XSUNX INC
Form 10-K/A
April 01, 2008

UNITED STATES
SECURITIES EXCHANGE COMMISSION
Washington, D.C. 20549

Amendment #1
To

FORM 10-K

ANNUAL REPORT PURSUANT TO
THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended September 30, 2007

Commission File Number 000-29621

XSUNX, INC.
(Exact Name of Registrant as Specified in Its Charter)

Colorado	**84-1384159**
(State of Incorporation)	(I.R.S. Employer Identification No.)

65 Enterprise, Aliso Viejo, CA 92656
(Address of Principal Executive Offices) (Zip Code)

(949) 330-8060
(Registrant's Telephone Number)

Securities registered pursuant to Section 12(b) of the Act: Title of each class: **None**

Name of Each Exchange on which Registered: **N/A**

Securities registered pursuant to Section 12(g) of the Act: Title of each class: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o NO x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o NO x

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

Check if disclosure of delinquent filers pursuant to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated file, an accelerated filer, or a non-accelerated filer.

(Check one):

o Large accelerated filer x Accelerated filer o Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.) (Check one): Yes o NO x

As of September 30, 2007, the aggregate market value of the registrant's Common Stock held by nonaffiliates of the registrant was approximately $54,584,383 million based on the closing price as reported on the NASDAQ OTCBB Market.

As of December 28, 2007, there were 164,752,188 shares of the registrant's Common Stock outstanding.

XSUNX, INC.

TABLE OF CONTENTS

	Page
PART I	
Item 1. Business	1
Item 1A. Risk Factors	12
Item 1B. Unresolved Staff Comments	16
Item 2. Properties	16
Item 3. Legal Proceedings	17
Item 4. Submission of Matters to a Vote of Security Holders	17
PART II	
Item 6. Selected Financial Data	22
Item 7. Management's Discussion and Analysis or Plan of Operations	23
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	31
Item 8. Financial Statements and Supplementary Data	32
Item 9. Changes in and Disagreements on Accounting and Financial Disclosure	32
Item 9A. Controls and Procedures	32
Item 9B. Other Information	35
PART III	
Item 10. Directors, Executive Officers, and Corporate Governance	38
Item 11. Executive Compensation	40
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	42
Item 13. Certain Relationships and Related Transactions, and Director Independence	43
Item 14. Principal Accounting Fees and Services	43

PART IV

Item 15. Exhibits, Financial Statement Schedules 44

Signatures 48

Explanatory Statement

We are filing this Amendment Number One to our Annual report on Form 10 K to enhance our disclosures in the following areas:

- Revised audit report to make it clear that Since Inception numbers were audited and the present auditors are relying on the work of previous auditors. This enhancement can be found in Part IV.
- Enhance the deferred tax asset disclosures in note 3 to the financial statements entitled Federal Incomes Tax.
- Enhance the disclosures relating to the Company's Marketable Prototype in note 7 to the financial statements entitled Marketable Production Machine Acquisition.
- Enhance the disclosures relating to the Company's Option and Warrant Expenses in note 2, Summary of Significant Accounting Policies and note 6, Stock Options and Warrants to the financial statements.
- Revised our discussion of the Company's Internal Controls to state the internal control framework the Company is using. This can be found in Item 9A - Controls and Procedures.

As a result, of these changes, we are also filing new Certificates has Exhibits 31.1, 31.2, 32.1 and 32.2 hereto.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Securities Exchange Act of 1934 and the Securities Act of 1933, which are subject to risks, uncertainties and assumptions that are difficult to predict. All statements in this Annual Report on Form 10-K, other than statements of historical fact, are forward-looking statements. These forward-looking statements are made pursuant to safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The forward-looking statements include statements, among other things, concerning our business strategy, including anticipated trends and developments in and management plans for, our business and the markets in which we operate; future financial results, operating results, revenues, gross margin, operating expenses, products, projected costs and capital expenditures; research and development programs; sales and marketing initiatives; and competition. In some cases, you can identify these statements by forward-looking words, such as “estimate”, “expect”, “anticipate”, “project”, “plan”, “intend”, “believe”, “forecast”, “foresee”, “likely”, “may”, “shoul “might”, “will”, “could”, “predict” and “continue”, the negative or plural of these words and other comparable terminology. Th forward-looking statements are only predictions based on our current expectations and our projections about future events. All forward-looking statements included in this Annual Report on Form 10-K are based upon information available to us as of the filing date of this Annual Report on Form 10-K. You should not place undue reliance on these forward-looking statements. We undertake no obligation to update any of these forward-looking statements for any reason. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance, or achievements to differ materially from those expressed or implied by these statements. These factors include the matters discussed in the section entitled “Item 1A: Risk Factors” and elsewhere in this Form 10-K. You should carefully consider the risks and uncertainties described under this section.

For further information about these and other risks, uncertainties and factors, please review the disclosure included in this report under Item 1A “Risk Factors.”

PART I

Item 1. Business.

In this Report, we use the terms “Company,” “XsunX,” “we,” “us,” and “our,” unless otherwise indicated, or the context otherwise requires, to refer to XsunX, Inc.

Business Overview

XsunX is a thin-film photovoltaic (“TFPV”) company that intends to grow its business by manufacturing TFPV amorphous solar modules and selling them into what we believe is a high growth solar market opportunity. Our decision to pursue this strategy is based on our three years of research in the design and use of technologies for the manufacture of TFPV solar cells utilizing amorphous silicon. During this time we have developed the technical capabilities, qualified core staff, and market understanding that we believe will be necessary to establish product manufacturing infrastructure and take our product to market.

We have designed a TFPV solar module which we believe will deliver an average of 125 peak watts. To produce solar modules in commercial quantities we intend to processes glass substrates within a proprietary semiconductor manufacturing system which employs the design of a high-throughput, automated, continuous process. We believe that the design of our TFPV module and manufacturing system can deliver per watt costs significantly less than those of traditional crystalline silicon solar module manufacturers, and allow us to market TFPV modules that will be highly competitive with other thin film offerings.

Our plan for growth is to build and operate a TFPV solar module manufacturing facility in the state of Oregon. Employing a phased roll-out of manufacturing capacities, our baseline production system is scheduled for installation in mid calendar year 2008, the installation of our first 25MW line is scheduled near the end of calendar 2008, and the installation of our 4th 25MW line is scheduled for early 2010. In anticipation of commercial production, we have begun to market our TFPV solar module under the brand name of the XsunX ASI-120. Furthermore, we have successfully developed and implemented a pre-sales reservation program for system installers and large users of solar.

Markets

We believe the solar market represents a high growth opportunity nationally and internationally, both currently and into the foreseeable future. The global demand for electrical energy has experienced significant growth due to growth in populations and the economic vitality of emerging economies. This has created a growing need to diversify and establish new sources of electrical production, and we believe has created tremendous opportunities for growth in the solar market. Within the markets for solar products we anticipate that growth in demand for solar products based on TFPV technologies will out perform the balance of the solar market.

Macro growth drivers for solar energy production products include political support and government subsidies, high energy prices, technical progress having led to cost reductions in manufacturing techniques, and advantages over other renewable energy sources including:

- Proven, commercialized and widely used solar technologies adapting to a host of applications
- Negligible environmental impact
- Reliability, little or no delivery risk
- Maximum power generation coincides with peak energy demands
- Potential for distributed point of use generation

Growth drivers that we believe may allow TFPV to outpace the balance of the solar market include:

- Highly scalable and automated manufacturing processes
- Lower material costs and fewer constraints to sufficient material supplies
- Lower per watt production costs for solar cells and integrated solar modules

Driving our solar module manufacturing plan is what we believe to be the ability to capitalize on long term growth in solar spurred by increasing electrical energy costs and demand. Large markets are developing for commercial operators of private solar farms, utilities meeting green mandates, government subsidized installations, and operators of large commercial and industrial properties. These projects represent large installations typically approaching 1MW

or more.

While we believe that the market conditions are excellent for all producers of solar products, we intend to deliver thin film solar products that provide extra value in performance and cost.

Products

Solar Modules

In designing our XsunX ASI-120 module, we interviewed solar systems integrators and developed a design that we believe provides for a module delivering high power output (relative to other thin films), and size and framing that would allow for the use of many existing mounting systems. In doing so, we believe our modules strike a balance between higher rated power silicon wafer modules and lower rated power thin film modules. Further, we believe the market will dictate retail installed pricing. Systems integrators will look to sell installed watts at market dictated prices, and after accounting for certain fixed installation costs inherent to each of the different solar technologies, they will drive pricing per watt for factory delivered modules to compensate for any added installation costs when using certain technologies.

We have focused on the development of thin film amorphous technologies and products due to what we perceive as inherent advantages of amorphous silicon over other solar absorbers in regards to conversion efficiencies. Amorphous silicon produces more power earlier in the day and later into the evening because it requires less incident light than many other technologies. Amorphous silicon also exhibits less thermal coefficient degradation effects when operating in hot climates. In contrast, other thin film and conventional silicon wafer technologies degrade at significant rates of approximately 10% to 20% conversion loss of peak rated performance when operating at normal temperatures of 65 degrees centigrade.

We plan to deposit two separate solar cell layers of amorphous silicon on to a glass substrate. This is to increase the amount of absorbed and converted solar energy in our modules. Based on previous experimental and limited commercial use of our thin film deposition recipes, we anticipate the finished solar module to produce 7.9% frame to frame efficiency delivering approximately 125 peak watts of direct current “DC” power. We believe that we may be able to improve conversion efficiencies through the use of derivative forms of amorphous and other proprietary cell structures.

We anticipate that we can present the superior per-rated-watt-performance of amorphous in “real world” operating conditions as a competitive strength over the factory-rated performance of various other solar technologies. We believe these factors will influence the purchasing decision process of large solar power farms and utility size installations.

Product Competitive Strengths

Other product and manufacturing design strengths that may allow us to become a competitive force within the solar energy industry and the broader electric power industry include:

Cost-Per-Watt Advantage. We contend the design of our solar module and our vertical, in-line, continuous process production system may allow us to take advantage of economies of scale and accelerate development cycles, enabling possible further reductions in our manufacturing costs per watt. As we introduce planned manufacturing efficiency gains, we anticipate our per watt production costs to fall from initially $1.58 in 2008 to approximately $1.19 per watt by 2011. We believe this pricing will continue to be significantly less than the costs of crystalline silicon solar modules. As we mature and integrate new cell designs and materials, we believe the opportunity exists to drive cell performance above 8% and deliver wholesale costs per watt approaching $1 per watt or less.

Stable Material Availability. Our planned operations are not impacted by the current shortage of polysilicon (a key raw material for conventional non thin film solar module products) that is affecting most of our competitors through higher costs and limited availability. The key raw materials to be used in our solar module design are low iron tempered glass, high purity industrial gases such as argon, nitrogen, hydrogen, and silane

and germane, and extruded aluminum for module framing with polymer materials employed in the encapsulation for weather proofing. We believe we have adequate sources for the supply of these key raw materials and components for our manufacturing needs and in most instances, have selected multiple source suppliers. As we begin to scale manufacturing efforts, we may single out certain key suppliers to enhance efficiency, cost and quality. The cost of certain raw materials may rise over the next several years and we intend to actively manage these costs through purchasing strategies, product design, and operating improvements.

Non-Toxic Finished Product. The design of our amorphous solar module transfers no heavy metals or toxic compounds in the finished product. Conventional polysilicon solar modules contain lead based cell interconnections and thin films such as cadmium telluride (CdTe) and copper indium gallium selenide (CIGS) contain toxic materials in the finished product.

Large Area, High Power Delivery Module Design. Our intent and execution plan is to work on establishing the most efficient way to deliver a commercially viable solar module at competitive price points as opposed to focusing strictly on how to increase energy conversion efficiencies of the solar cell. Our solar module is based on established module designs and well known manufacturing processes necessary to deliver a large area, TFPV module producing what we believe to be nearly twice the rated power delivery per module of other thin film offerings. We believe this design will require fewer solar panels per installation compared to the use of other thin film systems, thereby reducing the overall costs associated with mounting, installation, wiring and interconnection of fewer parts and pieces.

Knowledgeable System Component Vendor Base. Amorphous TFPV benefits from nearly thirty years of process development and research, which has produced a knowledgeable and experienced vendor base. These vendors provide access to improved semiconductor device technologies resulting in improvements to manufacturing processes in related areas such as thin film transistors, memory devices, and high performance opto-electric coatings. We have engaged a select group of these vendors and established a primary and secondary vendor for each major system component.

Certifications

We have selected components for use in our TFPV solar module that have previously been tested by Underwriters Laboratories (UL) and approved for use in the manufacture of solar modules. We plan to submit these materials, and a full scale working sample of our TFPV module, to UL for the purpose of receiving UL certification 1703 in the 2008 period. Upon completion of initial module production capabilities we plan to submit modules for participation in laboratory and field tests with the National Renewable Energy Laboratory, the Fraunhofer Institute for Solar Energy.

We plan to work to achieve and maintain all certifications required to sell solar modules in the markets we plan or expect to serve, including UL 1703, IEC 61646, TÜV Safety Class II and CE.

Planned Manufacturing Capacities

Production Line Features

The core feature of our plan revolves around the design of an efficient mass production system. The design utilizes an in-line vertical glass coating system processing two balanced and independent lines simultaneously. This design incorporates material handling, cell deposition, laser segmentation, cleaning, and module packaging functions necessary to convert an inexpensive piece of 100cm X 160cm sheet glass into a complete solar module in less than three hours. Our process uses only a fraction of the semiconductor material that would be necessary to produce crystalline silicon solar modules.

Phased Production Build Out and Planned Capacities

In the 2008 calendar year, we anticipate completing the assembly and installation of a small scale baseline production system and initiating construction of our first full scale 25 MW system. We further anticipate that the baseline production system will generate limited solar module production in 2008 for use in fueling our sales channel and establishing product recognition for larger quantity sales in 2009. We anticipate completing the assembly of and commissioning our first 25MW line between December 2008 and January 2009. Near the end of the 2008 calendar year, we plan to launch the build-out of the first of three additional 25 MW

systems necessary to eventually bring our capacity to 100MW. Barring assembly delays, the first of these lines is slated to come on-line in November 2009, the second in January 2010, and the final 25MW in March 2010. We intend to use the balance of the 2010 year to continue to work to improve system utilization, add shifts, and increase module yields to bring our production to peak capacities of 100MW or more of annualized solar module production. To

complete each new production line, we plan to use a systematic replication process that is designed to enable us to add production lines rapidly and efficiently, and achieve operating metrics that are comparable to the performance of our initial 25MW system.

Production Line Planned Utilization and Production Costs

Each system, or line, has an estimated annualized initial module production capacity of approximately 25 megawatts, "MW" per annum, based on an initial 58% system utilization (the percentage of system utilization in each 7 day by 24 hour period) and 80% yield (the percentage of product meeting saleable specifications). We plan to ramp-up system utilization and yield to industry standards of 80% & 85% respectively over the course of the first full year of production in 2009, thereby increasing total production capacities per line to an anticipated 33MW. Initial per watt production costs during ramp-up of operations in the 2009 period are anticipated to be $1.58 per watt. As we improve system utilization and production yield in 2009, we anticipate our production costs will lower to $1.38 in 2010 and $1.19 in 2011. By continuing to expand production and improve solar energy conversion efficiencies and manufacturing processes, we believe we can further reduce our manufacturing costs per watt and improve our cost advantage over traditional crystalline silicon solar module manufacturers.

At present, the majority of our operations development efforts for the period ending September 2008 and the foreseeable future thereafter will focus on establishing and expanding facilities necessary to manufacture our TFPV solar modules for commercial sale. Areas of specific focus and capital expenditures include:

(a) Lease and preparation of facilities necessary to house and operate, at minimum, our first of four proposed 25MW manufacturing lines; and

(b) Establishment of a baseline production system to produce full size (100cm × 160cm) sample modules; and

(c) The placement of orders with select vendors for the core and sub-system components necessary to begin assembly leading to the commissioning of the first of four proposed 25MW manufacturing lines; and

(d) Continued R&D efforts to establish enhanced solar cell deposition methods and reduce manufacturing costs.

The purpose of these ongoing investments is to first establish a base TFPV solar module manufacturing infrastructure necessary to produce approximately 25MW of annualized solar module production, and second, to establish a replication process designed to enable us to add the balance of our proposed three additional production lines as rapidly and efficiently as possible.

The following chart summarizes our planned initial production capacity and installation timing:

Manufacturing Facility	Number of Production Lines	Initial Annualized Solar Modules*	Initial Annualized Watts*	Anticipated System Commissioning Date
1st line	1	190,000	25MW	Dec 2008
Addition of 2nd line	1	190,000	25MW	Nov 2009
Addition of 3rd line	1	190,000	25MW	Jan 2010
Addition of 4th line	1	190,000	25MW	Mar 2010
Total Planned	4	760,000	100MW	

* Annualized solar module production rates are based on an initial system utilization rate of 58% (the percentage of system utilization in each 7 day by 24 hour period) and 80% yield (the percentage of product meeting saleable specifications). We plan to ramp-up system utilization and yield to industry standards of 80% & 85% respectively over the course of the first full year of production of each system.

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We anticipate that due to normal production variables we will produce on average marketable solar modules ranging from between 115 to 130 watts each.

Sales and Marketing

Driving our solar module manufacturing plan is what we believe to be the ability to capitalize on long term growth in solar spurred by increasing electrical energy costs and demand. Large markets are developing for commercial operators of private solar farms, utilities meeting green mandates, government subsidized installations, and operators of large commercial and industrial properties. These projects represent large installations typically approaching 1MW or more.

Solar systems installers looking to satisfy the module needs of these large and long term projects are looking for opportunities to secure access to modules supplies. We believe that the design and performance of our solar module is ideally suited for use in these project types, and we further believe that our module production capacities can be pre-sold well into the future.

Target Markets

Our primary target markets for our TFPV solar modules will be applications for On-Grid (facilities tied to conventional power distribution infrastructure) application of 1MW in size and above. Typical applications and buyers would include:

- Solar Farms
  - License Holders in Germany, Spain & Canada
  - US installers servicing commercial and utility scale installations
- Government Agencies (DOD)
  - Bureau of Land Management
  - Department of Defense
- Power Purchase Agreements
  - Renewable Ventures
- Utility Companies
  - Meeting Green Mandates
- Large Commercial Installations

Pricing

Our analysis made in predicting the anticipated sales per watt for module production in the years 2009, 2010, and 2011 was based on several factors. These factors included a review of pricing of both crystalline and thin film per watt sales trends for the previous several years including 2007 pricing trends. Trends were primarily derived from pricing surveys conducted by interviews and an industry watch firm named SolarBuzz.com. The following pricing of both

crystalline and thin film for September 2007 was produced by SolarBuzz.com:

"The lowest retail price for a multicrystalline solar module is $4.11 per watt (€3.00 per watt) from a US retailer. The lowest retail price for a monocrystalline module is $4.30 per watt (€3.14 per watt), also from a US retailer." **And** *"The lowest thin film module price is at $3.49 per watt (€2.55/Wp) per watt from a European retailer. As a general rule, it is typical to expect thin film modules to be at a price discount to crystalline silicon (for like module powers). This thin film price is represented by a 60 watt module."*

The pricing in the thin film category represents modules below 100 watts of stated peak power. Specifically, modules producing total peak power of only 60 watts were priced lowest at $3.49 per watt.

XsunX determined that a key driver in the lower price point for most thin film in relation to crystalline modules was the discount value assigned to the lower total power output per module requiring more modules per installation. As an example, if a 10kW project were to employ the use of 65 watt cadmium telluride

(CdTe) or copper indium gallium selenide (CIGS) modules as opposed to 125 watt amorphous silicon (a-Si) modules, the required number of modules necessary for installation would be approximately 70 more units. Additional units may also be necessary to compensate for thermal coefficient performance loss of a CdTe or CIGS solar cell resulting in power production loss from heat at normal operating temperatures*. In our estimate, this may bring the total number of additional units to an excess of 70 more 65 watt modules for the same project than with the use of a 125 watt amorphous module. To an installer/integrator, the use of more modules would increase overall balance of systems (BOS) cost due to increased labor, mounting hardware, and interconnection cost. We believe that integrators may demand lower per watt price points for certain modules over others as a result of these additional system costs.

In developing price points for the XsunX ASI-120 module, we determined that the rated power output of our device struck a balance between higher energy density crystalline modules and the lower power 60 to 75 watt products offered by other TFPV manufactures such as First Solar, Sharp, and ECD. The following chart reviews our factory per watt pricing assumptions based on integrator interviews, industry publications, and our manufacturing cost assumptions.

Period	Crystalline	Thin-Film < 100 watt	XsunX Thin Film > 120 watt
2009	$ 3.25	$ 2.25	$ 2.60
2010	$ 3.00	$ 2.00	$ 2.40
2011	$ 2.90	$ 1.75	$ 2.00

* NOTE: Solar technologies such as silicon wafer, CdTe, and CIGS exhibit performance loss due to heat. While the factory rated “Peak” power is determined at 25 degrees centigrade, real world operating temperatures average 65 degrees centigrade. This potential 40 degree increase can affect different solar technologies in varying percentages of approximately ¼ to ½ percent per degree in conversion efficiency. This results in an approximate reduction in efficiency at the “Peak” period (noon) of about 10% to 20%. To place this in perspective, a 100 watt module (silicon wafer, CdTe, CIGS) would deliver approximately 90 to 80 watts of power during the peak periods while operating at 65 degrees centigrade. Amorphous silicon does not experience the same degree of performance degradation, realizing only about 3% or less performance loss.

Sales & Distribution

In anticipation of commercial production, we have developed a pre-sales reservation program, based upon the solar module manufacturing industry’s policy of pre-selling manufacturing capacity to system installers and large users of solar. This is intended to aid in building a sales channel, loading that channel with customers interested in purchasing our future module production, and developing brand presence and recognition as early as possible. The program enables qualified, interested parties to specify the amount of solar module capacity they anticipate purchasing at favorable per watt pricing. As of the date of this report, we have signed reservation agreements with solar system integrators indicating interest in over 100MW of production in calendar 2008, 2009, 2010. Our agreements provide for the payment of a 5% deposit based on the 2009 calendar year purchase commitment either prior to, or not later than, 30 days after the delivery by XsunX to the reserving party of commercial samples for evaluation. The information in this paragraph is designed to summarize the general terms of the pre-sales reservation program and market opportunities. It is not intended to provide guidance about our future operating results, including revenues or profitability.

Product and Technology Development

Since our initial reorganization in October 2003 through the second period ended March 2007, we have focused the majority of our operational budgets towards the development of technological infrastructure, research and development of solar cell device types and manufacturing techniques, and the licensure of certain patented and patent pending technologies related to solar cell devices and manufacturing techniques. We focused on the solar cell structure and thin film manufacturing processes for amorphous and microcrystalline materials. The primary business purpose for these efforts was to establish intellectual property and “know how” that could be sold and/or licensed to third parties for use in the development of their respective solar product businesses. Over this period, we committed approximately $4,069,981 towards the above product and technical “know how” development.

In March 2007, we re-evaluated our business development and technology plans and launched efforts to prepare a plan to grow XsunX through the manufacturing and sales of TFPV solar modules. Our proposed expansion into solar module manufacturing required that we develop additional technical expertise in the areas of large area cell integration and packaging techniques necessary to produce commercially viable solar modules. Between March 2007 and the period ended September 30, 2007 we focused on the development of a TFPV solar module design, an integrated manufacturing and assembly line, attracting government incentive programs to offset start-up and initial operations costs of our proposed facilities, and the qualification of systems and material vendors to supply the manufacturing equipment and materials necessary to establish and operate our proposed manufacturing facilities.

We anticipate that for the foreseeable future the core of our operations and efforts will focus on the establishment of TFPV solar module manufacturing capabilities. Separately, we continue to explore opportunities with parties interested in the licensing and cooperative commercial development and use of our semi-transparent TFPV technologies.

The Company continues to develop additional processes, techniques, and device designs. These research and development efforts may provide the Company with additional proprietary technology that may lead to the filing of new provisional and patent applications.

Intellectual Property

In September 2003 the Company was assigned the rights to three patents as part of an Asset Purchase Agreement with Xoptix Inc., a California corporation. The patents acquired were No. 6,180,871 for Transparent Solar Cell and Method of Fabrication (Device), granted on January 30, 2001; No. 6,320,117 for Transparent Solar Cell and Method of Fabrication (Method of Fabrication), granted on November 20, 2001; and No. 6,509,204 for Transparent Solar Cell and Method of Fabrication (formed with a Schottky barrier diode and method of its manufacture), granted on January 21, 2003.

XsunX licensed the patent and technology portfolio of MVSystems, Inc., a Colorado corporation (“MVSystems”) in September 2004 and then later expanded our use rights under the license in October 2005. The patents acquired were Semiconductor Vacuum Deposition System And Method Having A Reel-To-Reel Substrate Cassette: US6, 258,408 B1: July 10th, 2001 (Method of Fabrication); and US Provisional Patent Application serial number 60/536,151- three terminal and four terminal solar cells, solar cell panels, and method of manufacture (Device and Method of Fabrication). The license granted XsunX the royalty free exclusive rights for use by XsunX in its pursuit to establish a commercially viable process for the manufacture of TFPV solar cells and accordingly, included all MVSystems technology, know how, and resources which are part of or related to the licensed patents and technology that was then or may become applicable or beneficial to the furtherance of the business objectives of XsunX in the future. The license was exclusive as to technology pertaining to the XsunX field of use as it pertains to the business of developing, commercializing and licensing processes for the manufacture of solar cells or photovoltaic technologies.

Effective January 1, 2007 we entered into a cooperative development agreement with Sencera, LLC for the licensure and development of a Sencera patent pending plasma source for use in the manufacture of deposited thin-film solar cells. Under the terms of the agreement, XsunX and Sencera entered into a Technology Development and License Agreement, providing for a phased program to further develop and proof the Sencera plasma source for use in the manufacture of deposited thin-film solar cells. In connection with the agreement, Sencera issued XsunX a seven (7) year royalty based license that provides XsunX with exclusivity in the area of the XsunX field of use as claimed in U.S. Patent No. 6,180,871; 6,320,117; 6,509,204; 6,488,777; 6,258,408; 6,472,622; and (b) as claimed in U.S. Provisional Application No. 60/536,151; and (c) for use in semi-transparent photovoltaic devices, multi-terminal photovoltaic devices, and cassette-based roll-to-roll manufacturing equipment.

The Company continues to develop additional processes, techniques, and device designs. These research and development efforts may provide the Company with additional proprietary technology that may lead to the filing of new provisional and patent applications.

Company History

XsunX is a Colorado corporation formerly known as Sun River Mining Inc. (“Sun River”). The Company was originally incorporated in Colorado on February 25, 1997. Effective September 24, 2003, the Company completed a Plan of Reorganization and Asset Purchase Agreement (the “Plan”).

Pursuant to the Plan, the Company acquired the following three patents from Xoptix, Inc., a California corporation for Seventy Million (70,000,000) shares of common stock (post reverse split one for twenty): No. 6,180,871 for Transparent Solar Cell and Method of Fabrication (Device), granted on January 30, 2001; No. 6,320,117 for Transparent Solar Cell and Method of Fabrication (Method of Fabrication), granted on November 20, 2001; and No. 6,509,204 for Transparent Solar Cell and Method of Fabrication (formed with a Schottky barrier diode and method of its manufacture), granted on January 21, 2003.

Pursuant to the Plan, the Company authorized the issuance of 110,530,000 (post reverse split) common shares. Prior to the Plan the Company had no tangible assets and insignificant liabilities. Subsequent to the Plan, the Company completed its name change from Sun River Mining, Inc. to XsunX, Inc. The transaction was completed on September 30, 2003.

Government Contracts

There are no government contracts at this time.

Competitive Conditions

Currently, management is aware of other amorphous silicon and thin film products similar to those proposed for manufacture by us on the market. Although similar in respect to the operation and use of these technologies, the Company believes the design of our large area TFPV solar module delivering 125 watts of DC power provides marketable improvements over other thin film products offering less total power output per module technologies. We believe our design will require fewer TFPV solar panels per installation compared to the use of other thin film systems, thereby reducing the overall costs associated with mounting, installation, wiring, and interconnection of fewer parts and pieces.

However, a number of solar cell technologies have and are being developed by other companies. Such technologies include amorphous silicon, cadmium telluride, copper-indium-gallium-selenide (CIGS), and copper indium diselenide as well as advanced concepts in thin film crystalline silicon, and the use of organic materials. Given the benefit of time, investment, and advances in manufacturing technologies any of these competing technologies may be offered in formats delivering power similar or greater to our design, and they may also achieve manufacturing costs per watt lower than our cost per watt to manufacture a TFPV solar module.

In accessing the principal competitive factors in the market for solar electric power products, we use price per watt, stability and reliability, conversion efficiency, diversity in use applications, and other performance metrics such as scalability of manufacturing processes and the ability to adapt new technologies into cell designs and the manufacturing process without antiquation of existing infrastructure. If we do not compete successfully with respect to these or other factors, it could materially and adversely affect our business, results of operations, and financial condition.

A number of large companies are actively engaged in the development, manufacturing and marketing of solar electric power products. The five largest TFPV cell suppliers are Q-Cells Shell Solar, Sharp Corporation, BP Solar, Kyocera Corporation, First Solar, and Energy Conversion Devices, which together supply the significant portion of the current TFPV market. All of these companies have greater resources to devote to research, development, manufacturing and marketing than we do.

Other competitive factors lie in the current use of other clean, renewable energy technologies such as wind, ocean thermal, ocean tidal, and geo-thermal power sources and conventional fossil fuel based technologies for the production of electricity. We expect our primary competition will be within the solar cell marketplace itself. Barriers to entering the solar cell manufacturing industry include the technical know-how required to produce solar cells that maintain acceptable efficiency rates, the design of efficient and scalable manufacturing processes, and access to necessary manufacturing infrastructure.

Compliance with Environmental Laws and Regulations

The operations of the Company are subject to local, state and federal laws and regulations governing environmental quality and pollution control. To date, compliance with these regulations by the Company has had no material effect on the Company's operations, capital, earnings, or competitive position, and the cost of such compliance has not been material. The Company is unable to assess or predict at this time what effect additional regulations or legislation could have on its activities.

Employees and Consultants

The Company is a development stage company and as of September 30, 2007 had 6 salaried employees. This represents an increase of 1 employee over the same period ended 2006. The Company also engages several consultants to perform specific functions that otherwise would require an employee. The Company projects that during the next 12 months the Company's workforce is likely to increase to 22, with 2 of the new employees being in Administrative, 2 in Marketing and Sales positions, 5 Scientific and Technical positions, 4 in Manufacturing Technicians, and 3 in Administrative Support. In addition to the anticipated retention of new employees the Company expects to expand its use of strategic relationships to leverage industry expertise in areas of design, systems automation, manufacturing and assembly to augment product commercialization time lines and the delivery of technologies. The Company may find a need to engage additional full-time employees as necessary.

Scientific Advisory Board

In September 2004 the Company established the XsunX Scientific Advisory Board to attract qualified specialists from the fields of material and device engineering. During the fiscal year 2007, the membership of the advisory board was enhanced to reflect the current operational status of the Company. It is anticipated that panel members will be engaged for a period of two years. The qualifications and biographical information for the members of the panel are as follows:

Dr. John J. Moore — Chairman Scientific Advisory Board

Dr. John J. Moore is a Materials Scientist who currently holds the position of Trustees' Professor and Head of Department of Metallurgical and Materials Engineering at the Colorado School of Mines. Dr. Moore is also Director of the interdisciplinary graduate program in Materials Science and Director of the Advanced Coatings and Surface Engineering Laboratory, ACSEL, at the Colorado School of Mines in Golden. He has been at the Colorado School of Mines since 1989.

Dr. Moore was awarded a B.Sc. in Materials Science and Engineering from the University of Surrey, UK, in 1966, a Ph.D. in Industrial Metallurgy from the University of Birmingham, UK, in 1969, and a D.Eng. from the School of Materials of the University of Birmingham, UK, in 1996. Dr. Moore worked as a Student Apprentice at Stewarts and Lloyds Ltd., UK, from 1962 to 1966, and as Manager of Industrial Engineering and Production Control at Birmid-Qualcast Industries Ltd., UK, the largest die casters in Europe at the time, from 1969 to 1974.

Prior to his appointment at the Colorado School of Mines, Dr. Moore served as Professor & Head, Department of Chemical and Materials Engineering, University of Auckland, New Zealand, from 1986 to 1989; Professor of Metallurgical Engineering at the University of Minnesota, USA, from 1979 to 1986, and Senior Lecturer of Chemical Metallurgy at Sandwell College, England, from 1974 to 1979.

Dr. Moore has published more than 500 papers in materials science and engineering journals, holds 13 patents, and has been the author or co-auth or editor of 9 books. Dr. Moore is a Fellow of the Institute of Materials (UK), a Fellow ASM International, a Fellow of the American Ceramic Society, and a Chartered Engineer, (C.Eng.), in the UK. Dr. Moore is also an Honorary Professor and has been awarded an Honorary Doctorate from the Moscow State Institute of

Steels and Alloys, Russia.

10

Dr. Richard K. Ahrenkiel, Member Scientific Advisory Board

Richard K. Ahrenkiel is currently a Research Professor of Metallurgical and Materials Engineering at the Colorado School of Mines in Golden, Colorado. He is also a Consultant and Research Fellow Emeritus at the National Renewable Energy Laboratory (NREL), (formerly the Solar Energy Research Institute) Golden,

Colorado, where he worked from 1981 to 2005. He became a Research Fellow at NREL in 2000. His area of specialization is the measurement and characterization of photovoltaic cells and materials. He also works in photovoltaic device design and modeling. He received a B.S. degree in Engineering Physics and the M.S. and Ph.D degrees in Physics at the University of Illinois, Urbana. He joined the staff of the Research Laboratories of the Eastman Kodak Company. From 1972-76, he worked on the newly founded electronic photography project using silicon charge coupled devices as sensing elements. He joined Laser Division of the Los Alamos National Laboratory in 1976 (then LASL), and in 1978, he became a Group Leader in the Electronics Division of LANL. He is a Fellow of the American Physical Society, the Institute of Electrical and Electronic Engineers (IEEE), the American Vacuum Society, and the Optical Society of America.

Edward T. Yu, Member Scientific Advisory Board

Edward T. Yu is currently Professor of Electrical and Computer Engineering at the University of California, San Diego (UCSD). He received his A.B. (summa cum laude) and A.M. degrees in Physics from Harvard University in 1986, and his Ph.D. degree in Applied Physics from the California Institute of Technology in 1991. From 1986 to 1989 he was a National Science Foundation Doctoral Fellow, and from 1989 to 1991 he was an AT&T Bell Laboratories Ph.D. Scholar, holding both appointments at Caltech. From 1991 to 1992 he was a Postdoctoral Fellow at the IBM Thomas J. Watson Research Center in Yorktown Heights, NY. From 1992 to 1996 he was Assistant Professor of Electrical and Computer Engineering at UCSD, and from 1996 to 1998 he was Associate Professor. He has held his current appointment as Professor since 1998. Dr. Yu also serves currently as a member of the DARPA Defense Sciences Research Council.

At UCSD Professor Yu directs a research laboratory concerned generally with the characterization, understanding, and application of physical phenomena and of solid-state material and device properties at nanometer to atomic length scales. Current research interests in his group include III-V nitride heterostructure materials and device physics; scanning probe characterization of advanced electronic materials and devices; solid-state nanoscience and nanotechnology; and photovoltaics and other technologies for energy generation. The results of his research have been reported in over 120 refereed journal publications and over 175 conference and seminar presentations.

Dr. Michael A. Russak, Member Scientific Advisory Board

Dr. Michael A. Russak has been working as a consultant in the hard disk drive and photovoltaic industries since Jan 2007. He is also currently the Executive Director of IDEMA-U.S. (the hard disk drive industry trade association) and a member of the Board of Directors and Scientific Advisory Board of XsunX, Inc. From 2001 to 2006 he was President and Chief Technical Officer of Komag, Inc., a manufacturer of hard magnetic recording disks for hard disk drive applications. From 1993 to 2001 he was Chief Technical Officer of HMT Technology, Inc. also a manufacturer of magnetic recording disks. From 1985 to 1993 he was a research staff member and program manager in the Research Division of the IBM Corporation. Dr. Russak has over thirty five years of industrial experience progressing from a research scientist to senior executive officer of two public companies. He has expertise in thin film materials and devices for magnetic recording, photovoltaic, solar thermal applications, semiconductor devices as well as glass, glass-ceramic and ceramic materials. He also has over twelve years experience at the executive management level of public companies with significant off shore development and manufacturing functions. He received his B.S. in Ceramic Engineering in 1968 and Ph.D. in Materials Science in 1971, both from Rutgers University in New Brunswick, NJ. During his career, he has been a contributing scientist and program manager at the Grumman

Aerospace Corporation, a Research Staff Member and technical manager in the areas of thin film materials and processes at the Research Division of the IBM Corporation at the T.J. Watson Research Laboratories. In 1993, he joined HMT Technology, a manufacturer of thin film disks for magnetic storage, as Vice President of Research and Development. His responsibilities included new product design and introduction. Dr. Russak became Chief Technical Officer of HMT and held that position until 2000 when HMT merged with Komag Inc. Dr. Russak was appointed President and Chief Technical Officer of the combined company. He continued to set technical, operational and business direction for Komag until his retirement at the end of 2006. He has published over 90 technical papers, and holds 23 U.S. patents.

Available Information

Our website address is www.xsunx.com. We make available on our website access to our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports that we have filed with the Securities and Exchange Commission ("SEC"). The information found on our website is not part of this or any other report we file with, or furnish to, the SEC.

Item 1A. Risk Factors

An investment in our stock involves a high degree of risk. You should carefully consider the following risk factors, as well as the other information in this Annual Report on Form 10-K, in evaluating XsunX and our business. If any of the following risks occur, our business, financial condition and results of operations could be materially and adversely affected. Accordingly, the trading price of our common stock could decline and you may lose all or part of your investment in our common stock. The risks and uncertainties described below are not the only ones we face. Additional risks that we currently do not know about or that we currently believe to be immaterial may also impair our business operations.

We have not generated any significant revenues and may never achieve profitability.

We are a development stage company and, to date, have not generated any significant revenues. From inception through September 30, 2007, we had an accumulated deficit of $10,197,938. We cannot assure you that we can achieve or sustain profitability in the future. Our operations are subject to the risks and competition inherent in the establishment of a business enterprise. There can be no assurance that future operations will be profitable. Revenues and profits, if any, will depend upon various factors, including whether our product development can be completed, and if it will achieve market acceptance. We may not achieve our business objectives and the failure to achieve such goals would have an adverse impact on us.

We expect that we will need to obtain significant additional financing to continue to operate our business, including significant capital expenditures to install our initial 25MW per annum production capacity, and financing may be unavailable or available only on disadvantageous terms.

We have in the past experienced substantial losses and negative cash flow from operations and have required financing, including equity and debt financing, in order to pursue the commercialization of products based on our technologies. We expect that we will continue to need significant financing to operate our business, including capital expenditures to install our planned production capacity.

On November 1, 2007, XsunX signed a $21 million common stock purchase agreement with Fusion Capital Fund II, LLC, an Illinois limited liability Company ("Fusion Capital"). Upon signing the agreement, XsunX received $1,000,000 from Fusion Capital as an initial purchase under the $21 million commitment in exchange for 3,333,332 shares of our common stock. The shares were issued in a transaction exempt from registration pursuant to Section 4(2) of the Securities Act of 1933. Concurrently with entering into the common stock purchase agreement, we entered into a registration rights agreement with Fusion Capital. Under the registration rights agreement, we agreed to file a registration statement related to the transaction with the U.S. Securities & Exchange Commission ("SEC") covering the shares that have been issued or may be issued to Fusion Capital under the common stock purchase agreement. After the SEC has declared effective the registration statement related to the transaction we have the right over a 25-month period to sell our shares of common stock to Fusion Capital, from time to time, in amounts up to $1 million per sale, depending on certain conditions as set forth in the agreement, up to the full aggregate commitment of $21 million. See Item 9B: Other Information, "Sale of Unregistered Securities and Financing Agreement".

There can be no assurance that such additional financing will be available or that the terms of such additional financing, if available, will be acceptable to us. If additional financing is not available or not available on terms acceptable to us, our ability to fund our operations, develop and install or expand our manufacturing operations and sales network, maintain our research and development efforts or otherwise respond to competitive pressures may be significantly impaired.

We are working to establish our manufacturing capacity for TFPV products in order to meet anticipated demand, and our revenues and profits will depend upon our ability to successfully complete our initial 25MW of manufacturing capacity and then to sell our TFPV products at volumes to match our available production capacity.

We are working to establish initial manufacturing capacity of 25MW per annum and plan to expand manufacturing capacity to 100MW per annum by 2010. This plan includes adding a new facility in Oregon. We will be installing and testing the equipment for this manufacturing facility internally and through third parties. We may experience delays, additional or unexpected costs and other adverse events in connection with our projects, including those associated with the equipment we purchase from third parties. Additionally, there can be no assurance that market demand will absorb our manufacturing capacity or that our marketing capabilities will be successful. As a result, we may not be able to realize revenues and profits based upon the expected capacity, or we may experience delays or reductions in these revenues and profits, and our business could be materially adversely affected.

Continued research and development efforts will be required to improve or maintain competitiveness of our products, and there can be no assurance that such efforts will be successful.

There can be no assurance that such research and development efforts will be successful or that we will be able to develop commercial applications for our products and technologies. Further, the areas in which we are developing technologies and products are characterized by rapid and significant technological change. Rapid technological development may result in our products becoming obsolete or noncompetitive. If future products based on our technologies cannot be developed for manufacture and sold commercially or our products become obsolete or noncompetitive, we may be unable to recover our investments or achieve profitability. In addition, the commercialization schedule may be delayed if we experience delays in meeting development goals, if products based on our technologies exhibit technical defects, or if we are unable to meet cost or performance goals. In this event, potential purchasers of products based on our technologies may choose alternative technologies and any delays could allow potential competitors to gain market advantages.

There is no assurance that the market will accept our products once commercial-scale manufacturing has been achieved.

There can be no assurance that products based on our technologies will be perceived as being superior to existing products or new products being developed by competing companies or that such products will otherwise be accepted by consumers. The market prices for products based on our technologies may exceed the prices of competitive products based on existing technologies or new products based on technologies currently under development by competitors. There can be no assurance that the prices of products based on our technologies will be perceived by consumers as cost-effective or that the prices of such products will be competitive with existing products or with other new products or technologies. If consumers do not accept products based on our technologies, we may be unable to recover our investments or achieve profitability.

Other companies, many of which have greater resources than we have, may develop competing products or technologies which cause products based on our technologies to become noncompetitive.

We will be competing with firms, both domestic and foreign, that perform research and development, as well as firms that manufacture and sell solar products. In addition, we expect additional potential competitors to enter the markets for solar products in the future. Some of these current and potential competitors are among the largest industrial companies in the world with longer operating histories, greater name recognition, access to larger customer bases, well-established business organizations and product lines and significantly greater resources and research and development staff and facilities. There can be no assurance that one or more such companies will not succeed in developing technologies or products that will become available for commercial sale prior to our products, that will have performance superior to products based on our technologies or that would otherwise render our products

noncompetitive. If we fail to compete successfully, our business would suffer and we may lose or be unable to gain market share.

The loss of strategic relationships used in the development of our products and the systems and components to our planned 25MW manufacturing system could impede our ability to complete our product and/or our initial manufacturing system and result in a material adverse effect causing our business to suffer.

We have established a plan of operations under which a portion of our operations rely on strategic relationships with third parties, to provide systems design, assembly and support. A loss of any of our third party relationships for any reason could cause us to experience difficulties in implementing our business strategy. There can be no assurance that we could establish other relationships of adequate expertise in a timely manner or at all.

We may suffer the loss of key personnel or may be unable to attract and retain qualified personnel to maintain and expand our business.

Our success is highly dependent on the continued services of a limited number of skilled managers, scientists and technicians. The loss of any of these individuals could have a material adverse effect on us. In addition, our success will depend upon, among other factors, the recruitment and retention of additional highly skilled and experienced management and technical personnel. There can be no assurance that we will be able to retain existing employees or to attract and retain additional personnel on acceptable terms given the competition for such personnel in industrial, academic and nonprofit research sectors.

Raw material costs could impact our cost of goods and our ability to successfully develop our products and technologies.

Higher costs for certain raw materials and commodities, principally glass, resin-based polymers and industrial gases, as well as higher energy costs, could negatively impact our cost of operations. While we have developed strategies to mitigate or partially offset the impact of higher raw material, commodity and energy costs, there can be no assurances such measures will be successful. In addition, no assurances can be given that the magnitude and duration of these cost increases or any future cost increases will not have a larger adverse impact on our profitability and consolidated financial position than currently anticipated. As part of our planned research and development activities, we are attempting to reduce costs through improved automation and substitution strategies. There can be no assurances that we will succeed in these future cost-reduction efforts, which may be essential for the continued development of our competitive presence.

Indemnification of Officers and Directors.

The Colorado Business Corporation Act provides for the indemnification of its directors, officers, employees, and agents, under certain circumstances, against attorney’s fees and other expenses incurred by them in any litigation to which they become a party arising from their association with or activities on behalf of the Company. The Company will also bear the expenses of such litigation for any of its directors, officers, employees, or agents, upon such person’s promise to repay the Company therefore if it is ultimately determined that any such person shall not have been entitled to indemnification. This indemnification policy could result in substantial expenditures by the Company which it will be unable to recoup.

Director’s Liability Limited.

The Colorado Business Corporation Act excludes personal liability of its directors to the Company and its stockholders for monetary damages for breach of fiduciary duty except in certain specified circumstances. Accordingly, the Company will have a much more limited right of action against its directors than otherwise would be the case. This provision does not affect the liability of any director under federal or applicable state securities laws.

Effective Internal Controls.

As a public company, we are required to document and test our internal control procedures in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act, which will require annual management assessments of the effectiveness of our internal control over financial reporting and a report by our independent registered public accounting firm that both addresses management's assessment of the effectiveness of internal control over financial reporting and the effectiveness of internal control over financial reporting. During the course of our testing, we may identify deficiencies which we may not be able to remediate in time to meet our deadline for compliance with Section 404. Testing and maintaining internal controls can divert our management's attention from other matters that are important to our business. We also expect the new regulations to increase our legal and financial compliance cost, make it more difficult to attract and retain qualified officers and members of our board of directors (particularly to serve on an audit committee) and make some activities more difficult, time consuming and costly. We may not be able to conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with Section 404. Our independent registered public accounting firm may not be able or willing to issue an unqualified report on the effectiveness of our internal control over financial reporting. If we conclude that our internal control over financial reporting is not effective, we cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or their effect on our operations since there is presently no precedent available by which to measure compliance adequacy. If we are unable to conclude that we have effective internal control over financial reporting or our independent auditors are unable to provide us with an unqualified report as required by Section 404, then we may be unable to continue to have our common stock traded on the Over the Counter Bulletin Board and investors could lose confidence in our reported financial information, which could have a negative effect on the trading price of our stock.

The following risks relate principally to our common stock and its market value:
Our Common Stock is deemed a low-priced "Penny" stock, therefore an investment in our Common Stock should be considered high risk and subject to marketability restrictions.

Since our Common Stock is a penny stock, as defined in Rule 3a51-1 under the Exchange Act, it will be more difficult for investors to liquidate their investment. Until the trading price of the Common Stock rises above $5.00 per share, if ever, trading in our Common Stock is subject to the penny stock rules of the Exchange Act specified in rules 15g-1 through 15g-10. Those rules require broker-dealers, before effecting transactions in any penny stock, to:

- Deliver to the customer, and obtain a written receipt for, a disclosure document;
- Disclose certain price information about the stock;
- Disclose the amount of compensation received by the broker-dealer or any associated person of the broker-dealer;
- Send monthly statements to customers with market and price information about the penny stock; and
- In some circumstances, approve the purchaser's account under certain standards and deliver written statements to the customer with information specified in the rules.

Consequently, the penny stock rules may restrict the ability or willingness of broker-dealers to sell our Common Stock and may affect the ability of holders to sell their Common Stock in the secondary market and the price at which such holders can sell any such securities. These additional procedures could also limit our ability to raise additional capital

in the future.

No Foreseeable Dividends. We have never paid cash dividends on our common stock and do not anticipate paying cash dividends in the foreseeable future. The payment of dividends on our common stock will depend on earnings, financial condition and other business and economic factors affecting it at such time as the board of directors may consider relevant. If we do not pay dividends, our common stock may be less valuable because a return on your investment will only occur if its stock price appreciates.

Limited Public Market. There is only a limited public market for the Company's common stock, and no assurance can be given that a market will continue or that a shareholder ever will be able to liquidate his investment without considerable delay, if at all. If a market should continue, the price may be highly volatile. Factors such as those discussed in this "Risk Factors" section may have a significant impact upon the market price of the securities offered hereby. Due to the low price of the securities, many brokerage firms may not be willing to effect transactions in the securities. Even if a purchaser finds a broker willing to effect a transaction in these securities, the combination of brokerage commissions, state transfer taxes, if any, and any other selling costs may exceed the selling price. Further, many lending institutions will not permit the use of such securities as collateral for any loans.

Stock Volatility. The market price of our common stock is likely to be highly volatile and could fluctuate widely in price in response to various factors, many of which are beyond our control, including:

- technological innovations or new products and services by us or our competitors;
- additions or departures of key personnel;
- sales of our common stock;
- our ability to integrate operations, technology, products and services;
- our ability to execute our business plan;
- operating results below expectations;
- loss of any strategic relationship;
- industry developments;
- economic and other external factors; and
- period-to-period fluctuations in our financial results.

Because we have a limited operating history with limited revenues to date, you may consider any one of these factors to be material. Our stock price may fluctuate widely as a result of any of the above listed factors.

In addition, the securities markets have from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. These market fluctuations may also materially and adversely affect the market price of our common stock.

Item 1B. Unresolved Staff Comments

(None)

Item 2. Properties

As of September 30, 2007 the Company leased administrative office facilities located at 65 Enterprise, Aliso Viejo CA 92656 for approximately $3,800 per month.

In April 2006 the Company entered into a three year lease for technical and marketing operations facilities in Golden, CO. The Company provided a $2,615 security deposit and expensed $79,867 in costs associated with tenant improvements to the facilities in preparation for occupancy. The following is a schedule, by years, of the minimum base payments required under this operating lease for facilities. An additional $905 monthly is also due as a pro rata share equaling 4.12% of the operating costs for real estate taxes, assessments, and the expenses of operating and maintaining common areas within the commercial grounds surrounding the leased facilities.

Annual Rent Schedule	Rate/sf	Annualized Rent	Monthly Rent