



# **LIVEWIRE MOBILE, INC.**

**Quarterly Report**

**Three Months and Year Ended**

**December 31, 2012**

## **Livewire Mobile, Inc. Quarterly Report**

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## **Use of Non-GAAP Financial Measures**

In addition to reporting its financial results in accordance with generally accepted accounting principles in the United States, or GAAP, the Company has also provided in this quarterly report adjusted EBITDA from continuing operations, which is a non-GAAP financial measure adjusted to exclude certain non-cash and other specified expenses. The Company believes the use of non-GAAP measures in addition to GAAP measures is an additional useful method of evaluating its results of operations. Management uses these non-GAAP financial measures when evaluating the Company's financial results, as well as for internal planning and forecasting purposes. Specifically, the Company has excluded stock-based compensation, depreciation, amortization of intangible assets, debt discount and deferred financing costs, restructuring charges, interest income and expense, other income/expense, gains and losses on derivative accounting, and taxes from its non-GAAP financial measures. The non-GAAP financial measures disclosed by the Company should not be considered a substitute for, or superior to, financial measures calculated in accordance with GAAP, and the expected results calculated in accordance with GAAP and reconciliations to those expected results should be carefully evaluated. The non-GAAP financial measures used by the Company may be calculated differently from, and therefore may not be comparable to, similarly titled measures used by other companies. The Company may consider whether other significant non-recurring items that arise in the future should also be excluded in calculating the non-GAAP financial measures it uses. Reconciliations between the non-GAAP financial measures on a GAAP basis and a non-GAAP basis are provided herein, as applicable.

## **Net Operating Losses (NOLs) Protective Provisions**

During the third quarter of 2010, the Company received shareholder approval to amend its articles of incorporation in order to protect its NOLs (the "NOL Protective Measures") and those measures are now in effect. Under the NOL Protective Measures any person, company or investment firm that wishes to become a "5% shareholder" of Livewire Mobile, Inc. must first obtain a waiver from the Company's board of directors. In addition, any person, company or investment firm that is already a "5% shareholder" of Livewire Mobile, Inc. cannot make any additional purchases of Livewire Mobile, Inc. stock without a waiver from the Company's board of directors.

Livewire Mobile, Inc. strongly urges that any stockholder contemplating owning more than 185,000 shares contact the Company before doing so.

## **About Livewire Mobile, Inc.**

Livewire Mobile, Inc. (otcmarkets: LVWR) is a mobile internet powerhouse with one of the most comprehensive one-stop digital entertainment solutions for network operators, consumer device manufacturers, brands and media companies entering the mobile market. The Company's integrated suite of content services includes applications, video, games, ringback tones, ringtones, DRM-free full-track music, e-books and more as well as application and portal development, mobile advertising solutions, integrated content publishing and merchandising, and turnkey managed VAS operations. For more information, please visit [www.livewiremobile.com](http://www.livewiremobile.com).

Livewire Mobile is a registered service mark of Livewire Mobile, Inc. Other trademarks are properties of their respective owners.

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**LIVEWIRE MOBILE, INC.**  
**Condensed Consolidated Balance Sheet**

	December 31,	
	2012	2011
	(unaudited)	
	(In thousands except per share data)	
<b>ASSETS</b>		
Current assets:		
Cash	\$ 1,802	\$ 1,914
Restricted cash	150	-
Accounts receivable, net of allowance for doubtful accounts of \$34 and \$88, respectively	3,658	1,030
Inventories, net	295	241
Prepaid expenses and other assets	477	659
Total current assets	6,382	3,844
Property and equipment, net	975	1,247
Goodwill	2,047	1,959
Other intangibles, net	2,639	1,261
Other assets, net	105	259
Total assets	\$ 12,148	\$ 8,570
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>		
Current liabilities:		
Accounts payable	\$ 3,297	\$ 765
Accrued expenses and other liabilities	2,220	2,068
Accrued restructuring	-	166
Capital lease obligations, current portion	290	290
Deferred revenue	827	738
Convertible notes payable, net of debt discount of \$1,622 and \$580	3,993	1,070
Derivative liabilities	3,986	2,486
Total current liabilities	14,613	7,583
Convertible notes payable, net of debt discount of \$0 and \$1,108	-	357
Derivative liabilities	-	2,360
Other long term liabilities	150	142
Capital lease obligations, long term portion	91	253
Total liabilities	14,854	10,695
Stockholders' deficit:		
Preferred stock, \$0.05 par value, 300,000 shares authorized at December 31, 2012 and 2011	-	-
Common stock, \$0.01 par value, 72,500,000 shares authorized at December 31, 2012 and 12,500,000 shares authorized at December 31, 2011; 4,651,433 shares issued and outstanding at December 31, 2012 and 2011.	47	47
Additional paid-in capital	415,812	415,761
Accumulated deficit	(414,324)	(413,680)
Accumulated other comprehensive loss	(4,241)	(4,253)
Total stockholders' deficit	(2,706)	(2,125)
Total liabilities and stockholders' deficit	\$ 12,148	\$ 8,570

**LIVEWIRE MOBILE, INC.**  
**Condensed Consolidated Statements of Operations**

	Three Months Ended December 31,		Year Ended December 31,	
	2012	2011	2012	2011
	(Unaudited)			
	(in thousands except per share data)			
Service revenues	\$ 4,859	\$ 1,922	\$ 12,502	\$ 9,239
Product revenues	30	111	749	264
Total revenues	<u>4,889</u>	<u>2,033</u>	<u>13,251</u>	<u>9,503</u>
Total cost of revenues	<u>3,872</u>	<u>1,061</u>	<u>9,091</u>	<u>4,768</u>
Gross profit	1,017	972	4,160	4,735
	21%	48%	31%	50%
Operating expenses:				
Selling, general and administrative	1,418	1,407	5,538	6,252
Research and development	1,001	646	3,233	3,088
Restructuring and other related charges	-	86	37	377
Total operating expenses	<u>2,419</u>	<u>2,139</u>	<u>8,808</u>	<u>9,717</u>
Operating loss	(1,402)	(1,167)	(4,648)	(4,982)
Gain (loss) on derivative liabilities	6,282	(3,501)	3,360	(2,900)
Bargain purchase gain on business acquisition	-	-	3,698	-
Other expense, net	<u>(690)</u>	<u>(86)</u>	<u>(2,854)</u>	<u>(351)</u>
Income (loss) from continuing operations before income taxes	4,190	(4,754)	(444)	(8,233)
Income tax expense	<u>9</u>	<u>14</u>	<u>24</u>	<u>43</u>
Income (loss) from continuing operations	4,181	(4,768)	(468)	(8,276)
Loss from discontinued operations	<u>(112)</u>	<u>(25)</u>	<u>(176)</u>	<u>(142)</u>
Net income (loss)	<u>\$ 4,069</u>	<u>\$ (4,793)</u>	<u>\$ (644)</u>	<u>\$ (8,418)</u>
Income (loss) from continuing operations per common share - basic and diluted	<u>\$ 0.90</u>	<u>\$ (1.03)</u>	<u>\$ (0.10)</u>	<u>\$ (1.78)</u>
Net income (loss) per common share - basic and diluted	<u>\$ 0.87</u>	<u>\$ (1.03)</u>	<u>\$ (0.14)</u>	<u>\$ (1.81)</u>
Common shares - basic and diluted	<u>4,651</u>	<u>4,651</u>	<u>4,651</u>	<u>4,651</u>

**LIVEWIRE MOBILE, INC.**  
**Condensed Consolidated Statements of Cash Flows**

	Year Ended December 31,	
	2012	2011
	(Unaudited)	
	(In thousands)	
Cash flow from operating activities:		
Net loss	\$ (644)	\$ (8,418)
Adjustments to reconcile net loss to cash used in operating activities:		
Depreciation of property and equipment	702	737
Impairment of intangible assets	-	12
Amortization of intangible assets	368	258
Amortization of debt discount and deferred financing costs	2,679	298
Amortization of development costs	192	295
Stock-based compensation expense	51	70
(Gain) loss on derivative liabilities	(3,360)	2,900
Bargain purchase gain on business acquisition	(3,698)	-
Changes in operating assets and liabilities:		
Restricted cash	(150)	-
Accounts receivable	(2,610)	384
Inventories	(54)	53
Prepaid expenses and other assets	132	(439)
Accounts payable	2,523	(1,077)
Accrued expenses and other liabilities	(138)	(399)
Accrued restructuring	(166)	166
Deferred revenue	89	(317)
Cash used in operating activities	(4,084)	(5,477)
Cash flow from investing activities:		
Purchases of property and equipment	(75)	(11)
Cash from business acquisition	2,000	-
Cash provided by (used in) investing activities	1,925	(11)
Cash flow from financing activities:		
Proceeds from issuance of convertible notes	2,500	3,115
Payment of deferred financing costs	(37)	(145)
Payment of capital lease obligations	(339)	(370)
Cash provided by financing activities	2,124	2,600
Effect of exchange rate changes on cash	(77)	(37)
Net decrease in cash and cash equivalents	(112)	(2,925)
Cash and cash equivalents, beginning of period	1,914	4,839
Cash and cash equivalents, end of period	\$ 1,802	\$ 1,914
Supplemental cash flow information:		
Purchase of equipment through capital leases	\$ 185	\$ 247
<u>Schedule A - Acquisition of Business, Non Cash Assets Acquired</u>		
Non cash net assets acquired:		
Property and equipment	\$ 210	\$ -
Other intangibles	1,688	-
Accrued expenses and other liabilities	(200)	-
Net non cash assets acquired	\$ 1,698	\$ -

**LIVEWIRE MOBILE, INC.**  
**Unaudited Reconciliation of Non-GAAP Measures to Comparable GAAP Measures**

	Three Months Ended December 31,		Year Ended December 31,	
	2012	2011	2012	2011
	(Unaudited)			
	(In thousands, except per share data)			
GAAP operating loss	\$ (1,402)	\$ (1,167)	\$ (4,648)	\$ (4,982)
Plus:				
Stock-based compensation	9	13	51	70
Impairment of intangible assets	-	12	-	12
Amortization of intangibles	148	63	368	258
Amortization of development costs	84	34	192	295
Depreciation	212	160	702	737
Restructuring	-	86	37	377
Non-GAAP adjusted EBITDA from continuing operations	\$ (949)	\$ (799)	\$ (3,298)	\$ (3,233)
GAAP operating loss per basic and diluted share:	\$ (0.30)	\$ (0.25)	\$ (1.00)	\$ (1.07)
Plus:				
Stock-based compensation	-	-	0.01	0.02
Impairment of intangible assets	-	-	-	-
Amortization of intangibles	0.03	0.01	0.08	0.06
Amortization of development costs	0.02	0.01	0.04	0.06
Depreciation	0.05	0.04	0.15	0.15
Restructuring	-	0.02	0.01	0.08
Non-GAAP adjusted EBITDA from continuing operations per share	\$ (0.20)	\$ (0.17)	\$ (0.71)	\$ (0.70)
Shares used in computing basic and diluted non-GAAP adjusted EBITDA from continuing operations per share	4,651	4,651	4,651	4,651



## **NOTES:**

### **1) BASIS OF PRESENTATION**

The condensed consolidated balance sheets as of December 31, 2012 and 2011, the condensed consolidated statements of operations for the three months and years ended December 31, 2012 and 2011, and the condensed consolidated statements of cash flows for the years ended December 31, 2012 and 2011 include the unaudited accounts of Livewire Mobile, Inc. and its wholly owned subsidiaries (collectively, the "Company"). The financial information included herein is unaudited. The condensed consolidated balance sheet at December 31, 2011 has been derived from, but does not include all the disclosures contained in, the audited consolidated financial statements for the year ended December 31, 2011. Certain prior period amounts have been reclassified to conform to the current period's presentation.

In the opinion of management, all adjustments which are necessary to present fairly the financial position, results of operations and cash flows for all interim periods presented have been made. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, management evaluates various estimates including those related to the allowance for doubtful accounts and sales returns, write-down of excess and obsolete inventories to the lower of cost or market value, derivatives, valuation of long-lived assets including goodwill and intangible assets, income taxes, restructuring and other related charges, and accounting for acquisitions and dispositions. Management establishes these estimates based on historical experience and various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The operating results for the three months and years ended December 31, 2012 and 2011 are not necessarily indicative of the operating results to be expected for any future period.

The Company encourages you to read these financial statements in conjunction with its other public disclosures.

### **2) ACQUISITION**

Effective September 1, 2012, the Company closed an Asset Transfer and License Agreement with RealNetworks, Inc. (the "Agreement") whereby RealNetworks transferred to the Company services provided under two domestic carrier services contracts, together with a team of employees and associated hardware and software technology. As part of this transaction, RealNetworks paid the Company \$2.0 million at closing. Per the terms of the Agreement, the Company paid RealNetworks one payment of \$100,000 in September 2012 and established an accrued liability for a second payment of \$100,000 related to the performance of the services under one of these carrier contracts. Additionally, the Company recorded a bargain purchase gain of \$3,698,000 relating to the business acquisition in the quarter ending September 30, 2012.

The fair value of RealNetworks, Inc. business acquisition is allocated to identifiable tangible and intangible assets and liabilities assumed based on their fair values as of the date of the completion of the transaction. Based upon a third-party preliminary valuation at the acquisition date, the Company has allocated the purchase price to assets and liabilities as follows:

	<b>Amount (in 000's)</b>	<b>Estimated Life</b>
Fixed assets .....	\$ 210	9 months
Customer relationships .....	1,678	5.0 years
Content provider relationships.....	10	1.0 years
Total assets acquired .....	<u>1,898</u>	
Total liabilities assumed .....	<u>200</u>	
Fair value of net assets acquired.....	<u>\$1,698</u>	

The preliminary allocation was based upon a valuation for which estimates and assumptions are subject to change within the measurement period (up to one year from the acquisition date). The final allocation price could differ materially from the preliminary allocation. Any subsequent changes to the purchase price allocation may result in changes to the Company's consolidated financial results.

The RealNetworks, Inc. business acquisition was accounted for as a purchase business combination. Accordingly, the related results of operations were included with those of the Company for the period subsequent to the date of the acquisition.

On December 17, 2010, the Company's wholly-owned subsidiary, LWM Holdings, Inc. entered into a Share Purchase Agreement ("SPA") with Fonestarz Media Group, Ltd. ("Fonestarz"), whose operations are based in the United Kingdom, for a purchase price of \$952,000, excluding transactions costs of \$319,000. Transaction costs were recorded as operating expenses within the statement of operations in the fourth quarter of 2010, in accordance with generally accepted accounting principles. Additionally, the Company repaid approximately \$1,345,000 of Fonestarz liabilities at closing.

Included in accrued liabilities on the condensed balance sheet for the year ended December 31, 2011 is \$350,000 related to additional cash consideration that was contingent on certain conditions being met during the first twelve months subsequent to the closing of the acquisition. The \$350,000 was paid in full prior to December 31, 2012.

### **3) RESTRUCTURING AND OTHER RELATED CHARGES AND ACCRUALS**

In the first quarter of 2012, in order to reduce operating costs, the Company eliminated three employee positions which resulted in severance-related costs of approximately \$37,000, which were paid during the first quarter of 2012.

In the fourth quarter of 2011, in order to reduce operating costs, the Company eliminated a senior employee position which resulted in severance-related costs of approximately \$64,000 and restructured a lease for lab space at its corporate headquarters in Littleton, MA, resulting in a charge totaling \$22,000.

In the second quarter of 2011, in order to reduce operating costs, the Company eliminated 9 employee positions which resulted in severance-related costs of approximately \$48,000.

In the first quarter of 2011, to reduce costs associated with excess office space, the Company amended the lease for its corporate headquarters in Littleton, MA to reduce its

office space by approximately 37%, effective the earlier of April 1, 2011 or when the Company vacates the space. The Company vacated the excess space in February 2011. The Company recorded both a restructuring charge of \$222,000 and a rent expense reduction of approximately \$173,000 related to the elimination of a deferred rent liability associated with this exited space in the quarter ended March 31, 2011.

#### **4) DISCONTINUED OPERATIONS**

On December 5, 2008, the Company sold its NMS Communications Platforms business and certain assets and liabilities of the NMS Communications Platforms business to Dialogic Corporation. Accordingly, the operating results, including certain compliance and other administrative costs related to several foreign subsidiaries of the NMS Communication Platforms business, have been reclassified as discontinued operations in the unaudited condensed consolidated statements of operations.

#### **5) SECURED CONVERTIBLE NOTES PAYABLE**

On July 9, 2012, the Company closed debt funding totaling \$1,200,000 in senior secured convertible notes with three existing note holders. The notes mature in June 2013, bear interest at 10% per annum, and are convertible into common stock at any time at the option of the note holders at an initial conversion rate (subject to adjustment) of \$0.37 per common share. Quarterly interest on the new notes is earned from the date of issuance and is payable the first day of each following quarter, which began October 1, 2012.

In accordance with Accounting Standards Codification ("ASC") 815 "Derivatives and Hedging", and as more further described in Note 6 below, the Company recognized a debt discount of \$1,200,000 in connection with the issuance of the July 9, 2012 convertible notes. Total amortization of debt discount for the convertible notes amounted to \$328,000 and \$626,000 for the three months and year ended December 31, 2012, respectively, and is included in interest expense.

On May 2, 2012, the Company closed debt funding totaling \$800,000 in senior secured convertible notes with three existing note holders. The notes mature in June 2013, bear interest at 10% per annum, and are convertible into common stock at any time at the option of the note holders at an initial conversion rate (subject to adjustment) of \$0.37 per common share. Quarterly interest on the notes is earned from the date of issuance and is payable the first day of each following quarter, which began July 1, 2012.

In accordance with ASC 815, and as more further described in Note 6 below, the Company recognized a debt discount of \$800,000 in connection with the issuance of the May 2, 2012 convertible notes. Total amortization of debt discount for the convertible notes amounted to \$185,000 and \$490,000 for the three months and year ended December 31, 2012, respectively, and is included in interest expense.

On March 16, 2012, the Company closed debt funding totaling \$500,000 in senior secured convertible notes with three existing note holders. The notes mature in June 2013, bear interest at 10% per annum, and are convertible at any time at the option of the holder, into shares of common stock at an initial conversion rate (subject to adjustment) of \$0.37 per common share. The March 16, 2012 funding modified the conversion price of the senior secured convertible notes issued in June 2011 and December 2011 to \$0.37. Quarterly interest on the notes is earned from the date of issuance and is payable the first day of each following quarter, which began July 1, 2012.

In accordance with ASC 815, and as more further described in Note 6 below, the Company recognized a debt discount of \$500,000 in connection with the issuance of the March 16, 2012 convertible notes. Total amortization of debt discount for the convertible notes amounted to \$100,000 and \$317,000 for the three months and year ended December 31, 2012, respectively, and is included in interest expense.

On December 8, 2011, the Company closed debt funding totaling \$1,465,000 in senior secured convertible notes with four existing and one new note holder. The notes mature in June 2013, bear interest at 10% per annum and are convertible at any time at the option of the holder, into shares of common stock at an initial conversion rate of \$0.45 (subsequently adjusted to \$0.37) per common share. Quarterly interest on the notes is earned from the date of issuance and is payable the first day of each following quarter, which began April 1, 2012.

In accordance with ASC 815, and as further described in Note 6 below, the Company recognized a debt discount of \$1,133,000 in connection with the issuance of the December 8, 2011 notes. Total amortization of debt discount for the convertible notes amounted to \$204,000 and \$552,000 for the three months and year ended December 31, 2012, respectively, and is included in interest expense.

On June 10, 2011, the Company closed debt funding totaling \$1,650,000 in senior secured convertible notes with three longstanding and one more recent stockholder. The notes (including accrued interest) totaling approximately \$1,800,000 matured on December 10, 2012. The Company notified the note holders in accordance with the Note Purchase Agreement on that date indicating default and its inability to repay the notes. Pursuant to the Security Agreement that underlies the Note Purchase Agreement and related Notes, the lenders had remedies to the default including the rights to all of the Company's assets that secured the notes. At December 31, 2012, the Company was currently in discussions with the note holders to extend the maturity of the notes, and the terms of such extension were finalized in January 2013 – see the Subsequent Events footnote below.

In accordance with ASC 815, and as more further described in Note 6 below, the Company recognized a debt discount of \$813,000 in connection with the issuance of the June 10, 2011 convertible notes. Total amortization of debt discount for the convertible notes amounted to \$145,000 and \$580,000 for the three months and year ended December 31, 2012, and is included in interest expense.

Included in other assets, net, are deferred financing costs of approximately \$28,000 and \$106,000 respectively at December 31, 2012 and 2011 related to the issuance of the July 2012, May 2012, March 2012, December 2011, and June 2011 convertible notes. The deferred financing costs are amortized on the terms of such notes. Amortization of deferred financing costs amounted to \$32,000 and \$116,000 during the three months and year ended December 31, 2012, respectively, and is included in interest expense. Amortization of deferred financing costs amounted to \$19,000 and \$40,000 during the three months and year ended December 31, 2011, respectively, and is included in interest expense.

If the Company elects to defer payment of quarterly cash interest payments on any or all of the convertible notes when due, interest-in-kind is calculated at 12% per annum. For the quarters ending December 31, 2012, September 30, 2012 and June 30, 2012, interest was calculated at 12% per annum as the Company elected to defer payment of quarterly cash interest due on January 1, 2013, October 1, 2012 and July 1, 2012, respectively.

The notes are secured by all of the assets of the Company and contain certain operating and financial covenants applicable to the Company. At December 31, 2012, the Company was in compliance with its working capital covenant of its note purchase agreements.

## **6) DERIVATIVE LIABILITIES**

ASC 815 describes accounting for convertible instruments with provisions that protect holders from declines in the stock price ("down-round" provisions). Instruments with down-round protection are not considered indexed to a company's own stock under generally accepted accounting principles, because neither the occurrence of a sale of common stock by the company at market nor the issuance of another equity-linked instrument with a lower strike price is an input to the fair value of a fixed-for-fixed option on equity shares.

The Company has accounted for the embedded conversion feature of the notes described above as a liability in the financial statements at the estimated fair value of such embedded conversion feature, and records changes in fair value in results of operations.

### July 9, 2012 Notes:

Based on fair value computations, using the closing stock price on the closing date of the notes issuance on July 9, 2012, the Company recorded a derivative liability totaling \$1,319,000 and a loss on derivatives on the statement of operations of \$119,000 – the amount of the derivative liability that exceeded the value of the \$1,200,000 notes on the date of issuance.

The fair value of the derivative instruments were based on the following assumptions:

Conversion price: \$ 0.37  
Market price at date of grant: \$ 0.46  
Expected volatility: 316.5%  
Term: 11 months  
Risk-free interest rate: 0.20%

The change in the fair value of the derivative liabilities amounted to a decrease of \$1,462,000 for the three months ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations. The change in the fair value of the derivative liabilities from July 9, 2012 amounted to a decrease of \$348,000 and was recognized as a gain in derivative liabilities on the statement of operations for the year ended December 31, 2012.

### May 2, 2012 Notes:

Based on fair value computations, using the closing stock price on the closing date of the notes issuance on May 2, 2012, the Company recorded a derivative liability totaling \$990,000 and a loss on derivatives on the statement of operations of \$190,000 – the amount of the derivative liability that exceeded the value of the \$800,000 notes on the date of issuance.

The fair value of the derivative instruments were based on the following assumptions:

Conversion price: \$ 0.37  
Market price at date of grant: \$ 0.51  
Expected volatility: 298.5%  
Term: 13 months

Risk-free interest rate: 0.19%

The change in the fair value of the derivative liabilities amounted to a decrease of \$975,000 for the three months ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations. The change in the fair value of the derivative liabilities from May 2, 2012 amounted to a decrease of \$232,000 and was recognized as a gain in derivative liabilities on the statement of operations for the year ended December 31, 2012.

March 16, 2012 Notes:

Based on fair value computations, using the closing stock price on the closing date of the notes issuance on March 16, 2012, the Company recorded a derivative liability totaling \$681,000 and a loss on derivatives on the statement of operations of \$181,000 – the amount of the derivative liability that exceeded the value of the \$500,000 notes on the date of issuance.

The fair value of the derivative instruments were based on the following assumptions:

Conversion price: \$ 0.37  
Market price at date of grant: \$ 0.56  
Expected volatility: 286.13%  
Term: 15.5 months  
Risk-free interest rate: 0.24%

The change in the fair value of the derivative liabilities amounted to a decrease of \$609,000 for the three months ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations. The change in the fair value of the derivative liabilities from March 16, 2012 amounted to a decrease of \$145,000 for the year ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations.

December 8, 2011 Notes:

Based on fair value computations, using the closing stock price on the closing date of the notes issuance on December 8, 2011, the Company recorded a derivative liability totaling \$1,133,000.

The fair value of the derivative instruments were based on the following assumptions:

Conversion price: \$ 0.45  
Market price at date of grant: \$ 0.45  
Expected volatility: 197.39%  
Term: 18 months  
Risk-free interest rate: 0.16%

The change in the fair value of the derivative liabilities amounted to a decrease of \$1,786,000 for the three months ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations. The change in the fair value of the derivative liabilities from January 1, 2012 amounted to a decrease of \$1,320,000 for the year ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations.

June 10, 2011 Notes:

Based on fair value computations, using the closing stock price on the closing date of the notes issuance on June 10, 2011, the Company recorded a derivative liability totaling \$813,000.

The fair value of the derivative instruments were based on the following assumptions:

Conversion price: \$ 2.50

Market price at date of grant: \$ 2.80

Expected volatility: 86.76%

Term: 18 months

Risk-free interest rate: 0.30%

The change in the fair value of the derivative liabilities amounted to a decrease of \$1,450,000 for the three months ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations. The change in the fair value of the derivative liabilities from January 1, 2012 amounted to a decrease of \$1,315,000 for the year ended December 31, 2012 and was recognized as a gain in derivative liabilities on the statement of operations.

**7) Other Expense, Net**

Other expense, net includes the following for the stated periods:

	Three Months Ended		Year Ended	
	December 31,		December 31,	
	2012	2011	2012	2011
<b>(In thousands)</b>				
Interest expense	\$ (194)	\$ (67)	\$ (622)	\$ (159)
FX transaction loss	(1)	(37)	(16)	(43)
Change in estimate of contingent and acquired liabilities	523	168	523	168
Amortization of debt discount and deferred financing costs	(993)	(152)	(2,681)	(298)
Taxes and other	(25)	2	(58)	(19)
Other expense, net	<u>\$ (690)</u>	<u>\$ (86)</u>	<u>\$ (2,854)</u>	<u>\$ (351)</u>

Included above for the three months and years ended December 31, 2012 and 2011 is \$523,000 and \$168,000, respectively, of benefits relating to a change in estimate of liabilities relating to contingent obligations from Fonestarz, which was acquired in December 2010.

## **8) Legal Matters**

There are numerous patents covering technology in the ring back tone ("RBT") market: (i) which may infringe on the RBT patents held by the Company or (ii) which the holders thereof may claim the Company's RBT technology infringes on.

In September 2011 and November 2011, the Company received notices of request for indemnity from a customer in connection with the provision by the Company of RBT services. The complaints filed by two third-parties against the Company's customer involves a number of services offered by the customer that are claimed to be infringing on the third-parties' intellectual property ("IP"). Under the Company's agreement with the customer, the Company may be obligated to indemnify and defend it against damages and attorneys' fees in connection with valid IP claims related to the provision of our RBT services.

In November 2011 and February 2013, the Company received a notice of request for indemnity from a second and third customer, respectively, in connection with the provision by the Company of RBT services relating to claims made by one of the third-party complainants noted above.

In November 2011, the Company was sued by one of the third party complainants for patent infringement relating to certain RBT patents.

Given the current stage of these matters, we cannot predict the outcome of the matters nor estimate the possible loss or range of loss, if any, we could incur if there was an unfavorable outcome with respect to these claims and lawsuit. However, the Company believes that it has substantial legal and factual defenses to these claims and intends to defend its interests vigorously. Should the Company fail to prevail in any of these legal matters, its financial condition and results of operations could be materially adversely affected.

## **9) Shareholders Equity**

On April 30, 2012, the stockholders of Livewire Mobile, Inc. approved by consent an increase in the number of authorized shares of capital stock of the corporation from 12,800,000 shares to 72,800,000 shares, which included an increase in the number of authorized shares of common stock, \$0.01 par value, from 12,500,000 to 72,500,000 shares in accordance with an amendment to the Company's Fifth Restated Certificate of Incorporation.

## **10) Subsequent Events**

In January 2013, the Company closed an agreement with the holders of senior secured convertible notes with a maturity date of December 10, 2012 to forbear the exercise of their rights under the notes and extend the maturity until June 8, 2013. In exchange for the forbearance and extension, the Company issued warrants to the note holders for the purchase of up to 1,032,035 common shares, in the aggregate, of the Company's common stock at \$0.52 per share. The notes will continue to earn interest at 12% per annum during the forbearance period.

In January 2013, the Company paid approximately \$122,000 to the India Tax Department as a deposit on a portion of outstanding tax assessments to allow the Company's dormant Indian subsidiary to have its tax appeals heard for fiscal years ended March 31, 2007 and 2008. The \$122,000 represented the amount of outstanding transfer pricing tax



assessments for fiscal years ended March 31, 2007 and 2008. In addition to the transfer pricing assessments, the India Tax Department has disputed the Company's use of a tax holiday for fiscal years ending March 31, 2007 and 2008, challenging that proper documentation of intercompany transactions were supplied by the Company. Also, for fiscal year ending March 31, 2009, the Company has received a Show Cause Notice (a preliminary stage to a tax assessment) which is a rebuttal of the Company's transfer pricing amounts, which totaled approximately \$90,000. The total amount of tax claims (including the \$122,000 payment made in January 2013 and interest and penalties) is approximately \$980,000 (and subject to additional interest and penalties). The Board of Directors of the dormant subsidiary has vigorously disputed the validity of the tax claims. As the claims relate to a dormant entity with no assets or local operations, it is unclear what future actions the Government of India Income Tax Department may take. These estimated obligations have been accrued within the consolidated balance sheet as of December 31, 2012 to the extent of the \$122,000 deposit paid in January 2013, and recorded as a loss from discontinued operations in the condensed consolidated statement of operations for the three months and year ended December 31, 2012. Changes in the current status of the tax assessments from the Government of India Income Tax Department could materially and adversely impact the financial condition of the Company.

In February 2013, the Company closed debt funding totaling \$1,000,000 in senior secured convertible notes with three existing note holders. The notes mature on June 8, 2013, bear interest at 10% per annum (12% per annum if paid-in-kind) and are convertible into common stock at any time at the option of the note holders at an initial conversion rate (subject to adjustment) of \$0.46 per common share. The notes are secured by all of the assets of the Company and contain certain operating and financial covenants applicable to the Company. Quarterly interest on the new notes is earned from the date of issuance and is payable the first day of each following quarter, beginning April 1, 2013.

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