**SONASOFT CORP.**
**December 31, 2014**
**NOTES TO FINANCIAL STATEMENTS**

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND ORGANIZATION

### *(A) Organization*

SONASOFT CORPORATION, Inc. (The "Company") was incorporated under the laws of the State of California on December 18, 2002. The Company develops software that automates the disk-to-disk backup and recovery process for Microsoft Exchange, SQL and Windows Servers with integrated data protection, IM and e-mail archiving and disaster recovery solutions.

The financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles for annual and interim financial information. Accordingly, they include all the information and footnotes required by accounting principles generally accepted in the United State of America for annual financial statements. However, the information included in these interim financial statements reflects all adjustments (consisting solely of normal recurring adjustments) which are, in the opinion of management, necessary for the fair presentation of the financial position and the results of operations.

### *(B) Use of Estimates*

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reported period. Actual results could differ from those estimates.

### *(C) Cash and Cash Equivalents*

For purposes of the cash flow statements, the Company considers all highly liquid investments with original maturities of three months or less at the time of purchase to be cash equivalents. The Company at times has cash in banks in excess of FDIC insurance limits and places its temporary cash investments with high credit quality financial institutions. As December 31, 2014, the Company had approximately $101,413 in cash balances at financial institutions which are within the FDIC insured limits.

### *(D) Loss per Share*

Basic and diluted net loss per common share is computed based upon the weighted average common shares outstanding as defined by Accounting Standards codification ASC 260, "Earnings per Share." As of December 31, 2014 there were 189,553,049 common shares outstanding (excluding the options not yet exercised). Common stock equivalents have been excluded from the diluted net loss per share as the amounts are anti diluted.

### *(E) Research and Development Costs*

The Company expenses all research and development costs as incurred for which there is no alternative future use. These costs also include expensing of employee compensation and employee stock based compensation.

### *(F) Income Taxes*

The Company accounts for income taxes under Accounting Standards Codification (ASC 740). Under ASC 740 deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statements carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences

are expected to be recovered or settled. The Company has incurred losses over period of time, so there is no income tax payable except the minimum state tax payment.

***(G) Revenue Recognition***

Revenue is recognized when earned in accordance with applicable accounting standard ASC 985-605. Revenue from software arrangements with end users is recognized upon final delivery of the software; provided the collection is probable and no significant obligations remain. Revenue is recognized following ASC 985-605, all the elements of bundle software sold (including installation and maintenance) will be allocated based on the residual method. Bundled software packages include the actual software, software installation, and maintenance contracts. The customer is able to purchase maintenance contracts based on a one-year, two-year, or three-year terms. Maintenance contracts are sold as a service; therefore, we calculate the VSOE for maintenance contracts to be a fixed percentage of the list price based on the term of the maintenance contract purchased. The maintenance contract revenue is recognized over the term of the maintenance contract. Amount billed in excess of revenue earned on the maintenance contract will be classified as deferred revenue. The software installation price is a fixed amount based on the number of mailboxes sold, and the residual amount after deducting installation charges and the maintenance contract will be allocated to the software product sale.

**Allocation of revenue among various elements:**

We sell software as a bundle product including installation, maintenance and product license. We allocate the revenue as follows:

- Installation revenue is a fixed amount based on the number of mailboxes sold.
- Fixed Price Maintenance Contract is a set amount calculated as 20% of list price for a one-year contract.
- Fixed Price Maintenance Contract is a set amount calculated as 17.5% of list price for a two-year contract.
- Fixed Price Maintenance Contract is a set amount calculated as 15% of list price for a three-year contract.
- Software revenue is calculated as the residual amount after deducting the installation and maintenance contract revenue

The one-year fixed price maintenance contracts revenue is recognized over 12 month period from the starting month to 12-month period. The two-year maintenance contracts revenue will be recognized on monthly basis and spread over a period of 24 months. The three-year maintenance contract revenue will be recognized over a period of 36 months.

In Dec 2012, a customer bought 2 years maintenance contract for our products, the revenue will spread over 24 month period, we will recognize first month revenue in Dec 2012, the balance 96% of revenue will be recognized in 2013 and 2014.

As of December 31, 2014 the Company has included deferred revenue of $86,032 in other current liabilities.

As of December 31, 2014, the Company has included deferred revenue of $48,601 in other long-term liabilities.

As of December 31, 2012 and 2013, the Company has included $170,333 and $114,295 of deferred revenue in other current liabilities, respectively.

As of December 31, 2012 and 2013, the Company has included $1,085 and $437 of deferred revenue in other long term liabilities, respectively.

***(H) Property & Equipment***

We record our property and equipment at cost and depreciate these assets on a straight-line basis to their estimated residual values over their estimated useful lives of 3 to 7 years.

***(I) Stock-Based Compensation***

The Company accounts for its stock-based compensation under the provisions ASC 718 " Accounting for stock based compensation" the Company is permitted to record expenses for stock options and other employee compensation plans based on their fair value at the date of grant. Any such compensation cost is charged to expense on a straight-line basis over the periods the options vest. If the options had cashless exercise provisions, the Company utilized variable accounting.

Common stock, stock options and common stock warrants issued to other than employees or directors are recorded on the basis of their fair value, as required by ASC 718 , which is measured as of the date required by ASC 505, *"Accounting for Stock based Compensation*" In accordance with ASC 505, the stock options or common stock warrants are valued using the Black-Scholes model on the basis of the market price of the underlying common stock on the "valuation date," which for options and warrants related to contracts that have substantial disincentives to non-performance is the date of the contract, and for all other contracts is the vesting date. Expense related to the options and warrants is recognized on a straight-line basis over the shorter of the period over which services are to be received or the vesting period. Where expense must be recognized prior to a valuation date, the expense is computed under the Black-Scholes model on the basis of the market price of the underlying common stock at the end of the period, and any subsequent changes in the market price of the underlying common stock up through the valuation date is reflected in the expense recorded in the subsequent period in which that change occurs.

***(J) Fair Value of Financial Instruments***

The carrying amounts of the Company's financial instruments including accounts receivable, accounts payable and accrued expenses approximate their fair value due to the relatively short period to maturity for these instruments.

***(K) Business Segments***

The Company operates in one segment and therefore segment information is not presented.

***(L) Advertising Costs***

Advertising costs are expensed as incurred and include the costs of public relations activities. These costs are included in selling, general and administrative expenses and totaled $4,995 for the year ended December 31, 2014.

***(M) Identifiable Intangible Assets***

As of December 31, 2014, $2,638 of costs related to filing patent applications has been capitalized. When patents are approved, the costs are amortized over the life of the patent. All costs for patents not approved will be expensed at that time of denial

***(N) Long-Lived Assets***

Long-lived assets and certain identifiable intangible assets related to those assets are periodically reviewed for impairment whenever circumstances and situations change such that there is an indication that the carrying amounts may not be recoverable. If the non-discounted future cash flows of the enterprise are less than their carrying amount, their carrying amounts are reduced to fair value and an impairment loss is recognized. There was no impairment recorded in 2010 and 2011.

## NOTE 2 GOING CONCERN

As reflected in the accompanying financial statements, the Company has net accumulated loss of ($13,429,335) and net income for fiscal year ending December 31, 2014 is $52,795, and as of December 31, 2014 a working capital deficiency of ($137,316) which includes $1,536,009 owed to key stockholders and a stockholder's deficiency of ($1,952,336) at December 31, 2014. This raises substantial doubt about its ability to continue as a going concern. The ability of the Company to continue as a going concern is dependent on the Company's ability to raise additional capital and implement its business plan. The financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

Management believes that actions presently being taken to obtain additional funding and to implement its strategic sales plan provide the opportunity for the Company to continue as a going concern.

## NOTE 3 ACCOUNTS RECEIVABLE

Accounts receivable at December 31, 2014 consisted of the following:

| | As of December 31, 2014 |
|---|---|
| Trade and other receivables | $ 457,851 |
| Less: Allowance for doubtful accounts | - |
| | $ 457,851 |

The bad debt expense for the six months ended December 31, 2014 was $0.

## NOTE 4 PROPERTY AND EQUIPMENT

Property and equipment at December 31, 2014 consisted of the following:

| | 2014 |
|---|---|
| Office equipment | $ 20,721 |
| Office furniture | 1,821 |
| Leasehold improvements | 7,588 |
| Computer equipment | 78,881 |
| Less: Accumulated depreciation | 109,010 |
| | $ 0 |

Depreciation expense for the quarter ended December 31, 2014, was $0.

## NOTE 5 STOCKHOLDERS' EQUITY

### *(A) Common Stock Issued for Cash*

During the quarter ended December 31, 2012, the Company did not issue any shares of common stock for cash.

During the quarter ended June 30, 2012 the Company issued 10,832,000 shares to existing shareholders and in Sept 30, 2012, the Company did issue 17,400,000 shares of common stock for cash. The number of shares issued for cash during Q4 were 12,800,000.

During the quarter ended December 31, 2013, the Company issued shares of common stock for cash of $86,000 at $0.005 per share.

| | |
|---|---|
| Ramesh Kumar Kannan (Existing Stockholder) | $50,000 |
| Barbara Tang (New Shareholder) | $15,000 |
| Doug MacKallor (Existing Shareholder) | $21,000 |

None of the above individuals is any officer, director or 10% stockholder of the company.

During the quarter ended December 31, 2013 the Company issued 5,000,000 shares of common stock for $25,000 cash at $.005 per share to Dr Romesh Japra, Chairman of the Board/Director and over 10% stockholder of the Company

During the quarter ending December 31, 2014, the Company issued 8,000,000 shares of common stock for $200,000 cash at $.025 cents per share to Dr Romesh Japra and Romi Randhawa, Directors of the Company.

### *(B) Common Stock Issued for Services*

During the year 2012, the Company issued 8,500,000 shares of common stock to various consultants for services.

During the year 2013, the Company issued 20,200,000 shares of common stock to various consultants for services and to key officer and employees in lieu of past due salaries.

During Q1, 2014, the Company issued 2,200,000 shares of common stock to various consultants for services and to employee in lieu of past due salary.

## NOTE 6 STOCK OPTION PLAN

Effective January 1, 2006, transactions under the Company's 2003 Plan (as defined below) were accounted for in accordance with the recognition and measurement provisions of ASC 718 "Share-Based Payment" , and related interpretations of ASC 718 requires compensation costs related to share-based payment transactions, including employee stock options, to be recognized in the financial statements. In addition, the Company adheres to the guidance set forth within SEC Staff Accounting Bulletin No. 107, which provides the views of the staff of the SEC regarding the interaction between ASC 718 and certain SEC rules and regulations and provides interpretations with respect to the valuation of share-based payments for public companies.

In adopting ASC718 ,the Company applied the modified prospective approach to transition. Under the modified prospective approach, the provisions of ASC 718 are applied to new awards and to awards modified, repurchased, or cancelled after the effective date. Additionally, compensation costs for the portion of awards for which the requisite service has not been rendered that are outstanding as of the effective date are recognized as the requisite services are rendered on or after such date. The compensation costs for that portion of awards are based on the grant-date fair value of those awards as calculated for either recognition of pro-forma disclosures

Stock option compensation expense for calendar year ending December 31, 2014 is the estimated fair value of options granted, amortized on a straight line basis over the requisite service period for the entire portion of the award.

*Black-Scholes Valuation*

The fair value of options at the date of grant is estimated using the Black Scholes option pricing model. The assumptions made in calculating the fair values of options are as follows:

| | For the quarter ended December 31, 2013 |
|---|---|
| Expected term (in years) | 3 |
| Expected volatility | 25% to 78% |
| Rick-free interest rate | 1.79% to 3.05% |

There were 23,1m stock option awards granted during the year ending December 31, 2014.

*Plan Information*

In February 2003, the 2003 Incentive and Non-Statutory Stock Option Plan was approved and adopted by the Board of Directors. The 2003 Plan became effective upon the approval of the holders of the Company's stock at the Company's annual stockholders meeting held on June 4, 2003. Under the 2003 Plan, the Company may grant stock options to its employees, officers, and other key persons employed or retained by the Company and any non-employee director, consultant, vendor or other individual having a business relationship with the Company. Options are granted at various times and usually vest over a thirty-six (36) month period. As of December 31, 2014 the Company had total options pursuant to the 2003 Plan of 23.1m

| Exercise Price | Number Outstanding December 31, 2014 | Weighted Average remaining Contractual Life | Weighted Average exercise Price | Number Exercisable at December 31, 2014 | Weighted Average Exercise Price |
|---|---|---|---|---|---|
| .00-.025 | 22,100,000 | .58 | 0.025 | 9,282,000 | 0.025 |
| | 1,000,000 | 100 | 0.025 | 1,000,000 | 0.049 |
| | 23,100,000 | | | 10,282,000 | |

## NOTE 7 COMMITMENTS AND CONTINGENCIES

### *(A) Employment Agreement*

The company has entered into an employment agreement with its Chief Executive Officer through the year 2014 at an annual minimum salary of $150,000 per year, with additional fringe benefits as determined by the Board of Directors. In the event of termination of the agreement by the company, the company is required to pay a severance payment equivalent to 60 months of salary at the rate, and with the benefits, in effect at the date of termination.

The company has also entered into similar agreements each extending through the year 2014 with two other employees/managers at an average annual salary of $120,000. In the event of termination of the agreement by the company, the company is required to pay a severance payment equivalent to 12 months of salary at the rate, and with the benefits, in effect at the date of termination.

### *(C) Royalty Agreement*

During the year 2003 the company entered into royalty agreements with investors. The maximum liability under the agreement will be $1,500,000. The maximum amount due to investors in each year will be 5% of revenue up to a total of $1,500,000. Such premium is payable only if management of the Company reasonably determines that the company is profitable. Accordingly, in accordance with the signed royalty agreements, the Company is accruing the royalty premium at 5% of revenue. The royalty balance as of December 31, 2012 is $230,766 and as of December 31, 2014 is $233,049.

***(D) Lease Agreement***

The company has entered into a lease agreement for an office building, the lease period ends on Feb 28, 2013. The company is currently on a month to month basis. The base rent for this property is $2,750 per month plus operating expenses approx. $500 per month... Our monthly rental bill for this property is between $3,250 and $3,500. The annual rent payable under month to month lease is $ 39,000.

***(E) Employment Related Lawsuit***

In 2006, an ex-employee filed a lawsuit against the Company for wrongful termination. The Company has accrued a tentative settlement with the ex-employee for the payment of $227,000 in cash and an additional 95,000 shares of the Company stock as of December 31, 2007. As of December 31, 2012 Company had made payments towards the settlement, the legal case is still pending and contested in Santa Clara County Court. The Company made the final payment of $85,526 on February 29, 2013. The legal suit is pending appeal.

## NOTE 9 NOTE PAYABLE – RELATED PARTY

**A)** Note Amount $500,000 payable to Dr Romesh Japra, issued on December 19, 2008, interest rate 10% p.a. The principal and outstanding interest due should be paid in 36 months, maturity date of December 18, 2011. The note holder is also entitled to warrants of 2,272,727 shares of common stock of Sonasoft with a term of 36 months exercisable by holder upon payment of $.22 cents per share of stock actually purchased. The note holder did not exercise the warrants granted. The balance outstanding including principal and interest as of December 31, 2013 is $700,000 and as of December 31, 2014 is $0. The Note holder agreed to convert the debt into Sonasoft common stock at $.025 cents per share as of December 30,2014 and forgiven the accrued interest in lieu of vested options.

**B)** Note Amount $33,000 payable to Michelle Rose, issued on November 1, 2009, carrying interest rate 10% p.a. The principal and outstanding interest due should be paid in 36 months, maturity date of October 31, 2012. The note holder is also entitled to warrants of 165,000 shares of common stock of Sonasoft with a term of 36 months exercisable by holder upon payment of $.22 cents per share of stock actually purchased. The note holder did not exercise the warrants granted. The balance outstanding including principal and interest as of December 31, 2013 is $43,450, and as of March 31, 2014 is 0. The Note holder agreed to convert the debt into Sonasoft common stock at $.025 cents per share as of December 30,2014 and forgiven the accrued interest in lieu of vested options.

**C)** Note Amount $100,000 payable to Joseph and Anne Rapp, issued on November 1, 2009, carrying interest rate 10% p.a. The principal and outstanding interest due should be paid in 36 months, maturity date of October 31, 2012. The note holder is also entitled to warrants of 500,000 shares of common stock of Sonasoft with a term of 36 months exercisable by holder upon payment of $.20 cents per share of stock actually purchased. The note holder did not exercise the warrants granted. The balance outstanding including principal and interest as of December31, 2013 is 131,667, as of December 31,2014 is $0. The Note holder agreed to convert the debt into Sonasoft common stock at $.025 cents per share as of December 30,2014 and forgiven the accrued interest in lieu of vested options.

**D)** Note Amount $22,000 payable to Ken Fishmen, issued on November 1, 2009, carrying interest rate 10% p.a. The principal and outstanding interest due should be paid in 36 months, maturity date of October 31, 2012. The note holder is also entitled to warrants of 110,000 shares of common stock of Sonasoft with a term of 36 months exercisable by holder upon payment of $.20 cents per share of stock actually purchased. The note holder did not exercise the warrants granted. The balance outstanding including principal and interest as of December 31, 2013 is $28,967, as of December 31, 2014 is $0. The Note holder agreed to convert the debt into Sonasoft common stock at $.025 cents per share as of December 30,2014 and forgiven the accrued interest in lieu of vested options.

**E)** Note Amount $400,000 payable to Dr Romesh Japra, issued on November 1, 2009, carrying interest rate 10% p.a. The principal and outstanding interest due should be paid in 36 months, maturity date of October 31, 2012. The note holder is also entitled to warrants of 2,000,000 shares of common stock of Sonasoft with a term of 36 months exercisable by holder upon payment of $.20 cents per share of stock actually purchased. The note holder did not exercise the warrants granted. The balance outstanding including principal and interest as of December 31, 2013 is $526,667, as of December 31, 2014 is $0. The Note holder agreed to convert the debt into Sonasoft common stock at $.025 cents per share as of December 30,2014 and forgiven the accrued interest in lieu of vested options.

**F)** Note Amount $50,000 payable to Muriel K MacKallor issued on Jan 15, 2013, carrying interest rate of 15% p.a. The principal and outstanding interest due should be paid in three installments, April, July and October 2013. The balance outstanding including principal and interest as of December 31, 2013 is $51,541. The first installment of principal and interest due was paid in April 2013. The balance outstanding including principal and interest as of December 31, 2013 is 35,828, as of December 31, 2014 is $40,448.

**G)** Note Amount $136,404 payable to Camden Properties issued on Jan 1, 2010, carrying interest rate of 10% p.a. The balance outstanding including principal and interest as of December 31, 2013 is $180,053, as of December 31, 2014 is $0. The Note holder agreed to convert the debt into Sonasoft common stock at $.025 cents per share as of December 30,2014 and forgiven the accrued interest in lieu of vested options.

## NOTE 9 SUBSEQUENT EVENT

On January 10, 2014, the Company changed its authorized capital by increasing the shares of common stock available for issuance from 200,000,000 shares to 400,000,000 shares.