COSTAR TECHNOLOGIES, INC.
AND SUBSIDIARIES
(FORMERLY KNOWN AS SIELOX, INC.)

CONSOLIDATED FINANCIAL STATEMENTS
AND
INDEPENDENT ACCOUNTANTS' REVIEW REPORT

DECEMBER 31, 2011 AND 2010

Rothstein Kass

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES
(FORMERLY KNOWN AS SIELOX, INC.)

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INDEPENDENT ACCOUNTANTS' REVIEW REPORT

To the Board of Directors and Stockholders of
Costar Technologies, Inc.

We have reviewed the accompanying consolidated balance sheets of Costar Technologies, Inc. and Subsidiaries (collectively, the "Company) (formerly known as Sielox, Inc.) as of December 31, 2011 and 2010, and the related consolidated statements of operations, changes in stockholders' equity and comprehensive income, and cash flows for the years then ended. A review includes primarily applying analytical procedures to management's financial data and making inquiries of company management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the consolidated financial statements as a whole. Accordingly, we do not express such an opinion.

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America and for designing, implementing, and maintaining internal control relevant to the preparation and fair presentation of the consolidated financial statements.

Our responsibility is to conduct the review in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance that there are no material modifications that should be made to the consolidated financial statements. We believe that the results of our procedures provide a reasonable basis for our report.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying consolidated financial statements in order for them to be in conformity with accounting principles generally accepted in the United States of America.

Rothstein Kass

Dallas, Texas
April 20, 2012

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES
(FORMERLY KNOWN AS SIELOX, INC.)

CONSOLIDATED BALANCE SHEETS
(AMOUNTS SHOWN IN THOUSANDS)

December 31,	2011	2010
ASSETS		
Current assets		
Cash	$ 193	$ 407
Accounts receivable, less allowance for doubtful accounts of $107 and $140 in 2011 and 2010, respectively	2,907	2,023
Inventories, net of reserve for obsolescence of $675 and $264 in 2011 and 2010, respectively	6,859	4,694
Prepaid expenses	483	335
Current assets of discontinued operations		10
Total current assets	10,442	7,469
Non-current assets		
Property and equipment, net	128	48
Trade names	925	800
Distribution agreement, net	1,064	1,137
Customer relationships, net	255	400
Covenant not to compete	47	
Promissory note	500	500
Total assets	$ 13,361	$ 10,354
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities		
Current liabilities		
Accounts payable	$ 2,722	$ 1,574
Accrued expenses and other	129	285
Lines of credit	2,974	626
Current liabilities of discontinued operations		75
Current liabilities, contingent purchase price	100	285
Total current liabilities	5,925	2,845
Long term liability, contingent purchase price		9
Total liabilities	5,925	2,854
Stockholders' Equity		
Common stock	42	42
Additional paid in capital	155,839	155,805
Accumulated other comprehensive income		260
Accumulated deficit	(143,921)	(144,083)
Less common stock held in treasury	(4,524)	(4,524)
Total stockholders' equity	7,436	7,500
Total liabilities and stockholders' equity	$ 13,361	$ 10,354

See independent accountants' review report and notes to consolidated financial statements

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES
(FORMERLY KNOWN AS SIELOX, INC.)

CONSOLIDATED STATEMENTS OF OPERATIONS
(AMOUNTS SHOWN IN THOUSANDS)

Years Ended December 31,	2011	2010
Net revenues	$ 17,341	$ 12,656
Cost of revenues	13,141	9,288
Gross profit	4,200	3,368
Selling, general and administrative expenses	4,156	4,051
Income (loss) from operations	44	(683)
Other income (expenses)		
Interest expense	(143)	(128)
Other income and expense, net	262	3
Total other income (expense), net	119	(125)
Net income (loss) from continuing operations	163	(808)
Net income (loss) from discontinued operations	(1)	450
Net income (loss)	$ 162	$ (358)
Per share of common stock		
Income (loss) from continuing operations	$ 0.00	$ (0.01)
Income (loss) from discontinued operations	(0.00)	0.00
Net income (loss) per share	$ 0.00	$ (0.01)
Weighted average shares outstanding	36,183	35,721

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES
(FORMERLY KNOWN AS SIELOX, INC.)

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME
(AMOUNTS SHOWN IN THOUSANDS)

Years Ended December 31, 2011 and 2010

	Common Stock		Additional Paid - In	Treasury Stock		Accumulated Other Comprehensive	Accumulated	Total Stockholders'	Comprehensive
	Shares	Amount	Capital	Shares	Amount	Income	Deficit	Equity	Income (loss)
Balances at January 1, 2010	42,017	$ 42	$ 155,805	6,296	$ (4,524)	$ 260	$ (143,725)	$ 7,858	
Net loss							(358)	(358)	$ (358)
Comprehensive loss for the year									$ (358)
Balances at December 31, 2010	42,017	$ 42	$ 155,805	6,296	$ (4,524)	$ 260	$ (144,083)	$ 7,500	
Net Income							162	162	$ 162
Change in other accumulated comprehensive income						(260)		(260)	(260)
Stock based compensation	462		34					34	
Comprehensive loss for the year									$ (98)
Balances at December 31, 2011	42,479	$ 42	$ 155,839	6,296	$ (4,524)	$ -	$ (143,921)	$ 7,436	

COSTAR TECHNOLOGIES, INC. AND SUBSIDIARIES
(FORMERLY KNOWN AS SIELOX, INC.)

CONSOLIDATED STATEMENTS OF CASH FLOWS
(AMOUNTS SHOWN IN THOUSANDS)

Years Ended December 31,	2011	2010
Cash flows from operating activities		
Net income (loss) from continuing operations	$ 163	$ (808)
Net income (loss) from discontinued operations	(1)	450
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Stock-based compensation	34	
Depreciation and amortization	390	416
Provision for doubtful accounts	(33)	(114)
Provision for obsolete inventory	408	74
Unrealized gain on other assets	(260)	
Changes in operating assets and liabilities:		
Accounts receivable, net	(778)	(334)
Inventory	(2,237)	(345)
Prepaid expenses	(148)	(151)
Other assets		22
Accounts payable	1,056	752
Accrued expenses and other	(156)	196
Net cash provided by (used in) operating activities	(1,562)	158
Net cash used in discontinued operations	(65)	(759)
Net cash used in operating activities	(1,627)	(601)
Cash flows from investing activities		
Purchase of property and equipment	(124)	
Payment of earnout provision related to Southern Imaging	(294)	(260)
Business purchase related to IVS	(517)	
Net cash used in investing activities of continuing operations	(935)	(260)
Net cash provided by investing activities of discontinued operations		2,547
Net cash provided by (used in) investing activities	(935)	2,287
Cash flows from by financing activity		
Proceeds (repayment) on lines of credit	2,348	(1,503)
Net increase (decrease) in cash	(214)	183
Cash, beginning of year	407	234
Cash, end of year	$ 193	$ 417
Cash of continuing operations	$ 193	$ 407
Cash of discontinued operations	$	$ 10
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	$ 143	$ 305
Cash paid during the year for taxes	$ 56	$ 52
Supplemental disclosure of non-cash investing activities:		
Promissory note received in connection with Sielox, LLC sale	$	$ 500

1. Nature of operations

Costar Technologies, Inc. (formerly known as Sielox, Inc.) ("Costar Technologies") was incorporated in the State of Delaware in February 1997 under the name "Fairmarket, Inc.". Costar Technologies, and its wholly owned subsidiaries, Costar Video Systems, LLC ("Costar") and LQ Corporation ("LQ") (collectively the "Company"), develops, designs and distributes a range of security solution products such as surveillance cameras, lenses, digital video recorders and high speed domes. The Company also develops designs and distributes industrial vision products to observe repetitive production and assembly lines, thereby increasing efficiency by detecting faults in the production process. Through December 31, 2010, the Company operated with another wholly-owned subsidiary, Sielox, LLC ("Sielox"). Sielox ran the Company's operations related to its access control systems.

As of December 31, 2010, the Company sold substantially all of its assets in its wholly-owned subsidiary, Sielox. The results of Sielox's operations have been classified in discontinued operations for the years ended December 31, 2010 (See Note 5).

2. Summary of significant accounting policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and include the accounts of Costar Technologies and its wholly owned subsidiaries, Costar and LQ, for the year ended December 31, 2011. The amounts for the year ended December 31, 2010 include the Company's wholly owned subsidiaries, Costar, LQ, and Sielox. As of December 31, 2010, the Company sold substantially all of its assets in its wholly-owned subsidiary, Sielox. All material intercompany transactions have been eliminated in consolidation.

These consolidated financial statements were approved by management and available for issuance on April 20, 2012. Subsequent events have been evaluated through this date.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents

The Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. As of December 31, 2011 and 2010, the Company had no such cash equivalents.

Accounts Receivable and Allowance for Doubtful Accounts

The Company complies with the accounting and reporting requirements of GAAP that lend to or finance the activities of others. Accounts receivable are recorded at net realizable values. The Company maintains an allowance for estimated losses resulting from the failure of customers to make required payments and for anticipated returns. The allowance is based on specific facts and circumstances surrounding individual customers as well as historical experience. Provisions for losses on receivables and returns are charged to income to maintain the allowance at a level considered adequate to cover losses and future returns. Receivables are charged off against the reserve when they are deemed uncollectible and returns are charged off against the reserve when the actual returns are incurred.

2. Summary of significant accounting policies (continued)

Inventories

Inventories are recorded on the first in first out basis and are stated at the lower of average cost or market. A provision is made to reduce excess or obsolete inventories to their net realizable value. As of December 31, 2011 and 2010, the Company had $6,859 and $4,694 in finished goods, respectively.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is computed using the straight-line method over estimated useful lives of 3-5 years as follows.

Computer hardware and software	3 years
Furniture and fixtures	5 years
Leasehold improvements	Shorter of lease term or asset useful life

Intangible Assets

In accordance with GAAP, intangible assets with indefinite lives are not amortized, but instead tested for impairment. Intangible assets are reviewed for impairment at least annually or whenever events or changes in business combinations indicate the carrying value of the assets may not be recoverable. Impairment losses are recognized if the fair value of the intangible is less than its carrying value.

Intangible assets with finite lives are amortized over their estimated useful lives. These intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable. A loss is recognized in the consolidated statements of operations if it is determined that an impairment exists based on expected future undiscounted cash flows. The amount of the impairment is the excess of the carrying amount of the impaired asset over its fair value.

Long-Lived Assets

In accordance with GAAP, we review property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable. A loss is recognized on the consolidated statements of operations if it is determined that an impairment exists based on expected future undiscounted cash flows. The amount of the impairment is the excess of the carrying amount of the impaired asset over its fair value.

Comprehensive Income (loss)

Comprehensive income (loss) consists of net income (loss) and other comprehensive income (loss), which includes foreign currency translation adjustments. In accordance with GAAP, the Company establishes standards for disclosure and financial statement presentation for reporting total comprehensive income (loss) and its individual components. Comprehensive income (loss), as defined, includes all changes in equity during a period from non-owner resources.

(AMOUNTS SHOWN IN THOUSANDS)

2. Summary of significant accounting policies (continued)

Revenue Recognition

The Company ships and invoices its sales in accordance with signed purchase orders. The Company only recognizes revenue when it is realized and earned. The Company considers its revenue to have been earned when goods are shipped in accordance with signed purchase orders. Any software imbedded in the products sold is considered incidental to the product being sold.

Research and Development

Expenditures for research, development and engineering of software and hardware products, that are included in selling, general and administrative expenses in the consolidated statements of operations, are expensed as incurred.

Stock-Based Compensation

The Company complies with the accounting and reporting requirements of the Accounting for Stock-Based Compensation guidelines which require companies to record compensation expense for share-based awards issued to employees in exchange for services provided. The amount of the compensation expense is based on the estimated fair value of the awards on their grant dates and is generally recognized over the applicable vesting period.

The fair value of stock options is determined using an option-pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option, the volatility of the underlying stock, expected dividends, and the risk free interest rate over the expected life of the option.

During the year ended December 31, 2011 the Company recognized $34 in stock based compensation expense in its consolidated financial statements relating to the issuance of 100 stock options and 462 stock-grants. The Company did not record stock based compensation expense during the year ended December 31, 2010 relating to the issuance of 555 stock options, due to the amount being immaterial to the consolidated financial statements taken as a whole. The fair value of the 2011 and 2010 stock options were estimated on the date of grant using the Black-Sholes valuation model based on the following assumptions:

	Year Ended December 31,	
	2011	**2010**
Expected dividend yield	0.00%	0.00%
Expected stock price volatility	14.48%	14.48%
Risk-free interest rate	2.00%	2.00%
Expected life in years	10 years	10 years
Weighted-average fair value of options granted	$.02	$.01

Income Taxes

The Company complies with GAAP which requires an asset and liability approach to financial reporting for income taxes. Deferred income tax assets and liabilities are computed for differences between the consolidated financial statement and tax bases of assets and liabilities that will result in future taxable or deductible amounts, based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred income tax assets to the amount expected to be realized.

2. Summary of significant accounting policies (continued)

The determination of the Company's provision for income taxes requires significant judgment, the use of estimates, and the interpretation and application of complex tax laws. Significant judgment is required in assessing the timing and amounts of deductible and taxable items and the probability of sustaining uncertain tax positions. The benefits of uncertain tax positions are recorded in the Company's consolidated financial statements only after determining a more-likely-than-not probability that the uncertain tax positions will withstand challenge, if any, from tax authorities. When facts and circumstances change, the Company reassesses these probabilities and records any changes in the consolidated financial statements as appropriate. Accrued interest and penalties related to income tax matters are classified as a component of income tax expense.

In accordance with GAAP, the Company is required to determine whether a tax position is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The Company files an income tax return in the U.S. federal jurisdiction, and may file income tax returns in various U.S. states and foreign jurisdictions. The tax benefit recognized is measured as the largest amount of benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. De-recognition of a tax benefit previously recognized results in the Company recording a tax liability that reduces increases the accumulated deficit. Generally, the Company is no longer subject to income tax examination by major taxing authorities for the years before 2007.

Reclassifications

Certain prior year amounts have been reclassified in order to conform to the current year presentation.

3. Company Liquidity

The Company has historically incurred losses and negative cash flows from operations. For the year ended December 31, 2011, the Company earned net income of $162 versus a net loss of $(358) for the year ended December 31, 2010. The Company had net cash outflows from operations of $(1,627) and $(601) for the years ended December 31, 2011 and 2010, respectively. However, The Company has taken measures to reduce expenses, beginning in the second half of 2009 and again in 2010. In addition, the Company sold certain underperforming assets and related liabilities of its wholly owned subsidiary, Sielox, LLC, for $2,525 in cash and a $500 promissory note in December 2010. Furthermore, effective September 23, 2011, Costar entered into a Loan and Security Agreement with Briar Capital L.P. ("Briar"). The Loan and Security Agreement allows for up to $3,500 in revolving lines of credit with a three year maturity. As a result, the Company's Management believes that the Company has the financial wherewithal to meet its ongoing liquidity needs.

4. Deregistration of the Company's stock

On March 30, 2010, the Company filed Form 15 with the United States Securities and Exchange Commission (the "SEC") to terminate the registration of its common stock under Section 12(g) of the Exchange Act, as amended. As a result, the Company has ceased to file current and periodic reports with the SEC. The Company is eligible to deregister its common stock because it has fewer than 300 stockholders of record.

The decision to deregister was made by the Company's Board of Directors on the recommendation of a Special Committee of independent directors that thoroughly examined the issue. The decision to deregister is consistent with other cost-cutting measures that the Company has taken in order to more effectively align the Company's operating cost structure with changing market conditions. Deregistration will also significantly minimize the

4. Deregistration of the Company's stock (continued)

administrative burden associated with being a SEC reporting company, permitting the Company's management team to better focus its attention and resources on existing plans to increase revenue including, among other things, the continued development of the Company's customer base and product lines.

The Board of Directors and management believe that deregistering under the Securities Exchange Act ("SEA") will not have a material negative impact on the Company's current relationships with employees, customers or suppliers, or its existing financing arrangements.

As of the date of the filing of the Form 15, the Company's obligation to file reports under the SEA, including forms 10-K, 10-Q and 8-K, was immediately suspended. Other filing requirements terminated upon the effectiveness of the deregistration under Section 12(g) of the SEA, which occurred 90 days after the filing of the Form 15.

The Company will continue to hold an annual stockholders' meeting and will make quarterly and annual financial information available to stockholders by press release and through its website.

The Company's shares are no longer quoted on the OTCBB. Instead, the share are quoted on the OTC Markets Group, LLC, an electronic network through which participating broker-dealers can make markets, and enter orders to buy and sell shares of companies.

5. Discontinued operations

As required under GAAP, the Company has classified the results of operations of Sielox within income from discontinued operations. The assets and liabilities of this entity have been classified to current and non-current assets and current and long term liabilities of discontinued operations on the consolidated balance sheets.

During December 2010, the Company entered into an agreement to sell certain of the assets and liabilities of its wholly owned subsidiary, Sielox, LLC. Sielox, LLC develops, designs and distributes a range of access control systems and products. The Company sold net assets of $2,431, including accounts receivable of $1,414 and inventory of $595 among others. These assets were sold for $2,525 in cash and a $500 promissory note. The net gain on the sale was $492, which includes approximately $100 in legal costs associated with the sale.

One of the agreed conditions of the sale was that Costar would continue to sell its range of security solution products through the Sielox, LLC network of approved business partners. The terms and conditions that govern the sale of Costar products are stated in the Master Distribution Agreement (the "Agreement") entered into between Costar and HGW Acquisition Company ("HGW"). The term of the Agreement commences on January 1, 2011, and ends on December 31, 2013. During the term of the Agreement, HGW has agreed to purchase Costar products in the minimum amount of $5,000. Actual purchases will be measured against a schedule of semi-annual purchase commitments (the "Purchase Commitment"). In furtherance of the Purchase Commitment, HGW delivered to Costar a secured promissory note with an original principal balance in the amount of $500 and bearing interest on the unpaid balance at a rate equal to 7% per annum. The promissory note is secured by a first priority security interest in HGW's accounts receivable. In the event that HGW fails to purchase Costar products in an amount equal to the Purchase Commitment as of the end of an applicable semi-annual period, HGW will have a period of 30 days to remedy the purchase default. That remedy will be in the form of a payment to Costar, of an amount equal to 25% of the shortfall, plus interest.

(AMOUNTS SHOWN IN THOUSANDS)

5. Discontinued operations (continued)

The results of discontinued operations included in the consolidated statements of operations and consolidated balance sheets are as follows:

	Year Ended December 31, 2011	Year Ended December 31, 2010
Net revenues	$ -	$ 6,963
Cost of revenues	-	4,480
Gross Profit	-	2,483
Selling, general & administrative expenses	1	2,350
Operating income (loss)	(1)	133
Other income (expenses)		
Gain on sale of assets, net of costs $100	-	492
Interest expense	-	(175)
Net income (loss)	$ (1)	$ 450

	December 31, 2011	December 31, 2010
Cash	$ -	$ 10
Accrued expenses	-	(75)
Net assets and liabilities	$ -	$ (65)

The assets and liabilities only include those assets and liabilities that were included in the asset based sale of Sielox, LLC.

6. Business combination

On October 20, 2011, Costar acquired substantially all of the assets of Industrial Vision Source (“IVS”), a division of Mace Security Products, Inc. for $517. Additionally, the “IVS Asset Purchase Agreement” calls for an additional earn-out payment of $100 if IVS reaches certain ninety day revenue targets. Pursuant to the IVS Asset Purchase Agreement, the minimum ninety day revenue target was achieved as of January 2012, and the $100 owed has been recorded in the accompanying consolidated balance sheet as of December 31, 2011.

(AMOUNTS SHOWN IN THOUSANDS)

6. Business combination (continued)

The acquisition of these properties meets the definition of a business combination under GAAP. The following table presents a summary of the fair value of assets acquired and liabilities assumed during the year ended December 31, 2011:

Assets acquired:		
Inventory	$	336
Accounts receivable		73
Trade name		125
Customer relations		125
Covenant not to compete		50
Total assets acquired		709
Liability assumed:		
Accounts payable		92
Total assets acquired and liabilities assumed, net	$	617

7. Property and equipment

Property and equipment from continuing operations are as follows:

	December 31,			
	2011		2010	
Office furniture and equipment	$	389	$	315
Demonstration and technical equipment		41		41
		430		356
Less accumulated depreciation		(302)		(308)
Total property and equipment, net	$	128	$	48

8. Intangible assets

In accordance with GAAP, intangible assets with indefinite lives are not amortized, but instead tested for impairment. Intangible assets are reviewed for impairment at least annually or whenever events or changes in business combinations indicate the carrying value of the assets may not be recoverable. Impairment losses are recognized if the fair value of the intangible is less than its carrying value.

Intangible assets that are subject to amortization are reviewed for potential impairment whenever events or circumstances indicate that carrying amounts may not be recoverable. Assets not subject to amortization are tested for impairment at least annually.

(AMOUNTS SHOWN IN THOUSANDS)

8. Intangible assets (continued)

The following is a summary of amortized and unamortized intangible assets from continuing operations at December 31, 2011 and December 31, 2010.

	December 31, 2011	
	Gross Amount	Accumulated Amortization
Amortized intangible assets		
Customer relations - Southern Imaging	$ 1,598	$ 1,465
Distribution agreement - Southern Imaging	1,468	404
Customer relations – IVS	125	3
Covenant not to compete – IVS	50	3
Total amortized intangible assets	3,241	1,875
Unamortized intangible assets		
Trade name - Costar	800	-
Trade name - IVS	125	-
Total unamortized intangible assets	925	-
Total intangible assets	$ 4,166	$ 1,875

	December 31, 2010	
	Gross Amount	Accumulated Amortization
Amortized intangible assets		
Customer relations - Southern Imaging	$ 1,598	$ 1,198
Distribution agreement - Southern Imaging	1,468	331
Total amortized intangible assets	3,066	1,529
Unamortized intangible assets		
Trade name - Costar	800	-
Total intangible assets	$ 3,866	$ 1,529

The weighted average amortization period for the Company's intangible assets is 12 years. The estimated useful lives for customer relationships, distribution agreements and covenant not to compete are 6, 20 and 3 years, respectively.

(AMOUNTS SHOWN IN THOUSANDS)

8. Intangible assets (continued)

Amortization expense for the years ended December 31, 2011 and 2010 was $346 and $340, respectively. Future amortization expense, as of December 31, 2011, is as follows:

Year Ending December 31,		
2012	$	244
2013		111
2014		108
2015		94
2016		94
Thereafter		715
Total future amortization expense	$	1,366

9. Lines of credit

Effective as of August 21, 2009, Costar entered into the "Costar Loan Agreement" with Compass Bank ("Compass"). The Costar Loan Agreement provided Costar with up to $4,000 in revolving lines of credit. The obligations under the Costar Loan Agreement are evidenced by a Master Revolving Promissory Note made by Costar in favor of Compass. The obligations under the Costar Loan Agreement are secured by a lien on substantially all accounts receivable, inventory, equipment, general intangibles, including intellectual property, chattel paper, instruments and documents of Costar, as set forth in the Costar Loan Agreement. The Company is a guarantor of Costar's obligations under the Costar Loan Agreement pursuant to the unlimited guaranty made by the Company in favor of Compass. Borrowings under the Costar Loan Agreement accrued interest at a rate equal to the greater of (i) 5% per annum and (ii) the 30-day LIBOR plus 3% per annum.

The Costar Loan Agreement contains customary representations and warranties, events of default and covenants, including, among other things, covenants that restrict the ability of Costar to incur certain additional indebtedness or to issue equity interests. The Costar Loan Agreement also contains financial covenants restricting Costar's Debt Service Coverage Ratio, Total Debt to Tangible Net Worth Ratio, and Quick Ratio (as each of such terms is defined in the Costar Loan Agreement), as well as limiting capital expenditures of Costar and requiring Costar and the Company to maintain a specific Tangible Net Worth. As of December 31, 2011 and 2010, approximately $- and $626, respectively, was owed to Compass.

In addition, effective as of June 1, 2010, and again on November 21, 2010, Compass amended and restated the Costar Loan Agreement dated as of August 21, 2009. The restated agreement provides Costar with up to $2,500 in revolving lines of credit due on January 21, 2011. Borrowings under the restated agreement accrued interest at a rate equal to the greater of 7% per annum or the 30-day LIBOR plus 4% per annum.

Effective January 21, 2011, Compass amended and restated the Costar Loan Agreement dated as of August 21, 2009. The restated agreement provides Costar with up to $1,500 in revolving lines of credit due on April 21, 2011.

(AMOUNTS SHOWN IN THOUSANDS)

9. Lines of credit (continued)

On March 31, 2011, the Company was in default of one of the covenants with Compass, and requested a waiver from the bank. Effective April 21, 2011, June 21, 2011, and August 5, 2011, Compass amended and restated the Costar Loan Agreement dated as of August 21, 2009. The restated agreement provides Costar with up to $1,500 in revolving lines of credit due on September 20, 2011. The Company did not renew their Revolving Credit and Costar Loan Agreement with Compass.

Effective as of September 23, 2011, Costar entered into a Loan and Security Agreement with Briar. The Loan and Security Agreement allows for up to $3,500 in revolving lines of credit, with a three year maturity. The obligations under the Costar Loan and Security Agreement with Briar are secured by a lien on substantially all accounts receivable, inventory, equipment, general intangibles, including intellectual property, chattel paper, instruments and documents of Costar, as set forth in the Loan and Security Agreement with Briar. The Company is a guarantor of Costar's obligations under the Costar Loan and Security Agreement with Briar pursuant to the guaranty made by the Company in favor of Briar. Borrowings under the Loan and Security Agreement accrue interest at a rate equal to the 30-day LIBOR rate plus 8.25% per annum.

The Costar Loan and Security Agreement with Briar contains customary representations and warranties, events of default and covenants, including, among other things, covenants that restrict the ability of Costar to incur certain additional indebtedness or to issue equity interests. The Costar Loan and Security Agreement with Briar also contain financial covenants restricting capital expenditures of Costar and requiring Costar and the Company to maintain a specific Tangible Net Worth. As of December 31, 2011 and December 31, 2010, approximately $2,974 and $-, respectively, was owed to Briar.

10. Deferred income taxes

Deferred tax assets are determined based on the difference between financial statement and tax bases using enacted tax rates in effect for the year in which the differences are expected to reverse. The components of the deferred taxes are as follows:

	December 31,	
	2011	2010
Net operating loss carryforward	$ 51,562	$ 51,618
Valuation allowance	(51,562)	(51,618)
Total net deferred tax asset	$ -	$ -

In connection with ownership changes, it was determined that certain of the Company's net operating loss carry forwards ("NOL") have been limited. As of December 31, 2011, the Company has approximately $151,600 of NOLs that can be utilized in future years. These NOLs, if not used, will expire between 2019 and 2030.

A valuation allowance has been established for the full amount of the tax asset since it is more likely than not that the deferred tax asset will not be realized.

(AMOUNTS SHOWN IN THOUSANDS)

11. Stockholders' equity (shown in whole amounts)

At December 31, 2011 and December 31, 2010, the authorized capital stock of the Company consisted of (i) 90,000,000 shares of voting common stock with a par value of $0.001 per share and (ii) 10,000,000 shares of preferred stock with a par value of $0.001 per share. As of December 31, 2011 and 2010, there was no preferred stock issued and outstanding. The Company's Board has the authority to determine the voting powers, designations, preferences, privileges and restrictions of the preferred shares.

12. Stock option plan (shown in whole amounts)

The Company's 2000 Stock Option and Incentive Plan (the "2000 Incentive Plan") provides for awards in the form of incentive stock options, non-qualified stock options, restricted stock awards and other forms of awards to officers, directors, employees and consultants of the Company. At December 31, 2011 there were 3,081,696 share options issued under this plan. At December 31, 2011, there were 3,426,702 shares available for issuance under the 2000 Incentive Plan.

The Board of Directors of the Company determines the term of each option, the option price, the number of shares for which each option is granted and the times at which each option vests. For holders of 10% or more of the Company's outstanding common stock, incentive stock options may not be granted at less than 110% of the fair market value of the common stock at the date of grant.

The following table summarizes information about stock options outstanding at December 31, 2011:

Options Outstanding				Options Fully Vested and Exercisable	
Range of Exercise Price Per Share	Number Outstanding	Remaining Contractual Life (In Years)	Weighted Average Exercise Price Per Share	Number Exercisable	Weighted Average Exercise Price Per Share
$0.029-$0.56	3,081,696	5.05	$0.27	2,850,846	$0.28

(AMOUNTS SHOWN IN THOUSANDS)

12. Stock option plan (shown in whole amounts) (continued)

Stock option activity for the years ended December 31, 2011 and 2010 is as follows:

	2011		2010	
	Number of Shares	Weighted Average Exercise Price Per Share	Number of Shares	Weighted Average Exercise Price Per Share
Outstanding at beginning of year	2,981,696	$0.27	2,501,696	$0.33
Granted	100,000	$0.06	555,000	$0.04
Exercised				
Canceled			(75,000)	
Outstanding at end of year	3,081,696	$0.27	2,981,696	$0.27
Options exercisable at end of year	2,850,846	$0.28	2,572,934	$0.31
Weighted average fair value of options granted during the year at fair value		$0.02		$0.01

During the year ended December 31, 2011 the Company recognized approximately $34,000 in stock based compensation expense in its consolidated financial statements relating to the issuance of 100,000 stock options and 462,000 stock-grants. The Company did not record stock based compensation expense during the year ended December 31, 2010, relating to the issuance of 555,000 stock options, due to the amount being immaterial to the consolidated financial statements taken as a whole.

13. Earn-out and contingent purchase price

On June 20, 2006, the Company entered into an Asset Purchase Agreement with Southern Imaging, Inc., Video Solutions Technology Center, Inc., and certain shareholders of Southern Imaging, Costar and Video Solutions Technology Center, LLC, whereby the Company acquired substantially all of the assets of Southern Imaging and Video Solutions (the “Southern Imaging Agreement,” included as Exhibit 2.1 to the Company’s 8-K filed on June 26, 2006), the Company was obligated to make an earn-out payment of $773 on April 1, 2009 (the “2008 earn out payment”). The Company was unable to pay, in full, the 2008 earn-out payment. Since that date, several payments were made that included principal and interest at 9% per annum.

On January 15, 2010, the Company and the previous owners of Southern Imaging agreed on a payment schedule whereby the Company would make a payment, on or about the 15th of each month, of $25, including principal and interest at 9% per annum.

Effective September 20, 2011, the Company entered into a payoff agreement with Thompson, Pritchett & Switzer, L.P., requiring approximately $84 to be paid as the final earn-out payment. In addition, effective September 23, 2011, the earn-out payment was paid in full, per the payoff agreement.

(AMOUNTS SHOWN IN THOUSANDS)

14. Lease agreements

On January 31, 2011 the Company entered into a new lease agreement for certain of its facilities that will expire in 2018. Future minimum annual rent payments are approximately as follows:

Year Ending December 31,		
2012	$	85
2013		99
2014		109
2015		117
2016		125
Thereafter		238
Total future minimum lease commitments	$	773

15. Legal proceedings

The Company, as well as the Company's subsidiary, LQ, were defendants in certain purported class action lawsuits filed by individual shareholders in the U.S. District Court for the Southern District of New York against certain of the Company's former officers and directors, and various of the underwriters in the Company's initial public offering and secondary offering. The lawsuits were filed by individual shareholders who purported to seek class action status on behalf of all other similarly situated persons who purchased our common stock between July 8, 1999 and December 6, 2000, and they were coordinated for pretrial purposes with similar lawsuits against more than 300 other companies as "In re Initial Public Offering Securities Litigation, 21 MC 92 (SAS)". On February 25, 2009, the parties to the coordinated litigation advised the District Court that they had reached an agreement-in-principle to settle the litigation in its entirety. A stipulation of settlement was filed with the District Court on April 2, 2009. On June 9, 2009, the District Court preliminarily approved the proposed global settlement. Notice was provided to the class, and a settlement fairness hearing, at which members of the class had an opportunity to object to the proposed settlement, was held on September 10, 2009. On October 6, 2009, the District Court issued an order granting final approval to the settlement. Ten appeals were filed objecting to the definition of the settlement class and fairness of the settlement. Five of those appeals were dismissed with prejudice on October 6, 2010. On May 17, 2011, the Court of Appeals dismissed four of the remaining appeals. On January 10, 2012, the last remaining appeal was dismissed with prejudice, as a result of which the settlement became final, by its terms, and all claims against the Company and its former officers and directors were dismissed with prejudice. The Company has no financial liability in connection with the settlement.

Thompson, Pritchett & Switzer, LP v. Sielox, Inc. Et al. C.A. No. 09-13228 (Tex. Dist. Dallas County)

A Complaint had been filed in the District Court of Dallas County, Texas, 162nd Judicial District (Cause No. 0913228), on behalf of Thompson, Pritchett & Switzer, L.P., as Plaintiff, against the Company, its predecessor company and Costar, as Defendants, alleging that the Defendants owe the Plaintiff approximately $705 plus 9% interest and attorneys fees in connection with certain "earn-out" payments alleged to be due and owing to the Plaintiff by the Defendants in connection with that certain Asset Purchase Agreement pursuant to which the predecessor of the Company acquired certain companies known as Southern Imaging Inc. and Video Solutions Technologies Center Inc. On October 13, 2009, the parties agreed that the Plaintiff would not serve the Defendants with the Complaint until after January 15, 2010 unless the Defendants default on any of the following agreed upon payments: $125 on October 14, 2009 (payment has been made), $25 on November 2, 2009 (payment has been made) and an additional $25 on December 15, 2009 (payment has been made). On January

15. Legal proceedings (continued)

15, 2010, the Company and the previous owners of Southern Imaging agreed on a payment schedule where by the Company will make a payment on or about the 15th of each month, of $25, including principal and interest at 9% per annum. Effective September 20, 2011, the Company entered into a payoff agreement with Thompson, Pritchett & Switzer, L.P., requiring approximately $84 to be paid as the final earn-out payment. In addition, effective September 23, 2011, the earn-out payment was paid in full, per the payoff agreement.

16. Risk concentrations

Concentration of Cash

The Company maintains its cash balances in financial institutions. These balances are insured by the Federal Deposit Insurance Corporation up to $250 per institution. The Company is subject to credit risk to the extent any financial institution with which it conducts business is unable to fulfill contractual obligations on its behalf. Management monitors the financial condition of such financial institutions and does not anticipate any losses from these financial institutions.

Concentration of Customers

The Company’s security surveillance product line customers include traditional “large box” national retailers and distributors. The Company’s industrial vision product line customers include manufacturers that assemble products using automated production lines; these customers use the Company’s video systems to monitor activity on the production line. For the years ended December 31, 2011 and 2010, the Company’s two largest customers accounted for approximately $7,600 and $4,200, or 43.7% and 33.2% of the Company’s total revenue, respectively. The same customers owed $1,500 and $602, or 53.2% and 29.8% of the outstanding receivable balance, as of December 31, 2011 and 2010, respectively.

Concentration of Suppliers

For the years ended December 31, 2011 and 2010, the Company made purchases from one main supplier of approximately 24.3% and 25.4% of total purchases, respectively. Amounts owed to this supplier were approximately 48.7% and 59.3% of the total accounts payable balance, as of December 31, 2011 and 2010, respectively.

17. Subsequent events

Effective March 2, 2012, the Company’s shares started trading on the OTC Markets Group under the ticker symbol “CSTI” to reflect the Company’s new name, Costar Technologies, Inc. The shares formerly traded on the OTC Markets Group under the stock ticker symbol “SLXN”. The Company has also changed the address of its website from www.sieloxinc.com to www.costartechnologies.com.