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nio®

Nio Security, Inc

ANNUAL REPORT

The Nio (Benevolent Kings) are a pair of protectors who stand guard outside the temple gate at most Japanese Buddhist temples, one on either side of the entrance. In Japan, the gate itself is often called the Nio-mon (literally Nio Gate). Their fierce and threatening appearance wards off evil spirits and keeps the temple ground free of demons and thieves. In some accounts, the Nio were said to have followed and protected the historical Buddha when he traveled throughout India. They have since been adopted by the Japanese into the Japanese Buddhist pantheon. Each is named after a particular cosmic sound. The open-mouthed figure is called "Agyo," who is uttering the sound "ah," meaning birth. His closed-mouth partner is called "Ungyo," who sounds "un" or "om," meaning death. Other explanations for the open/closed mouth include: (1) mouth open to scare off demons, closed to shelter/keep in the good spirits; (2) "Ah" is the first letter in the Sanskrit alphabet and "Un" is the last (same in Japanese syllabary too), so the combination symbolically represents all possible outcomes (from alpha to omega) in the cosmic dance of existence.

Letter from the CEO

- A Fresh Start

After a turbulent year, Nio Security is starting to get back on its feet. Our near future is still far from shining bright, but at least we are spotting light at the end of the tunnel.

2009 was our "annus horribilis". From 2007 Nio's revenues plunged by more than 75 per cent over a two-year period. Huge deficits almost drove the company over the edge. However, we succeeded in finding a way out of the imminent danger zone.
In my mind, we have come a long way in cleaning up and providing the company with a fresh start. In a major financial restructuring in November, Nio's debts were cleared and converted into equity. In this transaction the company became debt free and at the same time gained new main shareholders, who have assumed responsibility for Nio and entered the Board of Directors. Bringing vitality, professionalism and determination to the board room, the new main shareholders represent a significant reinforcement of the company.

The dire financial circumstances cannot overshadow the fact that Nio Security has the most sophisticated video surveillance equipment available. Our software has capabilities, which are generations ahead of our competitors' products. To be honest, being so far ahead of the market has been a disadvantage. And it was a direct cause of our lack of success in the past.

As far as the market is concerned, time is now on our side. The need for efficient and cost-effective surveillance is growing rapidly. Threats from crime and terrorism are moving closer and also the need for more innocent advanced surveillance, like traffic monitoring, is increasing. Traditional video surveillance has clear limitations and requires considerable manpower.
Also, the demand for live, crisp and dynamic video feed in a number of demanding applications apart from fixed surveillance is on the rise. For example in military and law enforcement operations, sports and aviation.

In this market environment we have products which do not only work to perfection, but also make a stunning impression on those who get to experience their performance. Using video language for a second, one could say that our products and the market's needs are in perfect sync for the first time.
In order to benefit from this situation, we are in the process of implementing a new distribution strategy.
While we in the past relied on a network of dealers reselling single components, we are now moving towards a broader distribution structure. In addition to our dealers we are addressing large security operators. They represent larger off takes and the ability to implement our solutions in their broad security offerings. Our ambition is to grow volumes in this sector, with a price structure benefiting both parties.
Our unique technology is also well suited for OEM arrangements, where Nio's software is embedded in our partner's product and marketed under his brand. The first OEM agreements are already operational.
We are confident that the versatility and pragmatism of our new distribution strategy will help build volumes in existing as well as new markets in Europe, the United States and Asia.

There is still plenty of hard work ahead and we do have to get out of bed quite early every morning to get the job done. But we do so more easily now than just a short while ago. We are determined to make the best of our fresh start.

Espen Brodin
Chairman & CEO

Products

To capture surveillance video that can be used in identifying objects like persons or vehicles, and documenting their movements, object tracking is an essential functionality. If the video capture is done solely by one or more stationary cameras, then either the field-of-view of a camera, or feature detail of its video will limit the usefulness.

Even for high resolution cameras the amount of usable detail in the area of interest will limit getting a clear picture of the situation. Pan-Tilt-Zoom (PTZ) cameras with optical zoom enable close scrutiny, but with the non-trivial challenge of steering the camera direction and zooming in an appropriate amount, while constantly watching for other moving objects. To a limited degree a person can do this, but alertness and attention to the task can only be effectively maintained for a brief span of time. Automating this task requires extensive algorithm and software development in the field of advanced Video Analytics. Many systems offer simplified solutions, like framing a portion of the video image and moving the frame following an object. Few offered systems are capable of giving detailed images with accurate and smooth tracking at high speed. Nio Security, Inc. has capitalized on many man years of advanced research and development, and has delivered the high quality solution.
Nio has two world leading products within the security market: CloseView™ and SteadyEye™.

The CloseView™ advanced video analytics appliance is a real-time video surveillance unit, designed by the computer vision experts of Nio, and is based on a highly optimized in-house developed embedded software into our hardware architecture. It allows attended and unattended operations for capturing Identification Video of the action in a scene, and supports leading PTZ camera models. Video from up to four wide-angled cameras are simultaneously watched, and when motion is detected in the field of view, it automatically directs the PTZ camera to zoom in and focus on the activity. In effect it works like a giga pixel camera where you can zoom in and get clear images with high resolution. There is little known competition with comparable performance to follow objects and close in on them. CloseView™ can identify multiple targets simultaneously, and sequentially move from target to target. In addition the CloseView™ unit deploys an alarm output to trigger recording, so faces and car licenses can be clearly and sharply captured in a video recording system for review and action. To maintain a smooth and accurate tracking with high-speed, agility of the system is essential. This means that the video to be analyzed should be captured from multiple wide-angle cameras without a delay, as e.g. the IP video compression step in IP cameras introduces. CloseView™ can also be configured remotely through an IP Network, either by uploading parameters or by adding a Video Server to actually see the picture while configuring.

The CloseView™ technology can operate fully automatically, but will also improve manual surveillance and make it more efficient due to the fact that suspicious objects are pointed out and followed. That is why, for example, the city of London, United States Army, Fed Ex, Airports and Schools/Universities are using Nio's technology.

SteadyEye™ is a world leading product in stabilizing camera movements, no matter if it is in a car, on a pole or in a plane. The uniqueness of this technology has guaranteed its usefulness and popularity in for example military drone planes and police cars.

Advanced Video Analytics software is the heart of Nio's technology, and Nio's core business is within the intelligent video surveillance market. Nio's initial products in this field were test launched in the market in 2003. To date, the products have achieved a positive response from commercial as well as military and government customers that require the best intelligent video surveillance capabilities to protect their critical infrastructure. Nio is considered the leader in automated PTZ camera control, implemented in the CloseView™ appliance, Nio's flagship product. To strengthen its control of PTZ cameras, Nio started developing own PTZ cameras in partnership with large PTZ manufacturers. These PTZ cameras, Interceptor™ and EyeMax™ are designed for optimal performance in combination with the CloseView™ appliance. In EyeMax™ the CloseView™ is integrated into one solid frame together with more than 2 reference cameras and a PTZ. This makes the installation and the calibration of the unit simpler.

The smart eye

Nio Security, Inc. redefines video surveillance and live video feed under extreme conditions. Our video software and products have unprecedented intelligent features and picture quality, providing our customers with more efficient and cost effective monitoring.

The need for sophisticated security solutions and advanced video transmission is growing rapidly. Nio's products are a perfect match for emerging and fast growing market demands.

After a period of financial distress, Nio has been refinanced and the organization totally restructured. New main shareholders and a new Board of Directors are now taking the company forward.

Nio Security, Inc.

- Board of Directors report 2009

Description of the Business

Nio Security, Inc. is a US software corporation incorporated in the state of Delaware with its registered address in Bokeelia, Florida, USA. Nio Security, Inc. is traded on the Oslo Stock Exchange with the ticker symbol "NIO". The Company has offices in Oslo (Norway), Memphis (Tennessee, USA) and Munich (Germany).

Nio represents the leading technology in intelligent video analysis and technology for the video surveillance industry. Nio works through a worldwide network of security integrators and OEM-partners. The Company has developed products and applications in the specific areas of video algorithm, digital video motion analysis, video compression and control. The company's software is embedded in the hardware in order to achieve the right speed of the solutions. This is contrary to Internet Protocol (IP) cameras, where the conversion of analogue signals delays the processing speed, making it difficult to for example follow a suspicious object by a moving pan tilt zoom (PTZ) camera, simply because the object will have moved on before the highly complex algorithms are completed which is necessary for a smooth tracking.

The basis for most of the Company's products is proprietary design software for complex video analytics used in motion estimation and video stabilization. Video stabilization is key to more efficient video encoding and better storage efficiency. Motion estimation is the basis for the Company's moving object detection and tracking products. The Company's focus for future product development of its proprietary video solutions will continue to be in the embedded Intelligent Video Surveillance space which is the fastest growing part of the security industry.

Nio has organized its sales and marketing efforts to operate effectively through distributors, OEM channels and the well-established distributor/manufacturer's representatives and system integrator channels. Specifically, the Company will use distributors for volume-oriented products and certified dealers and other partners for the more complex integration deals and higher-end products.

Although Nio has a strong focus on various video surveillance markets, its products and core technology can be further developed into other markets where the analysis of video or moving pictures is a necessary component.
As of December 31, 2009, Nio had 16 employees, whereof 12 were located in the US, one in Germany and three in Norway.

Financial Situation and Outlook

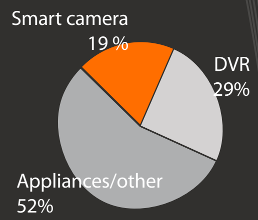
The Company experienced financial difficulties during 2009, hurting sales and overall development. Through 2009, the Board and management worked to rectify this situation, and in November 2009, the Company completed an extensive refinancing, securing new funding and comprehensive debt repayment.

The refinancing included a private placement of NOK 11 million from new investors and a conversion of its NOK 20.2 million secured short term loan into new shares. In addition, the Company entered into agreements with other creditors, resulting in a conversion of additional US$ 1.3 million of its accounts payable and accrued expenses, as well as a voluntary composition of other payables. Finally, the repayment of the two long term SBA loans on December 31, 2009, resulted in a full repayment of the Company's US$ 4.8 million secured and long term debt per December 31, 2009. The Company also initiated the close down of its San Diego operations the Tempest DVR product line has been discontinued, which has had a positive impact on operating expenses.

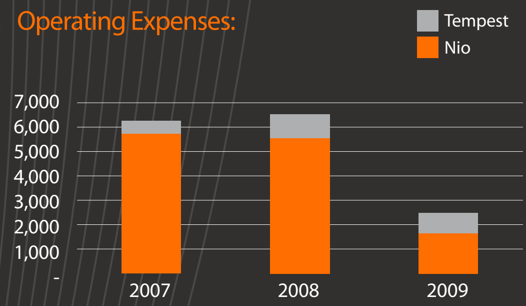
The Company has through the transactions and initiatives taken in the fourth quarter of 2009, significantly strengthened its balance sheet. This has improved Nio's ability to focus on building revenue in the fast growing security markets in America, Europe and Asia by selling Nio's existing products and improve Nio's ability to consider mergers and/or acquisitions and investigate new business opportunities. In the Board's opinion, the Company is well positioned for growth with a small and flexible operation in the worldwide, fast growing video surveillance market.

Due to the Company's financial difficulties in 2009, sales for the year was US$ 899,171 compared to US$ 2,282,383 for the year 2008. The Board of Directors believes that the refinancing and the subsequent initiatives taken to improve the Company's market

Segment Information:



Operating Expenses:



Gross Profit:

	Nio	Tempest	Total
Sales	636	263	899
CGS	281	327	607
Gross Profit	356	(64)	292
	56%	-24%	32%

position will significantly improve overall sales in 2010. The Company received an order for 600 units in February 2010 which was a milestone of proven technology and new distribution channels strategy, and is a significant first step towards break even operations.

Financial Performance

For the year 2009, sales were US$ 899,171, a decrease from US$ 2,282,383 in 2008. The decrease in sales is a result of the 2008-2009 economic downturn as well as reduced activity due to the Company's financial distress. As a consequence of the changes in the electronic components market, there is up to 30 weeks lead time for components used in Nio's products and the company's inability to finance manufacturing in 2009 affected sales volumes.

North America has been the primary market for Nio products, representing 88% of revenues in 2009, compared to 77% in 2008. The Company's core products, the appliances based on proprietary technology, contributed to 45% of sales in 2009. Smart cameras contributed to 19% and Tempest's DVR business 29%. The remaining 7% consists of licence fees, fixed cameras and other auxiliary products. CloseView is the single most important product, contributing to 32% of sales in 2009.

For the year 2009, the overall gross margin was 32%, and for Nio, exclusive of Tempest's DVR products, the gross margin was 56 % for the year 2009, compared to 39 % and 62 % for the year 2008 exclusive of Tempest's DVR products and some inventory write downs. Tempest's gross margins were weak due to generally lower margins on the DVR products and the allocation of the production facility's overhead expenses on a limited number of products manufactured. With the discontinuation of the DVR product range from January 2010, the Company expects a gross margin in excess of 50 % going forward.

For the year 2009, operating expenses was US$ 2,370,128, 64 % down from US$ 6,590,088 in 2008. Sales & Marketing expenses were 21% of total operating expenses, Research & Development 4% and general and administrative expenses 75%. All costs related to research and development have been expensed, in 2009 as well as in previous years.

The reduction in operating expenses is a result of initiatives taken in the second half of 2008 to significantly reduce the Company's monthly burn rate. With the closure of Tempest and San Diego operations effective in January 2010, operating expenses are at a low and acceptable level for the current operations.

Loss from operations was US$ 2,521.928 for the full year 2009, compared to US$ 8,122,076 in 2008, and net loss was US$ 4,897,583 for the full year 2009, compared to US$ 7,474,995 in 2008.

The Company's assets mainly consist of bank deposits, accounts receivables and inventory. Accounts receivables have been adjusted for all known uncollectible accounts. Current liabilities consist mainly of accounts payable and other current liabilities, all related to ongoing business.

Nio entered into a NOK 20,250,365 short term loan agreement with a group of lenders in December 2008, The loan had interest of 10% per annum, maturity on June 30, 2009, and had a first priority security interest in all of the Company's available intellectual property rights, including trademark and patents and the shares in Tempest. In June 2009, the maturity of the short term loan was extended until August 31, 2009 on the same terms, and thereafter the Company had a dialogue with the lenders to secure a refinancing of the Company. In November 2009, the Company finalized a refinancing, whereof the lenders under the short term loan agreement accepted to waive accrued interest and to convert the outstanding principal into share capital of the Company based on a conversion price of NOK 1.92 per share. As a result, liabilities were reduced by the US$ 3,629,523 short term loan balance.

In addition to the conversion of the short term loan, the Company entered into agreements with other creditors in November 2009, resulting in a conversion of additional US$ 1.3 million of its accounts payable and accrued expenses at a conversion price of NOK 1.92 per share, combined with a voluntary composition of other payables and short term debt. As a result, liabilities have been reduced by US$ 1,327,000, and a US$ 296,500 settlement gain has been booked under other income.

As a consequence of the board's decision to discontinue the Tempest DVR product line and to close down the Company's San Diego operations, goodwill, patents and trademarks related to the acquisition of Tempest as well as San Diego inventory has been written off in the fourth quarter of 2009, resulting in a US$ 1,858,412 loss under other expense.

From the acquisition of Tempest Microsystems Inc in 2007, the Company assumed the outstanding loan balance on the two SBA loans entered into in 2004 and 2006 by Tempest. On December 31, 2009, the Company entered into an agreement with California Bank & Trust regarding full prepayment of the Company's two long term SBA loans. As part of the agreement, the Company paid US$ 553,500 to the bank on December 31, 2009. In addition, the previous owner of Tempest, who was guarantor for the loans, paid the remaining US$ 553,500 and, in return, received certain assets. The two loans were paid in full as of December 31, 2009.

As of December 31, 2009, the Company had approximately US$ 40 million of net operating loss carry forwards, which expire at various dates beginning in the tax year 2012 through to 2029.The availability to offset income taxes in future years may be restricted if the Company undergoes an ownership change, which may occur as a result of future sales of any stock and other events. The Company has not valued the loss carry forwards in its balance sheet per December 31, 2009.

The Board of Directors confirms that the financial statements have been prepared based on the assumptions of a going concern. In our opinion, the consolidated financial statements present, in all material respects, the financial position of Nio Security, Inc. and subsidiaries as of December 31, 2009.

Accounting principles - IFRS

Nio's financial statements are prepared in conformity with US Generally Accepted Accounting Principles (US-GAAP) and on the going concern assumption. As a US registered company reporting in US-GAAP, Nio is not required to report in conformity with IFRS. The Company has, however, assessed the possible differences for its financial reporting between US-GAAP and IFRS and to the Company's knowledge; there would not be any significant changes to the financial statements under IFRS.

Tempest Microsystems was acquired in August 2007, and Tempest has been consolidated into the Company's financial statements from August 1, 2007.

Shareholder Matters

The Company concluded an Initial Public Offering in January 2005, with a listing of the Company's shares on the Oslo Stock Exchange, Norway. The Company's ticker symbol is "NIO".

As of January 1, 2009, the number of authorized shares in the Company was 30 million, whereof 23,079,797 were issued and outstanding, each with a par value of US$ 0.50.

At the Annual Meeting of Shareholders on June 2, 2009, it was resolved to amend the Company's Amended and Restated Certificate of Incorporation to reflect an increase in the Company's authorized shares from 30,000,000 to 70,000,000 shares of Common Stock, a change in the par value per share of the Company's Common Stock from fifty cents ($ 0.50) to ten cents ($ 0.10) and a reverse 10-for-1 stock split of the Company's Common Stock. In connection with the reversed stock split, Nio issued 258 new shares in June 2009 as compensation for fractional shares.

After the reversed stock split effective on June 8, 2009, the new number of issued and outstanding shares was 2,308,237, each with a par value of US$ 0.10. The financial statements and per share data in this annual report and the consolidated statements of income for the previous periods have been amended to reflect this change.

In November 2009, the Company completed a refinancing, including a private placement of NOK 11,000,000 at par value (USD 0.10) and a conversion of the NOK 20,250,365 short term loan and other debt at a share price of NOK 1.92. As a result, the Company issued a total of 33,669,804 new shares of its common stock during the fourth quarter of 2009. The number of outstanding shares was 35,978,041 per December 31, 2009. For the listing of the new shares, a prospectus was accepted by the Oslo Stock Exchange on December 17, 2009.

Nio has adopted stock option plans for its employees, consultants and directors, under which a total of 43,755 options were outstanding on January 1, 2009. During 2009, no options were granted or exercised and 3,129 options have expired. The total number of outstanding options under the Company's stock option plans was 40,626 at December 31, 2009.

In connection with the short term loan in December 2008, the Company issued 172,000 warrants to the lenders as compensation to participate in the loan. The warrants gave the lenders the right to purchase new shares in Nio at the price of NOK 10.00 per share, and expire on the maturity date of the new loan. These warrants were cancelled in November 2009 in connection with the repayment of the short term loan by way of conversion into new shares.

The investors in the private placement in November 2009 were granted warrants to purchase 15,000,000 shares at NOK 2.50 per share and 15,000,000 shares at NOK 5.00 per share which expire no later than December 31, 2012. In addition, 1,800,000 warrants to purchase shares at NOK 2.50 per share with expiry not later than December 31, 2012 were granted upon future allocation by the board of directors. As of December 31, 2009, a total of 31,800,000 warrants were outstanding, whereof 1,800,000 were allocated in February 2010.

Remuneration of the Board of Directors and management

As of January 1, 2009, the Company's Board of Directors consisted of three members, Mr. Ralph Carballal as Chairman, Mr. Espen Brodin and Mr. Bjarne Støtvig as directors. On April 28, 2009, Mr Carballal resigned from the Board of Directors, and the remaining board members, Mr. Brodin and Mr. Støtvig, continued to act as the Company's Board of Directors. In the Annual Meeting of Shareholders on June 2, 2009, Mr. Brodin and Mr. Støtvig were re-elected as the Company's Board of Directors with Mr. Brodin as Chairman.

As a Delaware, US registered company, and according to the Company's by-laws, the board members may, at its own discretion, elect new board members without a shareholder meeting. In a board meeting on November 18, 2009, Mr. Jon Skabo and Mr. Lars Moldestad were appointed as new board members, and since then, the Board of Directors has consisted of four members, Mr Brodin as Chairman and Messrs Støtvig, Skabo and Moldestad as board members.

Nio has compensated its board members with NOK 200,000 per year to the Chairman and NOK 100,000 per year to each of the other board members. For the year 2009, total compensation to the Board of Directors amounted to US$ 48,647. In addition, certain board members have been compensated for other consultancy work in addition to the normal board fee for a total amount of US$ 384,160 in 2009. Due to the difficult financial situation of the Company during 2009, no board compensation was paid to the board members prior to the refinancing, and a total of US$ 367,670 in accrued board fees and consultancy fees was converted into shares at a share price of NOK 1.92 in connection with the November 2009 refinancing.

None of the directors are entitled to any severance payment upon termination or expiration of their service as board members.

In December 2008, Mr. Michael Mojaver was appointed to the position of President and Chief Executive Officer of the Company. In August 2009, Mr. Brodin in his position as Chairman replaced Mr. Mojaver as the Company's CEO while Mr. Mojaver continued as the President of the Company. Mr. Mojaver has been compensated with US$ 180,000 in 2009.

Mr. Tore Formo, CFO, has been compensated with US$ 138,998 in 2009. Mr. Mojaver and Mr. Formo converted US$ 180,000 and US$ 89,764 respectively, into shares at a share price of NOK 1.92 in connection with the November 2009 refinancing. Finally, Dr. Dieter Koller, CTO up until November 2009 was compensated with US$ 63,507 in 2009.

The following table shows the number of shares, options and warrants held by the members of the Board of Directors and management of Nio and close associates or companies controlled by the Board of Directors or the management, as of December 31, 2009.

Members of the Board of Directors and CEO, as of December 31, 2009.

Name	Position	Compensation USD	No. of shares	No. of options	No. of warrants*
Espen Brodin	Chairman & CEO	204,447	0	0	0
Bjarne Støtvig	Director	221,095	680,829	0	0
Jon Skabo	Director	0	7,894,737	0	16,754,386
Lars Moldestad	Director	0	11,435,509	0	13,245,614
Michael Mojaver	President	180,000	1,915,302	0	0
Tore Formo	CFO	138,998	973,787	10,834	0

* In February 2010, Mr. Brodin, Mr. Formo and a company owned by close associates to Mr. Støtvig, were each allocated 600,000 warrants from the 1,800,000 warrants granted and held in escrow from the November 2009 refinancing.

The Board of Directors are:

Espen Brodin, Chairman & CEO

Mr. Brodin has a long international career from the banking and IT industry. He was Senior Vice President of one the largest bank in Norway, and co-founder and President and CEO of Fast Search & Transfer (FAST). Their Internet search is the core of Yahoo and Microsoft bought the company in January 2008. Mr. Brodin is serving as Board Member in various boards in Norway and abroad, and holds a Ph.D. in Philosophy.

Bjarne Støtvig, Executive Director

Mr. Støtvig has a long career from consultancy within real-estate, property management and IT industry. Furthermore, Mr. Støtvig has been working as a consultant for various companies both listed and unlisted in his fields financing, funding and organisational matters such as merger/acquisitions and serves as board member in various boards in Norway. Mr Støtvig holds a M.B.A. from Henley/Brunel University, London, UK and he is a Finnish Consul in Larvik, Sandefjord, Skien and Porsgrunn, Norway.

Lars Moldestad, Director

Mr. Moldestad has previously held the position as CEO (hired from Larsen Oil & Gas) in Petrolia Drilling Petrojack, Petromena and Petroprod Ltd. Mr. Moldestad has also previously worked for Finansbanken and Odfjell Drilling & Consulting Co. AS. Mr. Moldestad is educated from BI Norwegian School of Management.

Jon Skabo, Director

Mr. Skabo is currently partner in Skabo Offshore Ltd. From 2001 until 2006 Mr. Skabo was partner of S & T Energy N.V., from 1993 until 2001, partner of Jan Sundt AS, and from 1989 until 1993 shipbroker in Jan Sundt AS. Mr. Skabo's work experience includes involvement in the stock exchange listing of Safe Offshore ASA, Sævik Supply ASA, Havila Supply ASA and Deep Sea Supply ASA, work with new building of 15 FPSO's and Drilling Rigs, and sale of multiple second hand units.

Risk

The Company has suffered recurring losses from operations. The continuation of the Company as a going concern is dependent upon its ability to generate revenues and profits from the sale of its products and its ability to raise sufficient funding to meet any short-term needs. Despite the Company's recent initiatives, there is no assurance that the Company will become profitable in the immediate future, which could make it difficult to raise new capital if necessary.

The Company faces competition from existing competitors, as well as potential new competitors, which could result in loss of market share and diminished profits. The markets are characterized by technological advances, changes in customer requirements, and frequent new product introductions and enhancement. The Company's future success will depend mainly upon its ability to enhance its current products and to develop and introduce new products and services. In addition, there is risk associated with the marketing and sale of new products.

The Company is exposed to exchange rate fluctuations, with revenues mainly in USD and EUR and operating expenses divided between USD, NOK and EUR.

The Company's current technology and products are only to a limited degree covered by registered patents and patent applications, and the Company pursues a policy to protect its technology and products through trade secrets and know-how. If the Company fails to protect its intellectual prop-

May 7, 2010

Espen Brodin
(sign.)

Bjarne Støtvig
(sign.)

Jon Skabo
(sign.)

Lars Moldestad
(sign.)

Corporate governance

Nio Security, Inc. is a US public limited company incorporated in the State of Delaware, with its principle office in Bokeelia, Florida, USA. As a Delaware company, Nio is subject to Delaware company legislation and regulations. In addition, certain aspects of Norwegian Securities law apply to the company due to the listing on the Oslo Stock Exchange.

Due to the listing on the Oslo Stock Exchange, the Board of Directors has the ambition to follow the revised Norwegian recommendation for the Code of Practice for Corporate Governance, issued in October 2009, and aims to ensure compliance with all essential areas of this recommendation in areas where this may not yet have been achieved.

Adherence with the Code of Practice will be based on a comply- or explain-principle. If the Code of Practice is not complied with, an explanation shall be given as to why the company has elected another option. The Code of Practice contains 15 main points and the Company's operations are in all material respects in accordance with these. Below is a brief item-by-item account of the Company's adherence to the Code of Practice.

Implementation and reporting on corporate governance

The Code of Practice is complied with through regular board meetings, ordinary follow-up of operations, periodic press releases and statements in annual reports and other information distribution systems.

Business

The Code of Practice is complied with through the Company's articles of association and annual report. A description of the business is available on the Company's web pages. In short, Nio's goal is to be one of the leading Intelligent Video Systems providers in the worldwide market for video surveillance products. These goals, along with the strategic focal areas for attaining them, are described in more detail elsewhere in the annual report and on the Company's web site.

Equity and dividends

The Code of Practice is complied with and the Company has adopted a dividend policy under which, all else being equal, the Company would aim to pay a dividend according to continued self-imposed restrictions concerning financial solidity and liquidity, all of which should be complied with. To date, the Company has not paid any dividends to shareholders.

Nio's equity at 31 December 2009 amounted to US$ 500,193. Nio has a business model that requires relatively low capital other than operating expenses. The Board of Directors constantly assesses the Company's need for financial strength in the light of the Company's goals, strategy and risk profile, and are currently in the process to strengthen the Company's financial position. According to common practise for Delaware companies, the Company has an authorized number of shares available which is higher than the current number of issued shares. In compliance with the Company's by-laws and Delaware corporate law, the Board of Directors may issue shares up to this limit without shareholder approval.

Equal treatment of shareholders and transactions with close associates

The Code of Practice is complied with. The Company has only one class of shares. Under Delaware law, no pre-emption rights of existing shareholders exists, and the Company concluded a private placement in November 2009 to new investors as a consequence of the distressed financial situation.

Freely negotiable shares
The Code of Practice is complied with. The Company has no limitations on the ownership or sale of the Company's shares. All shares of Nio are freely negotiable and no form of restriction on negotiability is included in the Company's articles of association.

General meetings
The Code of Practice is in material respects complied with. Notices for shareholder meetings are sent by mail to all shareholders according to the Company's by-laws and articles of association. The annual general meeting ensures the shareholders' participation in the body that exercises the highest authority in the Company and in which the Company's articles of association are adopted.

Nomination committee
The Code of Practice in this instance is not complied with. As a Delaware corporation, the governing law does not require a nomination committee.

Corporate assembly and board of directors: composition and independence
The Code of Practice is in material respects complied with. The annual shareholders meeting elect representatives to the Board. The resolution on the composition of the Board takes place with a simple majority. The Company will seek to nominate representatives to the Board that are representing all shareholders and independent to management. Due to the size of the Company and difficulties in attracting interest from independent representatives due to the recent financial struggles, some of the current directors has also been part of the Company's management.

For the election of a new Board at the annual shareholder meeting in 2010, the proposal regarding its composition will be in line with the provisions in the Code of Practice. As a Delaware company, the board members has unlimited periods, but the board members will be proposed, elected and re-elected at the General assembly to be held annually. As a Delaware company, the Company does not have an independent election committee.

The work of the board of directors
The Code of Practice is complied with. The Board has the prime responsibility for the management of the Company and holds a supervisory position towards the executive management and the Company's activities. In addition to monitoring and advisory duties, the Board's main tasks consist of participating in compiling the Company's strategy. The Board appoints the CEO.

Risk management and internal control
The Code of Practice is complied with. The Board of Directors constantly assesses the Company's need for necessary internal control systems in the light of the size and complexness of the Company's business.

Remuneration to the board of directors
The Code of Practice is in material respects complied with. Remuneration to board members is at a sufficiently competitive level in order to ensure the desired composition of the board. The remuneration is a fixed amount and has no performance-related elements. The board members have warrants to purchase shares in the Company.

Remuneration of the executive management
The Code of Practice is complied with. The remuneration for the Chief Executive Officer is set by the Board. The Board also establishes guidelines for the remuneration of other members of the group management, including both the level of fixed salaries, the principles for and scope of bonus schemes and option grants. The Company has incentive stock option programs, which includes a vesting period. This program is described in the notes to the attached financial statement.

Information and communications
The Code of Practice is complied with. The Company assigns importance to informing its owners and investors about the group's development and economic and financial status. Prompt financial reporting reduces the possibility of leakage and contributes to the equal treatment of shareholders. Responsibility for investor relations (IR) and price sensitive information rests with the company's chief executive officer (CEO) and chief financial officer (CFO).

Take-overs

The Code of Practice is complied with. The board of directors is pragmatic with respect to a possible take over of the Company, and the main responsibility of the Board under such circumstances is to maximize value for the shareholders, while simultaneously looking after the interest of the company's employees and customers.

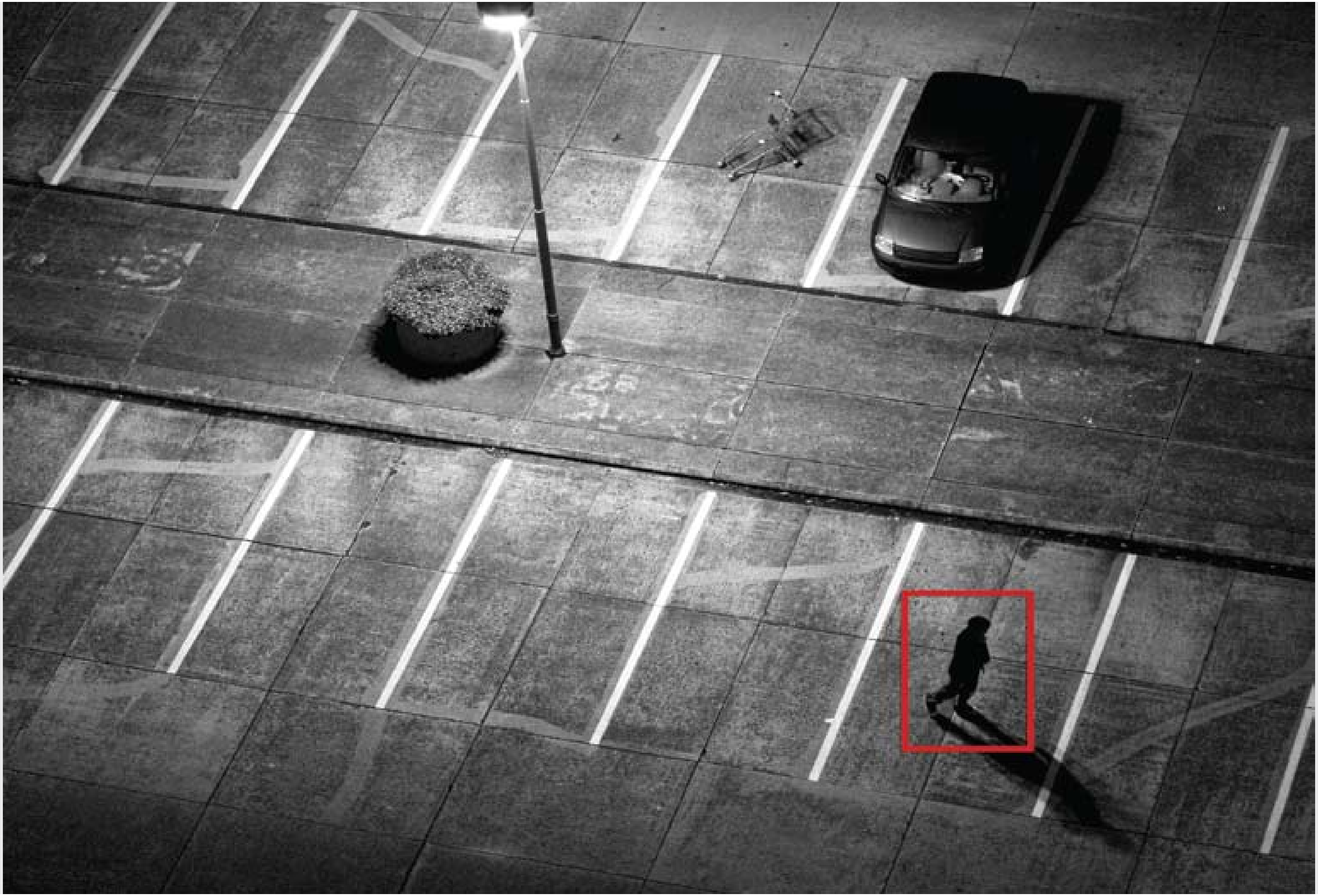
Auditor

The Code of Practice is complied with, but with the exception that there are no explicit specific guidelines for the management's opportunity to use the auditor for other services than audit. Nio uses the auditors as advisors for general financial purposes and in connection with the preparation of tax returns and tax advice generally. For the 2009 fiscal year, the auditors have not participated in the board meeting that approved the annual financial statements or presented to the board a review of its work and the Company's internal procedures. The auditor was paid US$ 54,839 for services in 2009.

Shareholders

The 20 largest shareholders as per May 7, 2010 hold 34,589,220 shares:

Name	Shares:	Percentage:
Lars Moldestad	11 435 509	31,8 %
Bellamare Resources Ltd.	8 016 235	22,3 %
Alba AS	4 265 413	11,9 %
SIX SIS AG	2 137 423	5,9 %
Michael Mojaver	1 915 302	5,3 %
Pål K. Fevang	1 704 971	4,7 %
Citibank N.A. nom.	688 696	1,9 %
Bawa AS	680 829	1,9 %
Tore Formo	654 483	1,8 %
MP Pensjon	409 980	1,1 %
Henrik Sundt	392 316	1,1 %
Viventus AS	319 854	0,9 %
Ralph Carballal	313 774	0,9 %
Ystholmen AS	309 129	0,9 %
Marit Formo	300 199	0,8 %
Joachim Nielsen	295 693	0,8 %
Helge Nielsen	289 896	0,8 %
Colon AS	279 589	0,8 %
Profilgest Management S.A.	100 000	0,3 %
Kristian Revne	80 000	0,2 %
Total 20 largest	34 589 291	96,1 %
Other	1 388 750	3,9 %
TOTAL	35 978 041	100,0 %



Independent auditors' report

The Board of Directors of Nio Security, Inc.

We have audited the accompanying consolidated balance sheet of Nio Security, Inc. and Subsidiary as of December 31, 2009 and 2008, and the related statements of operations and comprehensive loss, shareholders' equity (deficit) and cash flows for each of the years in the three-year period ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Nio Security, Inc. and Subsidiary as of December 31, 2009 and 2008, and the results of their operations and cash flows for each of the years in the three-year period ended December 31, 2009 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As set forth in the accompanying financial statements , the Company has incurred substantial losses in each of the last three years and has limited amounts of working capital and shareholders' equity at December 31, 2009. These factors raise substantial doubt about the Company's ability to continue as a going concern. As discussed in Note 1 to the financial statements, the continuation of the Company as a going concern is dependent upon its ability to raise sufficient funding to meet its short-term needs and its future ability to generate revenues and profits from the sale of its products. Management's plans to achieve these objectives are also described in Note 1. There is no assurance that the Company will be successful in these endeavors. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

May 7, 2010
Garden City, New York

Israeloff, Trattner & Co. P.C.
CERTIFIED PUBLIC ACCOUNTANTS · FINANCIAL CONSULTANTS
1225 Franklin Avenue, Garden City, NY 11530 (516) 240-3300 Fax (516) 240-3310 www.israeloff.com

Other Office
Empire State Building
350 Fifth Ave.
New York, NY

INDEPENDENT AUDITORS' REPORT

The Board of Directors
of Nio Security, Inc.

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Israeloff, Trattner & Co. P.C.

May 7, 2010
Garden City, New York

Nio Security, Inc. and Subsidiary
Consolidated balance sheet

December 31, 2009 and 2008

ASSETS	2009	2008
Current Assets:		
Cash and cash equivalents	$ 621,142	$ 705,139
Trade accounts receivable, net	55,963	149,491
Inventories	251,589	791,504
Other current assets	25,458	75,419
Total Current Assets	954,152	1,721,553
Other Assets:		
Property and equipment, net	37,492	304,747
Goodwill	-	669,788
Other intangible assets, net	-	1,401,429
Other assets	197,913	338,477
Total Other Assets	235,405	2,714,441
TOTAL ASSETS	$ 1,189,557	$ 4,435,994
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current Liabilities:		
Current maturities of long-term debt	$ 167,261	$ 832,350
Accounts payable	339,371	300,133
Liability for subsidiary insolvency	-	138,581
Accrued expenses and other current liabilities	182,732	165,725
Total Current Liabilities	689,364	1,436,789
Long-term debt and other liabilities subsequently converted to equity	-	4,754,336
Total Liabilities	689,364	6,191,125
COMMITMENTS AND CONTINGENCIES		
Shareholders' Equity (Deficit):		
Common stock, $ 0.10 par value, 70,000,000 shares authorized; 35,978,041 and 2,308,237 shares issued and outstanding, respectively	3,597,804	230,824
Additional paid-in capital	46,824,378	43,038,451
Accumulated deficit	(49,921,989)	(45,024,406)
Total shareholders' equity (deficit)	500,193	(1,755,131)
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 1,189,557	$ 4,435,994

See the accompanying notes to the consolidated financial statements.

Nio Security, Inc. and Subsidiary
Consolidated statement of operations and comprehensive loss

For the years ended December 31, 2007, December 31, 2008 and December 31, 2009

	2009	2008	2007
Sales	$ 899,171	$ 2,282,383	$ 3,773,382
Cost of sales	607,406	1,375,366	2,105,982
Gross profit	291,765	907,017	1,667,400
Operating expenses:			
Marketing, general and administrative	2,272,382	4,768,842	4,536,679
Research and development	97,746	1,821,246	1,656,509
Goodwill impairment	-	2,000,000	-
Interest expense	443,565	439,005	113,158
Foreign currency exchange losses (gains)	916,584	(552,630)	96,524
Total operating expenses	3,730,277	8,476,463	6,402,870
Loss before other income (expenses)	(3,438,512)	(7,569,446)	(4,735,470)
Other income (expenses):			
Loss on disposition of subsidiary assets	(1,858,412)	-	-
Gain on disposition of subsidiary	-	163,837	-
Other	399,341	(10,529)	(913)
Total other income (expenses)	(1,459,071)	153,308	(913)
Pre-tax loss	(4,897,583)	(7,416,138)	(4,736,383)
Provision for income taxes	-	14,648	22,137
Net loss	(4,897,583)	(7,430,786)	(4,758,520)
Other comprehensive income:			
Foreign currency translation adjustment	-	(44,209)	61,301
Comprehensive loss	$ (4,897,583)	$ (7,474,995)	$ (4,697,219)
Per share data:			
Basic and diluted net loss per share	$ (0.93)	$ (3.28)	$ (2.27)
Basic and diluted weighted average common shares outstanding	5,251,933	2,265,357	2,095,755

See the accompanying notes to the consolidated financial statements.

Nio Security, Inc. and Subsidiary
Consolidated statements of shareholders' equity (deficit)

For the years ended December 31, 2007, December 31, 2008 and December 31, 2009

	Common Stock Shares	Common Stock Amount	Paid-in Capital	Accumulated Deficit	Comprehensive Income (Loss)	Total Stockholders' Equity (Deficit)
BALANCES AT JANUARY 1, 2007	1,995,904	$ 199,590	$ 36,664,633	$ (32,835,100)	$ (17,092)	$ 4,012,031
Issuance of stock upon exercise of options	48,833	4,884	324,783	-	-	329,667
Sale of stock through private placement	63,500	6,350	1,462,911	-	-	1,469,261
Issuance of options to directors and employees	-	-	208,766	-	-	208,766
Issuance of stock to purchase subsidiary (net write off of goodwill)	100,000	10,000	2,241,542	-	-	2,251,542
Net loss	-	-	-	(4,758,520)	-	(4,758,520)
Unrealized foreign currency translation gain	-	-	-	-	61,301	61,301
BALANCES AT DECEMBER 31, 2007	2,208,237	$ 220,824	$ 40,902,635	$ (37,593,620)	$ 44,209	$ 3,574,048
Sale of stock through private placement	100,000	10,000	1,998,977	-	-	2,008,977
Issuance of options to directors and employees	-	-	136,839	-	-	136,839
Net loss	-	-	-	(7,430,786)	-	(7,430,786)
Unrealized foreign currency translation gain	-	-	-	-	(44,209)	(44,209)
BALANCES AT DECEMBER 31, 2008	2,308,237	230,824	$ 43,038,451	$ (45,024,406)	-	$ (1,755,131)
Issuance of stock upon conversion of debt	14, 371,558	1,437,156	3,831,356	-	-	5,268,512
Sale of stock through private placement	19,298,246	1,929,824	(71,517)	-	-	1,858,307
Issuance of options to directors and employees	-	-	26,088	-	-	26,088
Net loss	-	-	-	(4,897,583)	-	(4,897,583)
BALANCES AT DECEMBER 31, 2009	$ 35,978,041	$ 3,597,804	$ 46,824,378	$ (49,921,989)	-	$ 500,193

See the accompanying notes to the consolidated financial statements

Nio Security, Inc. and Subsidiary
Consolidated statements of cash flows

For the years ended December 31, 2007, December 31, 2008 and December 31, 2009

	2009	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES			
Net loss	$ (4,897,583)	$ (7,430,786)	$ (4,758,520)
Adjustments to reconcile net loss to net cash used by operating activities:			
Goodwill impairment	-	2,000,000	-
Loss on disposition of subsidiary assets	1,858,412	-	-
Loss on disposition of fixed assets	32,561	-	-
Interest accrued on bridge loan payable	-	6,946	27,101
Stock-based compensation	26,088	136,839	208,766
Depreciation	111,880	172,571	116,469
Amortization	90,756	90,756	37,815
Change in assets and liabilities:			
Trade accounts receivable	93,528	686,075	(67,216)
Inventories	249,985	530,610	30,191
Other current assets	49,961	42,019	62,354
Other assets	121,857	(63,729)	(12,610)
Accounts payable	39,237	288,073	(183,445)
Accrued expenses and other current liabilities	358,581	271,450	(258,521)
Liability for subsidiary insolvency	(138,581)	138,581	-
Net cash used by operating activities	(2,003,706)	(3,130,595)	(4,797,616)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Net cash paid to acquire subsidiary	-	-	(37,717)
Purchase of property and equipment	-	(12,821)	(168,946)
Net cash used by investing activities		(12,821)	(206,663)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net proceeds of common stock purchase	1,858,307	2,008,977	1,798,928
Proceeds from short-term loan and lines of credit	778,561	1,833,514	920,640
Repayment of bank loans	(717,159)	(110,543)	(54,740)
Net cash provided by financing activities	1,919,709	3,731,948	2,664,828
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	-	(44,209)	61,301
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(83,997)	544,323	(2,278,150)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	705,139	160,816	2,438,966
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 621,142	$ 705,139	$ 160,816
SUPPLEMENTAL CASH FLOW INFORMATION			
NON-CASH INVESTING AND FINANCING ACTIVITIES (See Note 3):			
Cost of fully depreciated equipment written off	-	$ 7,545	-
Issuance of shares in repayment of debt and accounts payable	$ 5,268,512	-	-
Issuance of shares to purchase subsidiary	-	-	$ 2,251,542
CASH PAID FOR:			
Income taxes	-	$ 13,941	$ 44,557
Interest during the year	$ 75,102	$ 150,824	$ 86,057

See the accompanying notes to the consolidated financial statements.

Nio Security, Inc. and Subsidiary

- Notes to consolidated financial statements

1. Business and organization and basis of presentation

Nio Security, Inc. ("Nio"), previously known as Dyna-Pel Systems Inc., was incorporated in the State of Delaware in 1992. Nio's corporate offices are headquartered in Florida with offices in Memphis, TN, Munich, Germany and Oslo, Norway.

In March 2004, Nio formed a German subsidiary, Holon Technology GmbH ("Holon") in Munich, Germany. Holon provided engineering and production services to its parent company through the end of September 30, 2008. As part of management's restructuring and cost cutting efforts, Holon filed for bankruptcy in October 2008. (See Note 13 for additional information).

On August 1, 2007, Nio acquired 100% of the shares of Tempest Microsystems, Inc. ("Tempest"), a company located in Poway, California. Tempest was established in 1999 and offered a range of digital video recorders for the security industry based on a PC platform. Under the purchase agreement, Nio paid Tempest's shareholders consideration of 100,000 shares of Nio common stock plus an additional consideration, not to exceed 250,000 Nio shares in the aggregate, to be determined according to an agreed earn-out formula. In January, 2010 the Poway, CA office was closed and the Tempest DVR line was discontinued. Certain Tempest assets were transferred to the previous owners as consideration for repayment of long-term loans. (See Notes 3 and 9).

Nio US develops and markets video processing and compression software and appliances based on in-house developed video processing and video analysis technology as well as video cameras. Nio has an existing suite of products that offer function and cost benefits to owners of existing and/or planned video surveillance systems employed in a wide range of applications.

Nio's products are sold to commercial as well as military and governmental users worldwide. The Company's operations comprise a single segment under accounting principles generally accepted in the United States of America.

Going concern

As reported in the accompanying financial statements, the Company incurred net losses of $ 4,897,583, $ 7,430,786 and $ 4,758,520 for the years ended December 31, 2009, 2008 and 2007, respectively. The Company had limited amounts of working capital and shareholders equity at December 31, 2009. These factors raise considerable doubt about the Company's ability to continue as a going concern. Management has been able to raise funds in late 2009 through the sale of shares and successfully repaid substantially all of its outstanding debt. The Company believes that it will continue as a going concern. However, there is no assurance that the Company will be successful. The accompanying financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

2. Summary of significant accounting policies

Recent accounting guidance not yet adopted

During 2009, the Financial Accounting Standards Board (FASB) issued authoritative guidance on revenue recognition, consolidation of variable interest entities and fair value disclosures for non-financial assets and liabilities, which guidance is not yet effective for the Company's financial statements. Management believes that these pronouncements will not have a significant impact on the Company's financial statements upon adoption.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

Principles of consolidation
The consolidated financial statements include the financial statements of Nio US and its wholly-owned subsidiaries, Holon (through the date of its termination) and Tempest. All significant inter-company balances and transactions have been eliminated in consolidation.

Financial instruments
The Company's financial instruments include cash, trade and affiliate accounts receivables and payables and bank debt for which carrying values approximate fair values due to the short maturities of those instruments.

Cash and cash equivalents
For financial statement purposes, the Company considers all highly liquid debt instruments with a maturity of three months or less when purchased to be cash equivalents. The Company maintains its cash in bank deposit accounts in the United States of America and overseas which, at times, may exceed applicable insurance limits. The Company has not experienced any such losses in these accounts.

The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

Trade accounts receivable and allowance for doubtful accounts
The Company has established an allowance for doubtful accounts receivable based upon factors such as the credit risk of specific customers, historical trends and other data. Based on management's evaluation of collectability, allowances for doubtful accounts of $ 12,060 and $ 30,400 were established at December 31, 2009 and 2008, respectively.

Inventories
Inventories are valued at the lower of cost (first-in, first-out) or market and consist of finished products at the Company's warehouses in Memphis, Tennessee and work-in-process at a third-party vendor in Munich, Germany.

Cost of sales
Cost of sales consists of materials and costs for assembly of the Company's products for sale incurred by the Company at its warehouses or those charged by third-party vendors (including freight to the warehouses) and materials and freight for finished goods purchased for sale from various vendors.

Property and equipment
Property and equipment are stated at cost, less accumulated depreciation. Depreciation is provided using straight-line and accelerated methods over the estimated useful lives of the assets. Fully depreciated assets are written off although they may still be utilized. The estimated useful lives of the various classes of assets are as follows: Computer software: 3 years; computer equipment: 3-10 years; furniture, fixtures and other: 3-5 years

Research and development expenses
Software development costs consist principally of compensation and benefits paid to the Company's employees. All software development costs not qualifying for capitalization are expensed as research and development costs when incurred.

The Company's policy is to expense all software development costs prior to establishing technological feasibility. Because the Company's products have reached this state of development almost concurrently with general release, the Company has not capitalized any software development costs.

Income taxes
On January 1, 2009, the Company adopted the authoritative guidance issued by the Financial Accounting Standards Board (FASB) on uncertain tax positions. The new guidance provides a threshold for determining when an income tax benefit can be recognized for financial statement purposes. The threshold for financial statement reporting generally is higher than the threshold claiming deductions in income tax returns. Under the new guidance, the tax benefit from an uncertain tax position can be recognized for financial statement purposes only if it is more likely than not that the tax position will be sustained upon examination by the taxing authorities including the resolution of appeals or litigation processes, if any. The new rules also provide guidance on classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, and income tax disclosures. Management believes there were no material uncertain tax positions at either January 1, 2009 or December 31, 2009.

The Company provides deferred income taxes resulting from temporary differences between the financial statement and tax bases of assets and liabilities. Deferred tax assets or liabilities at the end of each period are determined using the tax rate expected to be in effect when taxes are actually paid or recovered. Valuation allowances are established when necessary to reduce deferred tax assets to the amount that is more than fifty percent likely of being realized. Temporary differences result principally from the use of inventory uniform capitalization rules for tax purposes and accrued compensation costs and bad debt allowances that are not yet deductible for tax purposes.

The Company files U.S. federal income tax returns and state and local income tax returns in Florida, California, Tennessee and New York. Returns filed in these jurisdictions for tax years ended on or after December 31, 2006 are subject to examination by the relevant taxing authorities.

Translation of foreign currencies and foreign currency transactions
Financial statements of the Company's foreign subsidiary were translated into U.S. dollars at current exchange rates, except for costs and expenses, which were translated at average exchange rates during each reporting period. Net exchange gains or losses resulting from the translation of assets and liabilities were accumulated as "accumulated other comprehensive income or loss" and were reported as a separate component of shareholders' equity.

During the fourth quarter of 2008, the Company reached a final settlement of its obligations under the Holon bankruptcy and recognized the existing balance in the accumulated translation gain in the statement of operations. (See Note 13.)

Transactions in currencies other than the U.S. dollar are recorded in U.S. dollars at exchange rates prevailing at the transaction dates. Exchange gains and losses are included in the Company's results of operations.

Stock option plans

The Company accounts for stock options granted to its employees and directors under the fair value-based at date of grant method. Expense recognition is given for all compensatory options issued, including those with an exercise price equal to or greater than market value at the grant date. Such expense is recorded over the recipients' expected service period applicable to the grant.

Accounting for the impairment or disposal of long-lived assets

The Company follows the applicable accounting guidance for long-lived assets and certain identifiable intangibles. These are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds their fair value. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell.

Goodwill

Goodwill is the excess of cost over the fair value of net assets (including identifiable intangibles) acquired in a business acquisition. Goodwill is not amortized but rather tested at least annually for impairment or whenever events or changes in circumstances indicate that the carrying amount of the asset might not be fully recoverable. In accordance with the applicable accounting guidance, the Company compares the fair value of the acquired business to its carrying amount on an annual basis to determine if there is potential goodwill impairment. If the fair value of the acquired business is less than its carrying value, an impairment loss is recorded to the extent that the fair value of the goodwill is less than its carrying value. Fair values for acquired businesses are determined based on discounted cash flows, market multiples or appraised values.

At December 31, 2009, the Company recorded a loss on the disposition of its subsidiary. Such loss included the write off of $ 669,788 of goodwill originally recorded when the subsidiary was acquired in 2007 remaining on the books as of year-end. (See Notes 3 and 6).

Intangible assets, net

Intangible assets are amortized using the straight-line method over their estimated period of benefit. The Company periodically evaluates the recoverability of intangible assets and takes into account events or circumstances that warrant revised estimates of useful lives or that indicate that impairment exists. The Company has recorded a loss on the disposition of its subsidiary. (See Note 3). Such loss included the write off of $ 1,310,673 of unamortized balances of intangibles originally recorded when the subsidiary was acquired in 2007.

Classification of short-term liabilities subsequently converted to equity

Current portions of long-term debt, accounts payable and certain other liabilities, which are subsequently converted to equity in the succeeding fiscal year, are classified as long-term debt at the end of the year preceding such conversion.

Loss per common share

Basic and diluted loss per common share is computed by dividing net loss by the weighted average number of common shares outstanding. Due to net losses in 2009, 2008 and 2007 outstanding common stock purchase options and warrants were anti-dilutive and accordingly were excluded from this calculation. (See Note 10.)

Reverse stock split and increase in authorized shares

On June 2, 2009, the Company elected to amend and restate its certificate of incorporation to reflect an increase in the Company's authorized shares from thirty million to seventy million shares of common stock and change the par value per share of its common stock from fifty cents (USD 0.50) to ten cents (USD 0.10) and a reverse ten to one split of the outstanding common stock. The accompanying financial statements give full retroactive effect to the revised capital structure and also recognize adjustments for fractional shares.

Subsequent events

Management has evaluated subsequent events through May 7, 2010, the date the financial statements were available for issuance.

3. Acquisition and disposition of Tempest

On August 1, 2007, Nio acquired 100% of the shares of Tempest. (See Note 1). The assets acquired and liabilities assumed were recorded based on their relative fair values as follows:

Cash	$ 27,510
Accounts receivable	79,291
Inventory	100,176
Other assets	26,515
Goodwill, net of write-off	2,669,788
Patents and trademarks	1,530,000
Other property and equipment	266,333
Loans payable	(1,700,011)
Accounts payable and accruals	(682,833)
	2,316,769
Less: Cash paid for acquisition costs	65,227
Issuance of stock	$ (2,251,542)

The acquisition was recorded as a purchase and, accordingly, the Company's results of operations have been combined with the acquired business from the date of acquisition.

On January 21, 2010 the Company reached an agreement with the previous owner of Tempest to sell certain assets in return for $ 553,500, which amount had been advanced to pay certain bank debt in December 2009. The following details the assets sold and the resulting loss on the sale, all recognized as of December 31, 2009:

Fixed assets	$ 122,814
Inventories	289,930
Other assets	18,707
Goodwill	669,788
Patents	180,000
Trademarks	1,130,673
Total assets sold	2,411,912
Cash received	553,500
Net loss	$ 1,858,412

4. Inventories

Inventories at December 31 consist of the following:

	2009	2008
Finished products	$ 72,018	$ 397,632
Work-in-process	179,571	234,782
Raw materials	-	159,090
Total inventory	$ 251,589	$ 791,504

5. Property and equipment

Property and equipment consist of the following as of December 31:

	2009	2008
Computer software	$ 132,482	$ 132,482
Furniture, fixtures and computer equipment	14,446	789,714
	146,928	922,196
Less: Accumulated depreciation	109,436	617,449
Property and equipment, net	$ 37,492	$ 304,747

Depreciation expense for the years ended December 31, 2009, 2008 and 2007 was $ 111,880, $ 172,571 and $ 116,469, respectively.

6. Intangible assets and goodwill

Intangible assets, net

The components of the Company's intangible assets as of December 31, 2008 are as follows:

	Cost	Accumulated Amortization	Estimated Life Months	Net
Amortized intangible assets:				
Patents	$ 1,350,000	$ 128,571	178.5	$ 1,221,429
Unamortized intangible assets:				
Trademarks	180,000	-	-	180,000
Total	$ 1,530,000	$ 128,571	178.5	$ 1,401,429

Amortization expense was $ 90,756, $ 90,756 and $ 37,815 for the years ended December 31, 2009, 2008 and 2007, respectively. The intangible assets were sold effective as of December 31, 2009 (See Note 3).

Goodwill

The Company has elected to perform the annual impairment test on goodwill during the fourth quarter of each year, unless circumstances arise that require more frequent testing. During the fourth quarter of 2008, the Company completed the annual impairment tests of goodwill and concluded goodwill was impaired by $ 2,000,000. The impairment for 2008 was recorded as part of other expenses on the Company's statement of operations. As of December 31, 2009, the value of goodwill of $ 669,788 was written off as the subsidiary it related to was sold. (See Notes 1 and 3.)

7. Other assets

Other assets include security deposits on office leases and certain value added tax refunds due from German and Norwegian tax authorities.

8. Income taxes

As of December 31, 2009, the Company had approximately $ 40,127,000 of net operating loss carryforwards, which expire at various dates beginning in tax year 2012 through 2029. The availability to offset income taxes in future years may be restricted if the Company undergoes an ownership change, which may occur as a result of future sales of any stock and other events. For the years ended December 31, 2009, 2008 and 2007, the Company incurred taxable losses for domestic income tax purposes and, as such, had no related federal or state income tax expense. Income tax expense for the 2008 and 2007 fiscal years of $ 14,648 and $ 22,137, respectively, represent taxes that were due to German tax authorities from Holon's operations in Germany.

The tax effect of temporary differences that give rise to the Company's deferred tax assets and liabilities at December 31, 2009 and 2008 are as follows:

	2009	2008
Net operating loss carry-forwards	$ 16,051,000	$ 15,384,000
Less: Valuation allowance	16,051,000	15,384,000
Net deferred income tax assets	-	-

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. The ultimate realization of deferred tax assets depends on the generation of future taxable income. The Company has determined that it is more likely than not that it will not realize the benefit of its deferred tax assets and as such has recorded an allowance against 100% of its deferred tax assets.

The increase in the valuation allowance for deferred income taxes for the years ended December 31, 2009 and 2008 was $ 667,000 and $ 2,190,000 respectively. These increases are the result of losses incurred in 2009 and 2008 by the Company.

9. Financing

Short-term loans

During the first quarter of 2008, the short-term loan was increased with new loans from new lenders in the amount of NOK 3.625.866 (US$ 634,113), increasing the total loan to NOK 8,625,866 (US$ 1,554,753) plus accrued interest with maturity on April 1, 2008. In late March 2008, the short-term loans were increased with new loans from a new lender and one existing lender in the amount of NOK 2,500,000 (US$ 352,920), increasing the loan to NOK 11,125,866 (US$ 1,907,673) and extending the maturity until July 1, 2008. At the same time, the interest rate increased to 20% per annum.

In May 2008, a short-term Euro loan was entered into with a new lender in the amount of EUR 125,000 (US$ 176,012). In June, a loan of NOK 1.000.000 (US$ 196,746) was repaid in connection with a share issue reducing the total loans to NOK 11.391.792 (US$ 1,866,939). Prior to July 1, 2008, the short-term lenders agreed to extend the short-term loans until October 1, 2008.

During the third quarter of 2008, the NOK short-term loan was increased with new loans from new lenders in the amount of NOK 560,000 (US$ 95,092) and a short-term US$ loan was entered into with one existing lender in the amount of US$ 100,000 (NOK 719,225), increasing the total short-term loans to NOK 12,671,017 (US$ 2,082,031).

On the due date on October 1, 2008, the Company was not able to repay the short-term loans which had a total balance of US$ 2,082,031 plus accrued interest, and started negotiations with the lenders and possible new investors to restructure its debt.

On December 22, the Company completed a funding which included an extension of the maturity of the existing short-term loans, combined with new loans in the amount of NOK 6.1 million. The existing short term loans including accrued interest amounted to NOK 14,150,365 (US$ 2,055,784), and the total new loan facility was NOK 20,250,365 (US$ 2,903,032), with maturity on June 29, 2009. The interest is 10% per annum and the lenders have a first priority security interest in all of the Company's available intellectual property rights, including trademark and patents and all of the shares currently held by the Company in its U.S. subsidiary, Tempest Microsystems Inc. In addition, the Company issued 172,000 new warrants giving the lenders the right to purchase new shares at the price of NOK 10.00 per share. The warrants were to expire on the maturity date of the new loan, or June 29, 2009 at the latest. The new lenders received 122,000 warrants and the existing lenders received 50,000 warrants.

Prior to the due date on June 29, 2009, the Company extended the short-term loan due date until August 31, 2009 on the same terms. On August 31, 2009, the Company was not able to repay the short term loan and continued dialogue with the lenders under the short term loan agreement in order to secure a new financing.

In November, 2009, the Company finalized a refinancing, whereof the lenders under the short term loan agreed to convert the outstanding principal and accrued interest thereon into share capital of the Company based on a conversion price of NOK 1.92 per share. As a result, 10,541,097 new shares were issued to the lenders in December, 2009.

Long-term loans

On December 17, 2004, Tempest entered into a loan agreement with Vineyard Bank in the amount of $ 600,000 maturing on December 27, 2014, with interest at 4.75% per annum. On September 20, 2007, as a result of Nio's acquisition of Tempest, an agreement was signed between Nio and the Bank, whereby Nio assumed the outstanding loan balance of $ 475,291.

On February 24, 2006, Tempest entered into a loan agreement with Vineyard Bank in the amount of $ 950,000 maturing on July 28, 2018, with interest at 5.25% per annum. On September 20, 2007, as a result of Nio's acquisition of Tempest, an agreement was signed between Nio and the bank, whereby Nio assumed the outstanding loan balance of $ 923,878.

On December 31, 2009, the Company entered into an agreement with California Bank & Trust (successor to Vineyard Bank) regarding full pre-payment of the Company's two long-term loans for a US $ 1,107,000 payment and forgiveness of interest of $ 33,709, included in other income. As part of the agreement, the Company paid US $ 553,500 to the bank on December 31, 2009. In addition, the previous owner of Tempest, who was guarantor for the loans, paid the remaining $ 553,500 and, in return, received certain assets. (See Note 3) The two loans were paid in full as of December 31, 2009.

Also at December 31, 2009 and 2008, Tempest had one revolving line of credit in the amount of $ 115,191 and $ 115,195 respectively, with interest at prime plus 3.5%. The line is due on demand.

10. Shareholders' equity

Oslo Børs registration

The Company's shares are traded on the Oslo Stock Exchange ("OSLO BØRS") with the "NIO" ticker symbol.

Authorized shares

Pursuant to a shareholders meeting on June 2, 2009, the Company's number of authorized shares is 70,000,000 each with a par value of $ 0.10.

Private placements

On August 1, 2007, the Company concluded a private placement of 63,500 new shares at a subscription price of NOK 140.00 (US$ 24.4) per share. Total proceeds amounted to NOK 8,890,000 (US$ 1,546,676) less approximately US$ 77,415 in issuance costs. In addition, 1,000,000 shares were issued to the owners of Tempest during August 2007. (See Note 1).

In August 2007, 48,833 options were exercised under the Company's stock option plans for a total of approximately $ 330,000. As a result of the private placement, the purchase of Tempest and the exercise of options, the number of outstanding shares was increased to 2,207,979.

On February 15, 2008, the Company initiated a private placement of 100,000 shares at a subscription price of NOK 110.00 (US$ 21.7) per share, and on June 5, 2008 the private placement was concluded and 100,000 new shares were issued at the offered terms. Total proceeds amounted to NOK 11.000.000 (US$ 2,170,236) less approximately US$ 161,259 in placement fees. After this transaction, the number of outstanding shares was 2,307,979.

On November 30, 2009, the Company completed its refinancing and issued a total of 33,669,804 new shares of its common stock, including: (a) 19,298,246 shares to the investors in the private placement of NOK 11,000,000 at par value (US $ 0.10, $ 1,941,302 in the aggregate); (b) 10,541,097 shares at a share price of NOK 1.92; to the lenders from the conversion of the NOK 20,250,365 short term loan; and (c) 3,830,461 shares at a share price of NOK 1.92 to other creditors as consideration for other debt, all at the approximate US dollar equivalent of $ 0.3666.

For the listing of the new shares, a prospectus was accepted by the Oslo Stock Exchange on December

17, 2009. The number of outstanding shares was 35,978,041 as of December 31, 2009.

Stock option/warrant plans

The Company has various stock option plans. The Company's 1998, 2000, 2001 and 2004 plans provide for grants of up to 27,500, 5,000, 5,000 and 123,000 options, respectively and the 2006 plan where the total number of options available for grant is limited to 10% of the outstanding shares at the time of any grant. Each of the 1998, 2000 and 2001 plans limits the amount of options that may be granted to non-employee directors to 500 (an aggregate of 1,500 for all three plans), and for the 2004 plan, no more than 10% may be granted to non-employee directors and for the 2006 plan, no more than 20% may be granted to non-employee directors.

In addition, 40,000 warrants with an exercise price of NOK 35.00 were granted to a consultant as part of the compensation to undertake the initial public offering. In February 2007, 26,500 outstanding warrants were exercised for proceeds of approximately $ 147,000.

In addition, 172,000 warrants with an exercise price of NOK 10.00 (US$ 1.40) were granted to the lenders in the short term loan facility in December 2008. The warrants were cancelled in connection with the repayment of the short term loan through conversion into shares in November, 2009.

Lastly, in November, 2009, as part of the refinancing, the investors in the private placement were granted warrants to purchase 15,000,000 shares at NOK 2.50 per share and 15,000,000 shares at NOK 5.00 per share which expire no later than December 31, 2012. In addition, 1,800,000 warrants to purchase shares at NOK 2.50 per share with expiry not later than December 31, 2012 were granted for future allocation by the board of directors.

Options granted under the 2000, 2001, 2004 and 2006 Plans may be incentive stock options or non-qualified stock options, as determined by a Committee of the Board of Directors (the "Committee") at the time of grant. Incentive stock options are generally to be granted at a price not less than the fair market value of the stock on the date of grant, or at a price not less than 110% of the fair market value, if granted to a participant who is a greater than a 10% owner of the Company. Non-qualified stock options may be granted at a price to be determined by the Committee, which may be equal to, greater than, or less than the fair market value at the date of grant. Option vesting terms are established by the Committee at the time of grant.

The expiration dates of all options granted are determined at the time of grant and may not exceed ten years from date of grant, or five years from date of grant for participants who own greater than 10% of the Company. At December 31, 2009 there were 90, 1,200, 12,834 and 26,500 options outstanding under the above Plans, respectively, and 31,800,000 warrants outstanding.

During the years ended December 31, 2009, 2008 and 2007, the Company recognized stock-based compensation expense of $ 26,088 $ 136,839 and $ 208,766 respectively, in connection with stock options granted to employees and directors using the fair value method. The fair value per share of stock options granted at in 2008 to employees and directors ranged was $ 0.008 in 2008, on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions: No expected dividend yield, risk-free interest rate of 3.19%, volatility of 50.6% and an expected life of five years.

The following summarizes stock options and warrant activities under the 1998, 2000, 2001, 2004 and 2006 Plans for the years ended December 31, 2009, 2008 and 2007:

	Weighted Number of Shares	Average Exercise Price
Options outstanding at January 1, 2007	174,574	$ 23.20
Exercised	48,833	7.60
Cancelled	7,553	17.30
Options outstanding at January 1, 2008	118,188	37.10
Granted (warrants)	172,000	1.40
Cancelled	24,344	30.60
Expired	50,091	47.20
Total outstanding at December 31, 2008	215,753	5.90
Granted (warrants)	31,800,000	0.65
Cancelled (warrants)	172,000	1.40
Expired	3,129	47.12
Total outstanding at December 31, 2009	31,840,624	$ 0.67

The following tables summarize information about stock options and warrants outstanding at December 31, 2008 and 2009:

Exercise prices	Number outstanding at December 31, 2008	Weighted average remaining exercise life	Weighted average exercise price	Number of Shares exercisable at December 31, 2008	Weighted average exercise price
$ 1.40	172,000	0.49	1.40	172,000	1.40
5.00	12,333	6.07	5.00	12,333	5.00
11.00	3,000	6.92	11.00	3,000	11.00
15.00	1,200	3.99	15.00	1,200	15.00
28.70	26,500	7.96	28.70	17,666	28.70
175.00	410	0.74	175.00	410	175.00
275.00	310	1.26	275.00	310	275.00
	215,753	1.84	$ 5.90	206,920	$ 4.90

Exercise prices	Number outstanding at December 31, 2009	Weighted average remaining exercise life	Weighted average exercise price	Number of Shares exercisable at December 31, 2009	Weighted average exercise price
$ 6.08	9,834	5.07	6.08	9,834	6.08
13.29	3,000	5.92	13.29	3,000	13.29
15.00	1,200	2.99	15.00	1,200	15.00
34.74	26,500	6.96	34.74	26,500	34.74
275.00	90	0.26	275.00	90	275.00
0.43	16,800,000	3.00	0.43	16,800,000	0.43
0.87	15,000,000	3.00	0.87	15,000,000	0.87
	31,840,624	3.00	$ 0.67	31,840,624	$ 0.67

11. Major customers

Three customers accounted for 41%, 26% and 16%, respectively, of the outstanding accounts receivable balance at December 31, 2009 and three customers accounted for 24%, 17% and 13%, respectively, of the outstanding accounts receivable balance at December 31, 2008. Three customers accounted for 17% (9%, 4% and 4%), 18% (8%, 5% and 5%), and 15% (6%, 5% and 4%) of total sales for the years ended December 31, 2009, 2008 and 2007, respectively.

12. Commitments and contingencies

The Company is obligated under lease agreements in Tennessee and California, USA. As part of the Company's restructuring efforts the Munich, Germany lease was terminated in October 2008 as part of the insolvency agreement with the German insolvency court. The lease for the California location was taken pursuant to the sale of the Tempest assets effective January 2010.

Rental expense for the years ended December 31, 2009, 2008 and 2007 was $ 165,282, $ 499,337 and $ 329,615, respectively.

Minimum lease payments under the remaining leases as of December 31, 2009 are approximately:

2010	$ 41,189
2011	33,429
2012	33,429
	$ 108,047

13. Insolvency of Holon

During the fourth quarter of 2008, an agreement was reached between Holon and the insolvency administrator in Munich, Germany. Pursuant to the agreement, Holon agreed to pay 100,000 Euros ($ 138,581) in cash in exchange for its release from all liabilities outstanding as of the time of settlement. The Company recorded a gain on disposition of subsidiary of $163,837. The following details the components of the gain:

Liabilities and common stock outstanding at time of settlement released	$ 293,372
Adjustment for foreign currency	44,209
Assets given up at time of settlement	(38,432)
	299,149
Less: Cash paid	135,312
Net gain on insolvency	$ 163,837

14. Related party transactions

The Company incurred a total of $ 384,160, $ 134,739 and $ 40,809 for the years ended December 31, 2009, 2008 and 2007, respectively, in fees to board members for various per diem consulting work performed as well as $ 48,647, $ 45,290 and $ 30,786 in board fees for the years ended December 31, 3009, 2008 and 2007, respectively.

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