
Conversion of accrued interest into common stock	$	369,786	$	-
Settlement of working capital asset related to the Boomtext acquisition	$	153,317	$	-

See accompanying notes to condensed consolidated financial statements (unaudited).

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Mobivity Holdings Corp.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. Nature of Operations and Basis of Presentation

Mobivity Holdings Corp. ("Mobivity," "we" or "us" or "the Company") is in the business of developing and operating proprietary platforms over which resellers, brands and enterprises can conduct localized mobile marketing campaigns. Our proprietary platforms allow resellers, brands and enterprises to market their products and services to consumers through text messages sent directly to the consumers' mobile phones, mobile smartphone applications, or other solutions driven from consumers' mobile phones. We generate revenue by charging the resellers, brands and enterprises a per-message transactional fee, or through fixed or variable software licensing fees.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X promulgated by the Securities and Exchange Commission ("SEC"). Accordingly, they do not include all of the information and disclosures required by GAAP for annual financial statements. The accompanying unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 filed with the SEC on March 21, 2013.

In the opinion of management, such statements include all adjustments (consisting only of normal recurring items) which are considered necessary for a fair presentation of our condensed consolidated financial statements as of September 30, 2013, and for the three months and nine months ended September 30, 2013 and 2012. The results of operations for the three months and nine months ended September 30, 2013 are not necessarily indicative of the operating results for the full year ending December 31, 2013.

On November 12, 2013, we filed an amendment to our articles of incorporation on file with the Nevada Secretary of State for purposes of (i) effecting a reverse split of the issued and outstanding shares of our common stock at a ratio of one share for every six shares outstanding prior to November 12, 2013 and (ii) decreasing the authorized shares of its common stock to 50,000,000 shares. The reverse stock split was effective as of November 12, 2013. The reverse stock split effected a proportional decrease in the number of shares of common stock issuable upon the exercise of our stock options and warrants outstanding immediately prior to the effective date of the reverse stock split, with a proportional increase in the exercise price. No fractional shares were issued as a result of the reverse stock split. In lieu of issuing fractional shares, we rounded all fractional interests resulting from the split up to the nearest whole number. The share information contained in this Quarterly Report on Form 10-Q does not give any effect to the reverse stock split. See Note 11.

2. Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. All significant intercompany balances and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with GAAP 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 expenses during the reporting period. Significant estimates used are those related to stock-based compensation, the valuation of the derivative liabilities, asset impairments, the valuation and useful lives of depreciable tangible and certain intangible assets, the fair value of common stock used in acquisitions of businesses, the fair value of assets and liabilities acquired in acquisitions of businesses, and the valuation allowance of deferred tax assets. Management believes that these estimates are reasonable; however, actual results may differ from these estimates.

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Derivative Financial Instruments

We do not use derivative instruments to hedge exposures to cash flow, market or foreign currency risks.

We review the terms of the common stock, warrants and convertible debt we issue to determine whether there are embedded derivative instruments, including embedded conversion options, which are required to be bifurcated and accounted for separately as derivative financial instruments. In circumstances where the host instrument contains more than one embedded derivative instrument, including the conversion option, that is required to be bifurcated, the bifurcated derivative instruments are accounted for as a single, compound derivative instrument.

Bifurcated embedded derivatives are initially recorded at fair value and are then revalued at each reporting date with changes in the fair value reported as non-operating income or expense. When the equity or convertible debt instruments contain embedded derivative instruments that are to be bifurcated and accounted for as liabilities, the total proceeds received are first allocated to the fair value of all the bifurcated derivative instruments. The remaining proceeds, if any, are then allocated to the host instruments themselves, usually resulting in those instruments being recorded at a discount from their face value.

The fair values of the derivatives are estimated using a Monte Carlo simulation model. The model utilizes a series of inputs and assumptions to arrive at a fair value at the date of inception and each reporting period. Some of the key assumptions include the likelihood of future financing, stock price volatility, and discount rates.

Revenue Recognition and Concentrations

Our “C4” Mobile Marketing and Customer Relationship Management (CRM) and Txtstation Control Center platforms are hosted solutions. We generate revenue from licensing our software to clients in our software as a service (SaaS) model, per-message and per-minute transactional fees, and customized professional services. We recognize license fees over the period of the contract, service fees as the services are performed, and per-message or per-minute transaction revenue when the transaction takes place. We recognize revenue at the time that the services are rendered, the selling price is fixed, and collection is reasonably assured, provided no significant obligations remain. We consider authoritative guidance on multiple deliverables in determining whether each deliverable represents a separate unit of accounting. As for the Mobivity and Boomtext platforms, which are both hosted solutions, revenue is principally derived from subscription fees from customers. The subscription fee is billed on a month to month basis with no contractual term and is collected by credit card for Mobivity and collected by cash and credit card for Boomtext. Revenue is recognized at the time that the services are rendered and the selling price is fixed with a set range of plans. Cash received in advance of the performance of services is recorded as deferred revenue.

We generate revenue from the Stampt App through customer agreements with business owners. Revenue is principally derived from monthly subscription fees which provide a license for unlimited use of the Stampt App by the business owners and their customers. The subscription fee is billed each month to the business owner. Revenue is recognized monthly as the subscription revenues are billed. There are no per-minute or transaction fees associated with the Stampt App.

During the three months ended September 30, 2013 and 2012, one customer accounted for 36% and 21%, respectively, of our revenues. During the nine months ended September 30, 2013 and 2012, one customer accounted for 32% and 10%, respectively, of our revenues.

Comprehensive Income (Loss)

Comprehensive income (loss) is defined as the change in equity during a period from transactions and other events and circumstances from non-owner sources. We are required to record all components of comprehensive income (loss) in the consolidated financial statements in the period in which they are recognized. Net income (loss) and other comprehensive income (loss), including foreign currency translation adjustments and unrealized gains and losses on investments, are reported, net of their related tax effect, to arrive at comprehensive income (loss). For the three months and nine months ended September 30, 2013 and 2012, the comprehensive loss was equal to the net loss.

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Net Loss Per Common Share

Basic net loss per share excludes any dilutive effects of options, shares subject to repurchase and warrants. Diluted net loss per share includes the impact of potentially dilutive securities. During the three month and nine month periods ended September 30, 2013 and 2012, we had securities outstanding which could potentially dilute basic earnings per share in the future, but were excluded from the computation of diluted net loss per share, as their effect would have been anti-dilutive.

Reclassifications

Certain amounts from prior periods have been reclassified to conform to the current period presentation.

Recent Accounting Pronouncements

In 2013, the Financial Accounting Standards Board ("FASB") issued new accounting guidance clarifying the accounting for the release of cumulative translation adjustment into net income when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. The new guidance is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2013. We do not anticipate that adoption of this new guidance will have a significant impact on our financial position, results of operations, or cash flows.

In 2013, FASB issued new accounting guidance clarifying the accounting for obligations resulting from joint and several liability arrangements for which the total amount under the arrangement is fixed at the reporting date. The new guidance is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2013. We do not anticipate that adoption of this new guidance will have a significant impact on our financial position, results of operations, or cash flows.

In January 2013, FASB issued new accounting guidance clarifying which instruments and transactions are subject to offsetting disclosure requirements. The new guidance addresses concerns that the scope of the prior disclosure requirements was overly broad and imposed unintended costs that were not commensurate with estimated benefits to financial statement users. In choosing to narrow the scope of the offsetting disclosures, FASB determined that it could make them more operable and cost effective for preparers while still giving financial statement users sufficient information to analyze the most significant presentation differences between financial statements prepared in accordance with GAAP and those prepared under IFRSs. The new guidance will be effective for fiscal periods beginning on, or after January 1, 2013. We do not anticipate that adoption of this new guidance will have a significant impact on our financial position, results of operations, or cash flows.

3. Acquisitions

Sequence Acquisition

In May 2013, we acquired certain assets of Sequence, LLC (“Sequence”) pursuant to an asset purchase agreement. Pursuant to the asset purchase agreement, we acquired all application software, URL’s, websites, trademarks, brands, customers and customer lists from Sequence. We assumed no liabilities of Sequence.

The purchase price consisted of: (1) $300,000 in cash; (2) 750,000 shares of our common stock valued based on the closing market price on the acquisition date at $183,750; and (3) twenty-four monthly earn-out payments consisting of 10% of the eligible monthly revenue subsequent to closing with a fair value of $224,000.

We completed the acquisition in furtherance of our strategy to acquire small, privately owned enterprises in the mobile marketing sector through an asset purchase structure. This acquisition was consistent with our purchase price model in which equity will represent most of the purchase price plus a small cash component and, in some cases, the assumption of specific liabilities.

The acquisition was accounted for as a business combination and we valued the assets acquired at their fair values on the date of acquisition. An independent valuation expert assisted us in determining these fair values. The assets of the acquired entity were recorded at their estimated fair values at the date of the acquisition.

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The allocation of the purchase price to the assets acquired based upon fair value determinations was as follows:

Merchant relationships	$ 181,000
Trade name	76,000
Developed technology	71,000
Goodwill	379,750
Total assets acquired	$ 707,750

The purchase price consisted of the following:

Cash	$ 300,000
Common stock	183,750
Earn-out payable	224,000
Total purchase price	$ 707,750

Pro forma results of operations were not included due to the investment test not reaching the level of a significant acquisition.

Front Door Insights Acquisition

In May 2013, we acquired certain assets and liabilities of Front Door Insights, LLC (“FDI”), pursuant to an asset purchase agreement. The assets and liabilities acquired from FDI consisted of cash on hand, accounts receivable, all rights under all contracts other than excluded contracts, prepaid expenses, all technology and intellectual property rights, accounts payable, and obligations under a commercial lease.

The purchase price consisted of: (1) $100,000 in cash; (2) a non-interest bearing promissory note in the principal amount of $1,400,000, which was discounted by $34,904; and (3) 7,000,000 shares of our common stock valued based on the closing market price on the acquisition date at $1,112,310.

The asset purchase agreement included a working capital adjustment pursuant to which the number of shares issuable to FDI would be increased, or decreased, in the event the working capital of FDI exceeds, or is less than, $10,000, respectively, as of the closing. The working capital adjustment due to us is $1,552, and the parties determined to settle this amount in cash.

The asset purchase agreement contains customary representations, warranties and covenants by the parties, including each party’s agreement to indemnify the other against any claims or losses arising from their breach of the asset purchase agreement. FDI and its members have also agreed that for a period of three years following the closing not to engage in the business of providing interactive mobile marketing platforms or services or to solicit the pre-closing clients, vendors or employees of FDI, except in each case on our behalf.

We completed the acquisition in furtherance of our strategy to acquire small, privately owned enterprises in the mobile marketing sector through an asset purchase structure. This acquisition was consistent with our purchase price model in which equity will represent most of the purchase price plus a small cash component and, in some cases, the assumption of specific liabilities.

The acquisition was accounted for as a business combination and we valued all assets and liabilities acquired at their fair values on the date of acquisition. An independent valuation expert assisted us in determining these fair values. The assets and liabilities of the acquired entity were recorded at their estimated fair values at the date of the acquisition.

During the three months ended September 30, 2013, we adjusted the liabilities assumed in the transaction, in accordance with the asset purchase agreement, from $162,886 to $46,219, which resulted in an increase in additional paid-in capital of $78,000 and a reduction of goodwill of $38,667.

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The allocation of the purchase price to assets and liabilities based upon fair value determinations was as follows:

Cash	$ 5,500
Accounts receivable	27,467
Contracts	813,000
Customer relationships	22,000
Developed technology	96,000
Non-compete agreement	124,000
Goodwill	1,535,658
Total assets acquired	2,623,625
Liabilities assumed	(46,219)
Net assets acquired	$ 2,577,406

The purchase price consists of the following:

Cash	$ 100,000
Promissory note, net	1,365,096
Common stock	1,112,310
Total purchase price	$ 2,577,406

The following information presents unaudited pro forma consolidated results of operations for the nine months ended September 30, 2013 as if the FDI acquisition described above had occurred on January 1, 2013, and the results of operations for the year ended December 31, 2012 as if the FDI acquisition described above had occurred on January 1, 2012. The following unaudited pro forma financial information gives effect to certain adjustments, including the increase in compensation expense related to additional head-count and amortization of acquired intangible assets. The pro forma financial information is not necessarily indicative of the operating results that would have occurred if the acquisition been consummated as of the date indicated, nor are they necessarily indicative of future operating results.

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Pro Forma Results of Operations for the Nine Months Ended September 30, 2013

Mobivity Holdings Corp.
Consolidated Statements of Operations
(Unaudited)

	Mobivity	FDI	Pro forma adjustments		Pro forma combined
Revenues					
Revenues	$ 3,149,555	$ 162,280	$ -		$ 3,311,835
Cost of revenues	864,519	54,371	-		918,890
Gross margin	2,285,036	107,909	-		2,392,945
Operating expenses					
General and administrative	2,644,677	71,720	-		2,716,397
Sales and marketing	3,289,904	4,888	229,258	(b)	3,524,050
Engineering, research, and development	465,614	87,994	-		553,608
Depreciation and amortization	181,262	-	68,469	(c)	249,731
Total operating expenses	6,581,457	164,602	297,727		7,043,786
Loss from operations	(4,296,421)	(56,693)	(297,727)		(4,650,841)
Other income/(expense)					
Interest income	406	-	-		406
Interest expense	(6,347,360)	(6,785)	-		(6,354,145)
Change in fair value of derivative liabilities	(3,865,511)	-	-		(3,865,511)
Gain (loss) on adjustment in contingent consideration	(193,465)	-	-		(193,465)
Total other income/(expense)	(10,405,930)	(6,785)	-		(10,412,715)
Loss before income taxes	(14,702,351)	(63,478)	(297,727)		(15,063,556)
Income tax expense	-	-	-		-
Net loss	$ (14,702,351)	$ (63,478)	$ (297,727)		$ (15,063,556)
Net loss per share - basic and diluted	$ (0.28)				$ (0.27)
Weighted average number of shares during the period - basic and diluted	52,247,033				55,824,239

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Pro Forma Results of Operations for the Year ended December 31, 2012

	Mobivity	FDI	Pro forma adjustments	Pro forma combined
Revenues				
Revenues	$ 4,079,745	$ 347,797	$ -	$ 4,427,542
Cost of revenues	1,300,325	183,819	-	1,484,144
Gross margin	2,779,420	163,978	-	2,943,398
Operating expenses				
General and administrative	2,984,531	155,568	-	3,140,099
Sales and marketing	1,562,520	45,292	1,541,050 (b)	3,148,862
Engineering, research, and development	562,459	199,953	-	762,412
Depreciation and amortization	549,151	-	178,509 (c)	727,660
Goodwill impairment	742,446	-	-	742,446
Intangible asset impairment	145,396	-	-	145,396
Total operating expenses	6,546,503	400,813	1,719,559	8,666,875
Loss from operations	(3,767,083)	(236,835)	(1,719,559)	(5,723,477)
Other income/(expense)				
Interest income	2,833	-	-	2,833
Interest expense	(4,559,564)	(4,105)	(234,115) (a)	(4,797,784)
Change in fair value of derivative liabilities	359,530	-	-	359,530
Gain on adjustment in contingent consideration	625,357	-	-	625,357
Total other income/(expense)	(3,571,844)	(4,105)	(234,115)	(3,810,064)
Loss before income taxes	(7,338,927)	(240,940)	(1,953,674)	(9,533,541)
Income tax expense	-	-	-	-
Net loss	$ (7,338,927)	$ (240,940)	$ (1,953,674)	$ (9,533,541)
Net loss per share - basic and diluted	$ (0.32)			$ (0.32)
Weighted average number of shares during the period - basic and diluted	23,069,669			30,069,669

Pro Forma Adjustments

The following pro forma adjustments are based upon the value of the tangible and intangible assets acquired as determined by an independent valuation firm.

(a) Represents interest expense and note discount amortization for notes payable issued in conjunction with the transaction.
(b) Represents salary, bonus and stock based compensation (year ended December 31, 2012) for headcount added in conjunction with the transaction.
(c) Represents amortization of intangible assets for the period.

4. Goodwill and Purchased Intangibles

Goodwill

The carrying value of goodwill at September 30, 2013 and December 31, 2012 was $4,175,032 and $2,259,624, respectively. Goodwill at September 30, 2013 includes $1,915,408 recorded as a result of two acquisitions in May 2013. See Note 3.

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Intangible assets

The following table presents details of our purchased intangible assets as of September 30, 2013 and December 31, 2012:

	Balance at December 31, 2012	Additions	Amortization	Balance at September 30, 2013
Patents and trademarks	$111,620	$-	$ (6,298)	$105,322
Customer contracts	78,765	813,000	(60,259)	831,506
Customer and merchant relationships	29,056	203,000	(27,921)	204,135
Trade name	30,588	76,000	(12,566)	94,022
Acquired technology	193,458	167,000	(52,775)	307,683
Non-compete agreement	625	124,000	(15,601)	109,024
	$444,112	$1,383,000	$ (175,420)	$1,651,692

The intangible assets are being amortized on a straight line basis over their estimated useful lives of one to twenty years.

During the nine months ended September 30, 2013, the following intangible assets were purchased with the following useful lives:

Sequence, LLC:

	Fair value	Useful Life
Merchant relationships	$ 181,000	12 years
Trade name	76,000	5 years
Developed technology	71,000	5 years

Front Door Insights LLC:

	Fair value	Useful Life
Contracts	$ 813,000	7 years
Customer relationships	22,000	12 years
Developed technology	96,000	5 years
Non-compete agreement	124,000	3 years

Amortization expense for intangible assets was $87,081 and $123,666 for the three months ended September 30, 2013 and 2012, respectively. Amortization expense for intangible assets was $175,420 and $411,664 for the nine months ended September 30, 2013 and 2012, respectively.

The estimated future amortization expense of our intangible assets as of September 30, 2013 is as follows:

Year ending December 31,	Amount
2013	$ 87,081
2014	319,268
2015	319,268
2016	245,281
2017	190,064
Thereafter	490,730
Total	$ 1,651,692

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5. Derivative Liabilities

Convertible notes payable and underlying warrants

As discussed in Note 6 under Bridge Financing, we previously issued convertible notes payable that provided for the issuance of warrants to purchase our common stock at a future date. The conversion term for the convertible notes was variable based on certain factors. The number of warrants to be issued was based on the future price of our common stock.

As of December 31, 2012 and through June 17, 2013, the number of warrants to be issued was indeterminate. Due to the fact that the number of warrants issuable was indeterminate, the equity environment was tainted and the fair value of all of the warrants underlying the convertible notes payable was recorded as a derivative liability. The fair values of the variable maturity conversion feature ("VMCO") and the additional share issuance feature ("ASID") were recorded as derivative liabilities on the issuance date.

On June 17, 2013, we converted all of the outstanding convertible notes payable into shares of our common stock, and issued the warrants underlying the convertible notes payable. At that time, the derivative liabilities related to the VMCO and ASID totaling $7,792,657 were reclassified to additional paid-in capital.

Private Placement Shares and Warrants

We completed a private placement in September 2011 for the sale of units consisting of shares of common stock and warrants to purchase our common stock. Both the common shares and the warrants contain anti-dilutive, or down round, price protection. We recorded derivative liabilities related to the down round price protection on the common shares and the warrants.

The down round price protection on the common shares expired in August 2012, and the down round price protection for the warrants terminates when the warrants expire or are exercised.

Allonge

As discussed in Note 6 under Bridge Financing, all note holders with convertible notes payable maturing in February 2012 extended the maturity date through May 2012. As consideration to the note holders for the extension of the maturity date, we provided allonges which consisted of the accrued interest on each convertible note payable as of January 31, 2012. The allonges were convertible into shares of common stock at the latest financing price. The value of the allonges was recorded as a derivative liability at the issuance date.

On June 17, 2013, the number of common shares issuable under the allonges was determined to be 527,679 and these shares were issued in July 2013.

Non-employee Warrants

As discussed in Note 7 under Warrants, we previously accounted for warrants issued to non-employees as derivative liabilities. On June 17, 2013, the equity environment was no longer tainted and the value of the derivative liabilities related to the non-employee warrants totaling $176,555 were reclassified to additional paid-in capital.

Summary

The fair values of our derivative liabilities are estimated at the issuance date and are revalued at each subsequent reporting date using a Monte Carlo simulation discussed below.

At September 30, 2013 and December 31, 2012, we recorded current derivative liabilities of $237,098 and $3,074,504, respectively, which are detailed by instrument type in the table below.

The net change in fair value of the derivative liabilities for the three months ended September 30, 2013 and 2012 was a loss of $51,913 and a gain of $213,089, respectively.

The net change in fair value of the derivative liabilities for the nine months ended September 30, 2013 and 2012 was a loss of $3,865,511 and a gain of $407,079, respectively.

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The following table presents the derivative liabilities by instrument type as of September 30, 2013 and December 31, 2012:

Derivative Value by Instrument Type	September 30, 2013	December 31, 2012
Convertible Bridge Notes	$ -	$ 2,850,085
Common Stock and Warrants	237,098	129,378
Non-employee Warrants	-	95,041
	$ 237,098	$ 3,074,504

The following table presents details of our derivative liabilities from December 31, 2012 to September 30, 2013:

Balance December 31, 2012	$3,074,504
Issuances in derivative value due to new security issuances of notes	4,614,714
Issuances in derivative value due to vesting of non-employee warrants	26,969
Adjustment to derivative liability due to note repayment	(40,511)
Adjustment to derivative liability due to note conversion into new notes	(3,152,786)
Adjustment to derivative liability due to note conversion into equity	(7,923,875)
Adjustment to derivative liability due to non-employee warrant conversion	(176,555)
Adjustment to derivative liability due to warrant exercises	(23,904)
Change in fair value of derivative liabilities	3,838,542
Balance September 30, 2013	$237,098

An independent valuation expert calculated the fair value of the compound embedded derivatives using a complex, customized Monte Carlo simulation model suitable to value path dependent American options. The model uses the risk neutral methodology adapted to value corporate securities. This model utilized subjective and theoretical assumptions that can materially affect fair values from period to period.

Key inputs and assumptions used in valuing our derivative liabilities are as follows:

For issuances of notes, common stock and warrants:

- Stock prices on all measurement dates were based on the fair market value
- Down round protection for dates prior to April 15, 2013 is based on the subsequent issuance of common stock at prices less than $0.50 per share and warrants with exercise prices less than $0.50 per share. Down round protection for dates between April 15, 2013 and June 17, 2013 is based on the subsequent issuance of common stock at prices less than $0.25 per share and warrants with exercise prices less than $0.25 per share. Thereafter, down round protection is based on the subsequent issuance of common stock at prices less than $0.20 per share and warrants with exercise prices less than $0.20 per share
- The probability of a future equity financing event triggering the down round protection was estimated at 100% for dates prior to June 17, 2013 and 0% for subsequent measurement dates
- Computed volatility ranging from 86.1% to 128.9%
- Risk free rates ranging from 0.05% to1.41%

For issuances of non-employee warrants through June 17, 2013:

- Computed volatility of 128.9%
- Risk free rates ranging from 0.30% to 0.66%
- Expected life (years) ranging from 2.48 to 3.27

See Note 9 for a discussion of fair value measurements.

6. Bridge Financing, Notes Payable, and Accrued Interest

Bridge Financing

Summary

Prior to June 2013, we issued 10% Senior Secured Convertible Bridge Notes Payable (“Bridge Notes” or “new Bridge Notes”) to various accredited investors, and then extended the due dates on the majority of the Bridge Notes several times. In June 2013, the outstanding principal of the Bridge Notes totaling $4,984,720 was converted into 24,923,602 shares of our common stock at $0.20 per share. We no longer have any outstanding Bridge Notes.

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The Bridge Notes contained variable maturity dates and additional share issuance obligations and we recorded discounts to the Bridge Notes for the VMCO and ASID. The discounts were amortized to interest expense over the term of the Bridge Notes using the effective interest method. We determined that the VMCO and the ASID represented embedded derivative features, and these were recorded as derivative liabilities. See Note 5.

We capitalized costs associated with the issuance of the Bridge Notes, and amortized these costs to interest expense over the term of the related Bridge Notes using the effective interest method.

The following table summarizes information relative to the outstanding Bridge Notes at December 31, 2012:

	December 31, 2012
Bridge notes payable	$4,342,418
Less unamortized discounts:	
VMCO	(481,390)
ASID	(1,003,359)
Bridge notes payable, net of discounts	$2,857,669

Following is a detailed discussion of the Bridge Notes transactions.

2012

As of January 1, 2012, the principal balance on our outstanding Bridge Notes totaled $1,062,500. The principal balance and accrued interest was due on the earlier of (i) the date we completed a financing transaction for the offer and sale of shares of common stock (including securities convertible into or exercisable for its common stock), in an aggregate amount of no less than 125% of the principal amount (a qualifying financing), and (ii) February 2, 2012. If the Bridge Notes were held to maturity, we would have paid, at the option of the holder: i) in cash or ii) in securities to be issued by us in the qualifying financing at the same price paid by other investors. The Bridge Notes were secured by a first priority lien and security interest in all of our assets.

In January 2012, we issued additional Bridge Notes in the aggregate principal amount of $520,000. These Bridge Notes were due February 2, 2012 and contained the same rights and privileges as the previously issued Bridge Notes.

In March 2012, we repaid Bridge Notes totaling $65,000.

In April 2012, all note holders with Bridge Notes maturing on February 2, 2012 extended the maturity date through May 2, 2012. As consideration to the note holders for the extension of the maturity date, we provided allonges which consisted of the accrued interest for each Bridge Note as of January 31, 2012, which are convertible into shares of our common stock at the latest financing price. The value of the allonges was recorded as a derivative liability. See Note 5.

In March 2012 and April 2012, we issued additional Bridge Notes in the aggregate principal amount of $220,100 with a due date of May 2, 2012. In May 2012, theses notes were cancelled and converted into new Bridge Notes discussed below.

In May and June 2012, we issued to a number of accredited investors our new Bridge Notes in the aggregate principal amount of $4,347,419, consisting of (i) $2,656,250 of new funds and (ii) $1,691,169 of principal amount and accrued interest due under our previously issued Bridge Notes that were cancelled and converted into new Bridge Notes. The new Bridge Notes accrued interest at the rate of 10% per annum.

The principal amount under the new Bridge Notes plus all accrued and unpaid interest was due on the earlier of (i) the date we completed a financing transaction for the offer and sale of shares of common stock (including securities convertible into or exercisable for its common stock), in an aggregate amount of no less than 125% of the principal amount (a qualifying financing), and (ii) October 15, 2012, which date, as described below, was later extended to April 15, 2013. Payments could have been made in cash, or, at the option of the holder of the new Bridge Notes, in securities to be issued by us in the qualifying financing at the same price paid for such securities by other investors. The new Bridge Notes were secured by a first priority lien and security interest in all of our assets.

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We also had the obligation to issue to the holders of the new Bridge Notes on the date that is the earlier of the repayment of the new Bridge Notes or the completion of the qualifying financing, at their option:

five year warrants to purchase that number of shares of common stock equal to the principal amount plus accrued interest divided by the per share purchase price of the common stock offered and sold in the qualifying financing (the offering price) which warrants were to be exercisable at the offering price and would include cashless exercise provisions commencing eighteen months from the date of issuance of the warrants if there is not at that time an effective registration statement covering the shares of common stock exercisable upon exercise of the warrants, or

that number of shares of common stock equal to the product arrived at by multiplying (x) the principal amount plus accrued interest divided by the offering price and (y) 0.33.

We granted piggy-back registration rights with respect to the securities to be issued in connection with the new Bridge Notes.

The new Bridge Notes further provided that in the event of a change of control transaction, the proceeds from such transaction must be used by us to pay to the holders of the new Bridge Notes, pro rata based on the amount of new Bridge Notes owned by each holder, an amount equal to 1.5 times the amount of the aggregate principal amount outstanding under the new Bridge Notes, plus accrued interest due there under, plus all other fees, costs or other charges due there under.

The holders of the new Bridge Notes were also granted the right to appoint two designees to serve as members of our board of directors, which members will also serve as members of the Compensation Committee and the Audit Committee of our board of directors.

We used $184,081 from the proceeds of the sale of the new Bridge Notes to pay off existing principal balances under the Bridge Notes that were not cancelled and converted into the new Bridge Notes.

In October 2012 and continuing thereafter, we entered into amendments with the holders the new Bridge Notes. Under the terms of the amendments, the holders of new Bridge Notes in the aggregate principal amount of $4,342,419 agreed to extend the maturity date of the new Bridge Notes to April 15, 2013. In consideration of the new Bridge Note holders' agreement to extend the maturity date, the amendment provides that the holder shall have the option to convert the principal and interest under the new Bridge Note into the securities offered by us in a qualifying equity financing at the lower of (a) the same price paid for such securities by other investors investing in the financing or (b) $0.50 per share (subject to adjustment in the event of a stock split, reclassification or the like). Prior to the amendment, the conversion option under the new Bridge Note entitled the holder to convert the principal and interest under the new Bridge Note into the securities offered by us in a qualifying equity financing at the same price paid for such securities by other investors investing in the financing. The conversion price of $0.50 in (b) above triggered the price protection guarantee contained in the warrants issued in our 2011 private placement, and the exercise price on the warrants changed from $2.00 per share to $0.50 per share.

In November 2012, we repaid a new Bridge Note totaling $5,000.

2013

In January 2013, we partially repaid a new Bridge Note totaling $21,040.

In March 2013, we issued new Bridge Notes in the aggregate principal amount of $200,000 that contained the same rights and privileges as the previously issued new Bridge Notes.

In April 2013, we issued new Bridge Notes in the aggregate principal amount of $75,000 that contained the same rights and privileges as the previously issued new Bridge Notes.

In April 2013, we repaid a new Bridge Note totaling $36,659.

In April 2013, we issued a new Bridge Note to our Chief Financial Officer (“CFO”) totaling $20,000 that contained the same rights and privileges as the previously issued new Bridge Notes, the due date of which was extended to October 15, 2013.

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In May 2013, a majority of the new Bridge Note holders agreed to extend the maturity date of the new Bridge Notes to October 15, 2013 from April 15, 2013. In consideration of the new Bridge Note holders' agreement to extend the maturity date, the amendment provides that the new Bridge Note holders have the option to convert the principal and accrued interest under the new Bridge Note into the securities offered by us in a qualifying equity financing at the lower of (a) the same price paid for such securities by other investors investing in the financing or (b) $0.25 per share (subject to adjustment in the event of a stock split, reclassification or the like). Prior to the amendment, the conversion option under the new Bridge Notes entitled the new Bridge Note holders to convert the principal and accrued interest under the new Bridge Notes into the securities offered by us in a qualifying equity financing at the lower of (a) the same price paid for such securities by other investors investing in the financing or (b) $0.50 per share (subject to adjustment in the event of a stock split, reclassification or the like).

As a result of this amendment and the additional consideration given, the embedded derivative features in the Bridge Notes were revalued on April 15, 2013 to $4,052,148. We recorded new note discounts and derivative liabilities on April 15, 2013 based on the fair value of the derivative instruments. During the period from April 15, 2013 through June 17, 2013, the entire balance of the note discounts was amortized to interest expense as the conversion on June 17, 2013 triggered the immediate recognition of the full value of the debt discount.

In May 2013, we issued new Bridge Notes in the aggregate principal amount of $387,500 that contained the same rights and privileges as the previously issued and amended new Bridge Notes.

In May 2013, we issued a new Bridge Note to our Chief Executive Officer ("CEO") totaling $17,500 that contained the same rights and privileges as the previously issued and amended new Bridge Notes.

In June 2013, we completed a qualifying equity financing at $0.20 per share. See Note 7. Pursuant to the terms of the new Bridge Notes, we converted the principal amount of Bridge Notes totaling $4,984,720 into 24,923,602 shares of our common stock at $0.20 per share. Also, in June 2013, we converted accrued interest on the Bridge Notes totaling $369,786 into 1,848,930 shares of our common stock at $0.20 per share.

Certain note holders elected to receive cash payment for their accrued interest, and the remaining accrued interest on the Bride Notes of $95,404 was paid in July 2013.

Discounts recorded related to the Bridge Notes

We recorded discounts to the Bridge Notes for the VMCO and ASID. The discounts were amortized to interest expense over the term of the Bridge Notes using the effective interest method. All of the discounts related to the Bridge Notes were recognized as interest expense in June 2013 in conjunction with the conversion of the Bridge Notes into shares of our common stock.

We determined that the VMCO and the ASID represented embedded derivative features, and these were shown as derivative liabilities on the balance sheet. See Note 5.

The following table presents details of the discounts to our Bridge Notes from December 31, 2011 to September 30, 2013:

	VMCO	ASID	Total
December 31, 2011	$ (12,031)	$ (47,739)	$ (59,770)
Additions	(1,409,797)	(3,942,607)	(5,352,404)
Amortization	940,438	2,986,987	3,927,425
December 31, 2012	(481,390)	(1,003,359)	(1,484,749)

Additions	(1,936,191)	(2,678,523)	(4,614,714)
Amortization	2,417,581	3,681,882	6,099,463
September 30, 2013	$ -	$ -	$ -

During the three months ended September 30, 2013 and 2012, we recorded Bridge Note discount amortization to interest expense of $-0- and $1,528,438 respectively.

During the nine months ended September 30, 2013 and 2012, we recorded Bridge Note discount amortization to interest expense of $6,099,463 and $2,543,979, respectively.

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Deferred financing costs related to the Bridge Notes

We capitalized deferred financing costs and amortized the capitalized amounts to interest expense over the term of the Bridge Notes using the effective interest method.

During the three months ended September 30, 2013 and 2012, we recorded deferred financing cost amortization to interest expense of $-0- and $139,086, respectively.

During the nine months ended September 30, 2013 and 2012, we recorded deferred financing cost amortization to interest expense of $-0- and $239,943, respectively.

Digimark, LLC Notes

As partial consideration for the acquisition of Boomtext in 2011, we issued an unsecured subordinated promissory note in the principal amount of $194,658. The promissory note did not bear interest, was payable in installments (varying in amount) from August 2011 through October 2012, and was subordinated to our obligations under the Bridge Notes discussed above.

We recorded the promissory note at the present value of the payments over the subsequent periods which amounted to $182,460. We amortized the discount using the effective interest method.

As of December 31, 2012, the outstanding balance on the note payable was $100,000, which was paid in June 2013.

Summary of Notes Payable and Accrued Interest

The following table summarizes our notes payable and accrued interest as of September 30, 2013 and December 31, 2012:

	Notes Payable		Accrued Interest	
	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
Bridge notes, net, as discussed above	$-	$2,857,669	$-	$261,213
Convertible notes payable, net of discounts	-	2,857,669	-	261,213
Unsecured (as amended) note payable due to our Company's former Chief Executive Officer, interest accrues at the rate of 9% compounded annually, all amounts due and payable December 31, 2008. Currently past due.	20,000	20,000	16,117	13,775
Note payable due to a trust, interest accrues at the rate of 10% per annum, all amounts due and payable December 31, 2006.	-	51,984	-	24,297
Digimark, LLC subordinated promissory note, net, as discussed above.	-	100,000	-	22,083
Notes payable	20,000	171,984	16,117	60,155

Totals	$20,000	$3,029,653	$16,117	$321,368

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Interest Expense

The following table summarizes interest expense for the three months and nine months ended September 30, 2013 and 2012:

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Amortization of note discounts	$-	$1,530,412	$6,134,367	$2,551,161
Amortization of deferred financing costs	-	139,086	-	239,943
Other interest expense	807	111,627	212,993	228,521
	$807	$1,781,125	$6,347,360	$3,019,625

7. Stockholders' Equity (Deficit)

Common Stock

In May 2013, we issued: 750,000 shares of common stock as part of the purchase price in the Sequence acquisition which were valued at $183,750 based on the closing market price on the acquisition date, see Note 3; 7,000,000 shares of common stock as part of the purchase price in the FDI acquisition which were valued at $1,112,310 based on the closing market price on the acquisition date, see Note 3; and 1,483,669 shares of common stock in satisfaction of the Boomtext earn-out payment, see Equity Payable below.

In June 2013, we issued 36,780,000 shares of common stock at $0.20 per share to accredited investors for net proceeds of $6,789,686. Transaction costs netted against the proceeds totaled $566,315. This transaction constituted a qualified financing, pursuant to which the Bridge Notes were converted into 26,772,532 shares of common stock, see Note 6.

In June 2013, we also issued 75,000 shares of common stock for services and recorded general and administrative expense of $18,375.

In July 2013, we issued: 527,679 shares of common stock in satisfaction of the allonges granted under the Bridge Notes valued at $131,248; and 32,825 common shares for the cashless exercise of warrants and recorded a reduction to our derivative liabilities of $18,731.

In August 2013, we issued 720,000 shares of common stock at $0.20 per share to accredited investors for net proceeds of $107,492. Transaction costs netted against the proceeds totaled $36,508.

In August 2013, we also issued: 90,252 shares of common stock for services and recorded general and administrative expense of $51,444; 236,292 shares of common stock in satisfaction of our additional share issuance obligation under the Bridge Notes and reduced our equity payable by $96,960; 78,125 shares of common stock in satisfaction of the accrued bonus to our CEO of $25,000; 37,500 shares of common stock in satisfaction of the accrued bonus to our CFO of $12,000; and 9,986 shares of common stock for the cashless exercise of warrants and recorded a reduction of our derivative liabilities of $5,173.

At September 30, 2013, we had 97,811,977 shares of common stock outstanding.

Equity Payable

We had an earn-out commitment associated with the acquisition of Boomtext from Digimark, LLC. The earn-out payment (payable March 31, 2013) consisted of a number of shares of our common stock equal to (a) 1.5, multiplied by our net revenue from acquired customers and customer prospects for the twelve-month period beginning six months after the closing date, divided by (b) the average of the volume-weighted average trading prices of our common stock for the 25 trading days immediately preceding the earn-out payment (subject to a collar of $1.49 and $2.01 per share).

In June 2013, the final value of the earn-out payment of $2,210,667 was satisfied through the issuance of 1,483,669 shares of common stock. As of December 31, 2012, the estimated value of the earn-out payment of $2,032,881 was recorded as a current liability.

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In June 2013, we recorded equity payable of $218,446 related to the additional share issuance obligations under the Bridge Notes. As discussed above under Common Stock and below under Warrants Issued to Note Holders and Placement Agent, we satisfied a portion of these obligations during the three months ended September 30, 2013 through the issuance of shares of common stock or warrants to purchase common stock.

Stock-based Plans

Stock Option Activity

The following table summarizes stock option activity for the nine months ended September 30, 2013:

	Options
Outstanding at January 1, 2013	1,955,000
Granted	32,792,129
Exercised	-
Canceled/forfeited/expired	(408,334)
Outstanding at September 30, 2013	34,338,795

The weighted average exercise price of stock options granted during the period was $0.33 and the related weighted average grant date fair value was $0.29 per share.

The exercise of 32,317,129 options granted under our 2013 Plan was subject to our increasing the number of shares of common stock authorized for issuance, which took place on November 12, 2013 as a result of the one for six reverse stock split and accompanying decrease in our authorized common stock to 50,000,000 shares. See Note 11.

Stock-Based Compensation Expense

The impact on our results of operations of recording stock-based compensation expense for the three and nine months ended September 30, 2013 and 2012 was as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
General and administrative	$386,347	$84,886	$662,510	$248,911
Sales and marketing	656,396	19,217	1,656,052	54,083
Engineering, research, and development	3,081	458	5,056	11,996
	$1,045,824	$104,561	$2,323,618	$314,990

Valuation Assumptions

An independent valuation expert calculated the fair value of each stock option award on the date of grant using the Black-Scholes option pricing model. The following weighted average assumptions were used for the three months and nine months ended September 30, 2013 and 2012.

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Risk-free interest rate	1.82 %	0.57 %	1.27 %	0.52 %

Expected life (years)	6.17		3.58		5.57		3.37	
Expected dividend yield	0	%	0	%	0	%	0	%
Expected volatility	132.0	%	61.0	%	131.9	%	67.6	%

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The risk-free interest rate assumption is based upon published interest rates appropriate for the expected life of our employee stock options.

The expected life of the stock options represents the weighted-average period that the stock options are expected to remain outstanding and was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards, vesting schedules and expectations of future employee behavior as influenced by changes to the terms of its stock-based awards.

The dividend yield assumption is based on our history of not paying dividends and no future expectations of dividend payouts.

The expected volatility in 2013 is based on the historical publicly traded price of our common stock. The expected volatility prior to 2013 is based on the weighted average of the historical volatility of publicly traded surrogates in our peer group.

Warrants Issued to Non-Employees

We issued warrants to purchase 905,000 shares of common stock to non-employees in 2010 and 2011. Prior to June 17, 2013, the warrants were accounted for as derivative liabilities because the equity environment was tainted as discussed in Note 5. The equity environment was no longer tainted as of June 17, 2013, and our independent valuation expert began calculating the stock-based compensation for these warrants using the Black-Scholes valuation model. The valuation assumptions used are consistent with the valuation information for options above.

We recorded stock-based compensation expense of $26,214 in general and administrative expense for the three months ended September 30, 2013, and we recorded a gain of $133,120 in change in fair value of derivative liabilities for the three months ended September 30, 2013.

We recorded stock-based compensation expense of $26,214 in general and administrative expense for the nine months ended September 30, 2013, and we recorded a loss of $91,720 in change in fair value of derivative liabilities for the nine months ended September 30, 2013.

A summary of non-employee warrant activity under the 2010 Plan from December 31, 2012 to September 30, 2013 is presented below:

	Number Outstanding