

HS3 TECHNOLOGIES INC.  
Form 10QSB  
February 13, 2007  
UNITED STATES

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Form 10-QSB**

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **December 31, 2006**

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number **001-32289**

**HS3 TECHNOLOGIES, INC.**

(Exact name of small business issuer as specified in its charter)

**Nevada**

(State or other jurisdiction of incorporation or organization)

**20-3598613**

(IRS Employer Identification No.)

**1800 Boulder Street, Suite 600, Denver, CO 80211-6400**

(Address of principal executive offices)

**303.455.2550**

(Issuer's telephone number)

**N/A**

(Former name, former address and former fiscal year, if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:

24,501,500 **common shares** as of February 5, 2007 transitional Small Business Disclosure Format (Check one): Yes  No

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



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**PART I FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**

**HS3 Technologies, Inc.**

**CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**As of December 31, 2006**

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**HS3 Technologies, Inc.**  
(a development stage company)

Condensed Consolidated Balance Sheets

December 31, 2006

June 30, 2006

**ASSETS**

**Current Assets**

Cash and cash equivalents	\$ 111,666	\$ 13,616
Accounts receivable	4,797	9,946
Inventory	128,845	112,993
Prepaid inventory	-	8,350
Total current assets	245,308	144,905

Furniture, fixtures and equipment, net of accumulated depreciation of \$16,188 and \$7,688, respectively

	73,120	80,329
<b>Total assets</b>	<b>\$ 318,428</b>	<b>\$ 225,234</b>

**LIABILITIES**

**Current Liabilities**

Accounts payable and accrued liabilities	\$ 50,658	\$ 75,845
Convertible debenture	-	500,000
Value of warrant liability	2,176,859	-
Notes payable	115,000	100,000
<b>Total current liabilities</b>	<b>2,342,517</b>	<b>675,845</b>

**STOCKHOLDERS' EQUITY(DEFICIT)**

Preferred stock, \$0.001 par value, 2,500,000 shares authorized, none issued or outstanding

Common stock, \$0.001 par value, 50,000,000 authorized, 24,411,500 and 17,491,500 shares issued and outstanding, respectively	-	-
Additional paid- in capital	24,412	17,492
(Deficit) accumulated during development stage	1,609,347	(17,492)
<b>Total stockholders' equity (deficit)</b>	<b>(3,657,848)</b>	<b>(450,611)</b>
	<b>(2,024,089)</b>	<b>(450,611)</b>

<b>Total liabilities and stockholders' equity (deficit)</b>	<b>\$ 318,428</b>	<b>\$ 225,234</b>
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The accompanying notes are an integral part of these condensed consolidated financial statements

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**HS3 Technologies, Inc.**  
(a development stage company)

					For the Cumulative Period from
	Three Months ended	Three Months ended	Six Months ended	Six Months ended	December 24, 2004 (inception) to
<b>Condensed Consolidated Statements of Operations</b>	December 31, 2006	December 31, 2005	December 31, 2006	December 31, 2005	December 31, 2006
Net revenues	\$5,686	\$ 2,323	\$ 19,456	\$ 5,827	\$ 66,588
Cost of goods sold	10,879	-	17,694	-	41,497
Gross profit (loss)	(5,193)	2,323	1,762	5,827	25,091
Operating expenses:					
Sales and marketing	671,461	-	705,513	-	758,928
General and administrative	196,847	75,670	324,095	79,204	743,366
Total operating expenses	868,308	75,670	1,029,608	79,204	1,502,294
Income (loss) from operations	(873,501)	(73,347)	(1,027,846)	(73,377)	(1,477,203)
Other income (expense)					
Interest income	2,016	-	2,074	-	3,277
Interest (expense)	(2,246)	-	(4,606)	-	(7,063)
Warrant valuation income (loss)	(1,506,170)	-	(2,176,859)	-	(2,176,859)
Total other income (expense)	(1,506,400)	-	(2,179,391)	-	(2,180,645)
Net (loss)	\$(2,379,901)	\$(73,347)	\$(3,207,257)	\$(73,377)	\$(3,657,848)
Net (loss) per share-basic and diluted	\$(0.12)	\$(0.00)	\$(0.17)	\$(0.00)	\$(0.34)
Weighted average number of common shares outstanding basic and diluted	19,798,167	17,491,500	18,644,833	17,491,500	10,621,917

**The accompanying notes are an integral part of these condensed consolidated financial statements**

**HS3 Technologies, Inc.**  
(a development stage company)

**Condensed Consolidated Statement of Stockholders' Equity (Deficit)**  
**Period from December 24, 2004 (inception) to December 31, 2006**

	Common Stock Shares	Amount	Additional Paid-in Capital	(Deficit) accumulated during development stage	Total Stockholders' Equity (deficit)
Inception, December 24, 2004	-	\$ -	\$ -	\$ -	\$ -
Shares issued	625,000	625	375	-	1,000
Contributed services	-	-	1,000	-	1,000
Net (loss) for the period ended June 30, 2005	-	-	-	(5,841)	(5,841)
Balances as of June 30, 2005	625,000	625	1,375	(5,841)	(3,841)
Effect of recapitalization on November 9, 2005	16,866,500	16,867	(18,867)	-	(2,000)
Net (loss)	-	-	-	(444,770)	(444,770)
Balances as of June 30, 2006	17,491,500	17,492	(17,492)	(450,611)	(450,611)
Issuance of shares in conversion of debenture	125,000	125	499,875	-	500,000
Shares issued for cash	5,925,000	5,925	468,075	-	474,000
Shares Issued for services	870,000	870	347,130	-	348,000
Value of warrants issued for services	-	-	311,759	-	311,759
Net (loss) for the period ended December 31, 2006	-	-	-	(3,207,237)	(3,207,237)
Balances as of December 31, 2006	24,411,500	\$ 24,412	\$ 1,609,347	\$ (3,657,848)	\$ (2,024,089)

**The accompanying notes are an integral part of these condensed consolidated financial statements**

<b>HS3 Technologies, Inc.</b> (a development stage company)	Six Months ended December 31, 2006	Six Months ended December 31, 2005	For the Cumulative Period from December 24, 2004 (inception) to December 31, 2006
<b>Condensed Consolidated Statements of Cash Flows</b>			
<b>Cash flows from operating activities:</b>			
Net (loss)	\$ (3,207,237)	\$ (73,377)	\$ (3,657,848)
Adjustments to reconcile net (loss) to net cash provided by (used in) operations:			
Depreciation	8,500	175	16,188
Effect of recapitalization	-	(2,000)	(2,000)
Contributed services	-	-	1,000
Warrant valuation loss (income)	2,176,859	-	2,176,859
Fair value of common stock and warrants issued for services	659,759	-	659,759
Write off of deposit on inventory	8,350	-	-
Changes in other assets and liabilities:			
Accounts receivable	5,149	(1,311)	(4,797)
Inventory	(15,852)	(27,840)	(128,845)
Accounts payable and accrued liabilities	(25,187)	7,613	50,658
Net cash (used in) operating activities	(389,659)	(96,740)	(889,026)
<b>Cash flow from investing activities</b>			
Purchase of fixed assets	(1,291)	(30,500)	(89,308)
Net cash from (used in) investing activities	(1,291)	(30,500)	(89,308)
<b>Cash flow from financing activities</b>			
Proceeds from convertible debenture	-	500,000	500,000
Proceeds from issuance of common stock	474,000	-	475,000
Payment on advance from stockholder	-	(7,310)	-
Proceeds from notes payable	15,000	-	115,000
Net cash flow provided by financing activities	489,000	492,690	1,090,000
<b>Increase in cash and cash equivalents</b>	<b>98,050</b>	<b>365,450</b>	<b>111,666</b>
Cash and cash equivalents, beginning of period	13,616	3,041	-
Cash and cash equivalents, end of period	\$ 111,666	\$ 368,491	\$ 111,666
<b>Supplemental cash flow information:</b>			
Interest paid	\$ -	\$ -	\$ -
Income taxes paid	\$ -	\$ -	\$ -
<b>Non-cash investing and financing activities:</b>			
Conversion of debenture to common stock	\$ 500,000	\$ -	\$ 500,000
<b>The accompanying notes are an integral part of these condensed consolidated financial statements</b>			



**HS3 Technologies, Inc.**

(A Development Stage Company)

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2006**

**1. Organization and Business**

HS3 Technologies, Inc. (a development stage company) was incorporated in Nevada on January 28, 2003, and herein is referred to as the Company. Prior to a name change in October 2005, the Company was known as Zeno, Inc. The Company also changed its fiscal year end from March 31 to June 30.

On November 9, 2005, the Company acquired ip-Colo, Inc., in a reorganization, a development stage corporation organized in Colorado on December 24, 2004 (herein referred to as ip-Colo). On the date of the reorganization, the Company was a non-operating entity without any assets or liabilities.

Immediately prior to the reorganization, the Company had a total of 77,623,000 shares of issued and outstanding common stock. The reorganization was entered into pursuant to an Asset Purchase Agreement whereby the Company issued 1,612,520 shares of common stock to the shareholders of ip-Colo for all of the previously issued and outstanding common stock of ip-Colo. Concurrently, the Company cancelled 9,269,520 shares of common stock outstanding upon agreement with shareholders.

As a consequence of the reorganization, the former ip-Colo shareholders owned approximately 57.6% of the resultant 69,966,000 outstanding shares of the Company common stock. The reorganization was recorded as a recapitalization effected by a reverse acquisition wherein the Company is treated as the acquiree for accounting purposes, even though it was the legal acquirer. Accordingly, the results of operations included in the financial statements consist solely of the accounting acquirer, ip-Colo since its December 24, 2004 inception and the Company from the date of reorganization. Since the accounting acquiree, the Company, was previously inoperative, goodwill was not recorded.

On September 6, 2006, the Company effected a one (1) new for four (4) old reverse stock split of its authorized, issued and outstanding stock. As a result, its authorized capital decreased to 50,000,000 shares of common stock with a par value of \$0.001 each and 2,500,000 preferred stock with a par value of \$0.001 each.

The Company is a development stage company with minimal revenues in the business of providing satellite-based internet connectivity and remote video monitoring for businesses and households.

**2. Basis of Presentation**

The unaudited interim financial statements of the Company included herein have been prepared in accordance with the instructions for Form 10-QSB under the Securities Exchange Act of 1934, as amended, and Item 310 of Regulation S-B under the Securities Act of 1933, as amended. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations relating to interim financial statements.

In the opinion of management, the accompanying unaudited interim condensed consolidated financial statements reflect all adjustments, including normal recurring accruals, necessary to present fairly the financial position of the Company at December 31, 2006, the results of operations for the three months and the six months ended December 31, 2006 and 2005, and the period from inception (December 24, 2004) to December 31, 2006, and the cash flows for the six months ended December 31, 2006 and 2005, and the period from inception (December 24, 2004) to December 31, 2006. The results of operations for the three months ended December 31, 2006 are not necessarily indicative of the expected results of operations for the full year or any future period. The balance sheet as of June 30, 2006 is derived from the Company's audited financial statements. These financial statements should be read in conjunction with the consolidated financial statements and footnotes included in the Company's Annual Report on Form 10-KSB for the period ended June 30, 2006 as filed with the Securities and Exchange Commission.



The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. At present, the Company is in the development stage, is wholly reliant on its ability to raise additional capital for future financing needs and has had minimal revenues, saleable product, service or other business operations through December 31, 2006. These factors raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Management plans to address this uncertainty include completion of product acquisition, development of a sales force and initiating revenue producing activities. In the first quarter of 2007, management continues to aggressively pursue alternative financing arrangements to assist in meeting these goals.

### 3. Notes Payable

On May 9, 2006, the Company entered into an unsecured short-term promissory note for \$100,000. The note bears interest at 8% annually and is due in full on May 9, 2007.

On August 8, 2006, the Company entered into an unsecured short-term promissory note for \$15,000. The note bears interest at 8% annually and is due in full on August 8, 2007.

### 4. Stockholders' Equity (Deficit)

The Company computes net earnings (loss) per share in accordance with SFAS No. 128, Earnings per Share, which establishes standards for computing and presenting net earnings (loss) per share. Basic earnings (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding and the number of dilutive potential common share equivalents during the period. No common share equivalents are outstanding for the periods presented.

On October 10, 2005, the Company received total gross proceeds of \$500,000 and issued a convertible debenture, convertible into 125,000 shares of common stock at the option of the Company once the fair market value of the Company's common stock exceeds \$4.00 per share. Interest was to accrue and be paid in full at 5% per annum if the acquisition of ip-Colo, Inc. did not occur within 120 days of the closing of the debenture. As described in Note 1 in the accompanying footnotes, the acquisition of ip-Colo, Inc. did occur on November 9, 2005 or within 29 days of the closing of the debenture. Thus, no interest is due or payable. Further, the fair value of the Company's stock did exceed \$4.00 per share as quoted on the Over-the-Counter Bulletin Board in November 2005. On October 13, 2006, the Company converted the outstanding debenture using a conversion price of \$4.00 per share into 125,000 shares of common stock.

On August 23, 2006 and September 19, 2006, the Company entered into two stock subscriptions aggregating \$50,000 and \$24,000, respectively. Under these subscriptions, on December 12, 2006, the Company issued 925,000 shares of common stock at a purchase price of \$0.08 per share. In addition, between September 24, 2006 and November 1, 2006, the Company completed a series of equity stock subscription placements aggregating \$400,000. Under the subscriptions, on December 12, 2006, the Company issued 5,000,000 shares of common stock at a purchase price of \$0.08 per share.

On September 8, 2006 the Company entered into a warrant purchase agreement with a private consultant for certain financial advisory services provided to the Company by the Consultant, the Company agreed to issue to the Consultant share purchase warrants in the capital of the Company. The Company granted to the Consultant 6,250,000 common share purchase warrants (each a Warrant) exercisable at \$0.12 per share for a period of two years from date of issuance. The value of the 6,250,000 warrants issued, \$670,689, was recorded as a warrant liability and charged to warrant valuation income (loss). The warrants were valued using the Black-Scholes option pricing method with a common stock price of \$0.16 based on the quoted trade price, two-year expected term, zero expected dividends, volatility of 120.13% and a discount rate of 3%. In accordance with EITF 00-19, the Company re-valued the 6,250,000 warrants issued at \$2,176,859, resulting in additional \$1,506,170 recorded as a warrant liability and charged to warrant valuation income (loss) for the period ending December 31, 2006. The warrants were valued at December 31, 2006 using the Black-Scholes option pricing method with a common stock price of \$0.39 based on the quoted trade price, two-year expected term, zero expected dividends, volatility of 188.39% and a discount rate of 3%.

On December 4, 2006 the Company entered into an agreement with a Business Communications Consulting firm for market communications, investor relations and strategic planning services. On December 13, 2006 the Company issued 870,000 shares of common stock to the consulting

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firm valued at \$348,000 and charged to sales and marketing expense in the accompanying statement of operations. The Company agreed to issue to the Firm share purchase warrants in the capital of the Company. The

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Company granted to the Firm 1,000,000 common share purchase warrants (each a Warrant) exercisable at \$0.50 per share for a period of two years from date of issuance. The value of the 1,000,000 warrants issued, \$311,759, was recorded as additional paid-in capital and charged to sales and marketing expense. The warrants were valued using the Black-Scholes option pricing method with a common stock price of \$0.39 based on the quoted trade price, two-year expected term, zero expected dividends, volatility of 188.39 and a discount rate of 3%

#### **5. Stock Option Plan**

The board of directors has approved a Stock Option Plan ( the Plan ) authorizing the issuance of a total of 10,000,000 shares pursuant to which directors, officers, employees of the Company are eligible to receive grants of options for the Company s common stock. Each stock option entities its holder to purchase one common share of the Company. The Plan is administrated by the board of directors but is subject to the approval of the Company s stockholders.

To date, no options have been granted under the Plan.

#### **6. Related Parties**

The Company leases office space from a company owned by a major stockholder. Rent expense under this lease was \$24,000, \$12,000 and \$63,500 for the six months ended December 31, 2006 and 2005, and from inception (December 24, 2004) to December 30, 2006, respectively.

In addition, included in accounts payable as of December 31, 2006 and June 30, 2006 is \$2,324 and \$20,868 respectively, resulting from activities of the Company associated with various entities controlled by a major stockholder of the Company.

#### **7. Subsequent Events**

On January 22, 2007 the Company issued 90,000 shares of common stock, valued at \$28,800, to Wall Street Resources, Inc. to provide written analytical coverage and consultation in matters concerning corporate finance and investor communications.

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## Item 2. Management's Discussion and Analysis or Plan of Operation

### FORWARD-LOOKING STATEMENTS

This quarterly report contains forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. These statements relate to future events or our future financial performance. In some cases, you can identify forward-looking statements by terminology such as *may*, *should*, *expects*, *plans*, *anticipates*, *believes*, *estimates*, *predicts*, *potential* or *continue* or the negative or other comparable terminology. These statements are only predictions and involve known and unknown risks, uncertainties and other factors, including the risks in the section entitled *Risk Factors*, that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Except as required by applicable law, including the securities laws of the United States, we do not intend to update any of the forward-looking statements to conform these statements to actual results.

Our financial statements are stated in United States dollars and are prepared in accordance with United States Generally Accepted Accounting Principles. In this quarterly report, unless otherwise specified, all dollar amounts are expressed in United States dollars. All references to *shares* of common stock refer to the common shares in our capital stock.

As used in this quarterly report, the terms *we*, *us*, *our company*, and *HS3* mean HS3 Technologies, Inc., a Nevada corporation, unless otherwise indicated.

### Corporate History

We were incorporated under the laws of the State of Nevada on January 28, 2003 under the name Zeno Inc. Following our incorporation, we focussed our business efforts on establishing our company as an exploration stage mineral exploration company, with claims on properties located in the Thunder Bay Mining District in Ontario, Canada.

We were not successful in implementing our business plan or successful in raising sufficient capital to explore our properties in any material way. As management of our company investigated opportunities and challenges involved with financing and exploring our properties, management realized that the business did not present the best opportunity for our company to realize value for our shareholders. Accordingly, we abandoned our exploration plan and focussed on the identification of suitable businesses with which to enter into a business opportunity or business combination.

On or about October 10, 2005, we changed our name to HS3 Technologies, Inc.

On August 31, 2005, we entered into an asset purchase agreement with IP-Colo, Inc. (IPC). The agreement contemplated acquisition of all of the assets of IPC. IPC was incorporated pursuant to the laws of the State of Colorado on December 24, 2004. IPC is in the development stage of providing advanced wireless technologies, integrated with high-speed internet via satellite to provide real-time security and monitoring for many industries.

The closing of the transactions contemplated in the agreement and the acquisition by our company of all of the assets of IPC occurred on November 9, 2005. In accordance with the closing of the agreement, and effective as of November 9, 2005, we acquired all of the assets of IPC, in exchange for the issuance by our company of 1,612,520 shares of our common stock to the shareholders of IPC.

Our company had 77,623,000 shares of common stock issued and outstanding as of November 9, 2005 immediately prior to the issuance of 1,612,520 shares of common stock in connection with the closing of the agreement and prior to the cancellation of 9,269,520 shares of common stock that were outstanding on closing that have been agreed to

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be cancelled. The former shareholders of IPC now owns 1,612,520 shares of our common stock, which represented approximately 2.30% of the issued and outstanding shares of our common stock on November 9, 2005, and 38,700,480 additional shares of common stock which represented a further 55.31% of our 69,966,000 issued and outstanding shares of common stock as of November 9, 2005.

As the shareholders of IPC held 57.6% of our shares of common stock, and because the business of IPC represents the only business operations of our company, the acquisition of IPC is deemed to be a reverse acquisition for accounting purposes. Starting with the periodic report for the quarter in which the acquisition was consummated, our company will file quarterly and annual reports based on the June 30, 2005 fiscal year end of IPC. Such financial statements will depict the operating results of IPC from its inception (December 24, 2004) and our company from November 9, 2005.

The shares of our common stock issued to the shareholders of IPC pursuant to the agreement and the shares of common stock issued under the subscription agreement will not be registered with the United States Securities Exchange Commission or the securities commission of any state in the United States, and were issued in reliance upon an exemption from registration under the United States Securities Act of 1933, as amended.

On September 6, 2006, the Company effected a one (1) new for four (4) old reverse stock split of its authorized, issued and outstanding stock. As a result, its authorized capital decreased to 50,000,000 shares of common stock with a par value of \$0.001 each and 2,500,000 preferred stock with a par value of \$0.001 each.

#### **Current Business**

Following the closing of the agreement with IPC, our company commenced the development of the internet services and wireless technology acquired from IPC.

Currently Hs3 Technologies, Inc. is primarily focused in the security industry. We are broadening our focus from a premiere satellite security company to a diverse organization that will meet the many needs of the security industry with a rich line of products, integrated solutions, and services that provide customers with a customized approach to meet all levels of the security industry. According to Security Industry Association (SIA) the electronic security business is a business that constitutes more than \$30 billion per year. This figure climbs to over \$100 billion when factoring in ancillary services and products such as guards, barriers and fences, etc. Many projections forecast sustained industry growth of 10 to 15 percent annually through the year 2020. World events are identifying increased use of security products and services across virtually every segment of society.

We have refocused our company and are pleased to announce that we have expanded our market strategies with a diverse new line of cutting edge products and services to meet the growing needs of the security industry. To meet the ever changing needs of the industry, HS3 is launching a combination of state-of-the art products and services that include digital video recording technology (DVR), biometric access control (door locks), personal biometric identification units, CCTV, video monitoring centers, cellular networks, wireless mesh network units and wireless internet-linked satellite surveillance systems. This will encompass a total line of products that will meet virtually all commercial and residential customer security needs.

Our integrated security system solutions will primarily focus on three customer groups; business, government, and residential.

With the ever increasing need to protect company employees, assets and inventory the business customer has already identified the requirements for a higher, less intrusive and less expensive solution.

The government has always been very aware of the need for security. Since 9/11 the priority and focus has steadily increased opening up a tremendous opportunity to market customized security solutions.

Although the residential customer market commands the largest amount of opportunity, it is the toughest segment to support effectively. The residential customer is highly demanding of their security service needs for the lowest price point.





We are continuing to establish a sales network capable of delivering our unique products and services, nationally and internationally, through distribution, dealers and directly to end users. There are different types of distributors and dealers. The distributors cater to their specific markets and the dealers specialize in various products and services. There are of course many types of end users. We are also able to compliment our products and services with are customers through the close relationships we have developed with are manufacturing and distribution partners. While each serves a different segment such as Biometric access control, CCTV or remote monitoring products all of our products and services enhance the level of security protection and surveillance needs.

We understand the market focus is important. We plan on meeting the critical needs through customized integration. By integrating technology, service and people into our programs we can give all of our customers a substantial benefit while being on the leading edge of the industry. This plan will also help HS3 forge stronger relationship with our partners and form better strategic alliances.

### **Market Growth Strategy**

The number of prospective customers for the security industry is unlimited. With the internet reaching the entire globe HS3 is able to provide its products and services to anyone in the world. The security products and services we offer are the fastest growing and most requested in the industry.

Our strategy for internal growth starts with HS3 building a sales force that consists of inside, outside/external sales representatives, and independent representatives. Each set of representatives will be responsible for different sectors of the market.

To reach our market penetration strategy we will use a combination of inside, outside, and independent sales representatives supported by an aggressive advertising campaign to reach the three different levels of the security industry: distribution, dealer and end user. We will also use an aggressive advertising campaign to reach the individual business and home owners to drive business to our dealer network.

HS3 also plans on aggressively pursuing several acquisition possibilities that will compliment the current product line and business model and strengthen the company.

### **Manufacturing**

Manufacturing of our products will be contracted to third parties. These contract manufacturers have expertise in the manufacturing of products such as ours. We will rely on these contract manufacturers to produce high quality products for sale to our customers.

### **Competition**

We will face competition from companies providing a variety of security products and services. Many of our competitors and potential competitors have established customer bases, widespread brand recognition and existing partnerships with other industry participants, as well as substantially greater financial, technical and marketing resources than we do. We expect significant competitive factors to include: price, service reliability, ease of access and use, transmission speeds, breadth of service offerings, customer support, brand recognition, operating experience, and the ability to bundle complementary services. We expect to encounter a number of challenges in competing with companies already providing some of the same products and services. Our plans are to stay ahead of the competition by establishing exclusive relationships for OEM designed and produced products unique to the industry. Many of these companies have an entrenched position in the marketplace and lower upfront installation charges than ours. Increased competition may come in the form of new market entrants, greater cooperation among our competitors, whether in the form of alliances or vertical or horizontal integration, or changes in the capabilities of other companies arising from technological innovations that we cannot foresee.

### **Regulation**

The majority of this industry is in an unregulated format. With part of our product line related to satellite usage the satellite industry is highly regulated both in the United States and internationally. We are subject to the regulatory authority of the U.S. government, primarily through the FCC. The FCC is the government agency with primary authority in the United States to regulate and license commercial satellite systems, including those which we will be dependent upon. FCC rules require that satellite systems avoid interfering with other authorized users of radio spectrum, and that they comply with FCC rules governing U.S.-licensed satellite systems in general and Ka-band geostationary satellite systems in particular. The U.S. Congress has enacted the Communications Assistance for Law Enforcement Act of 1994, or CALEA, which requires that any equipment, facilities, and services deployed by telecommunications carriers meet certain electronic surveillance requirements identified in the statute. The statute specifically exempts providers of information services, such as internet service providers. We believe that the services we intend to offer will not be covered by CALEA. However, the convergence of technology continues to blur the line between exempt information services and covered telecommunications services. If we were held to be subject to the requirements of CALEA, we may have to deploy additional equipment in order to comply with the statutory obligations, and we could be subject to monetary civil penalties for failure to comply with the statute or implementing regulations.

### **Research and Development**

Our company's research and development efforts are focussed on enhancing our products including: (i) periodic re-design of products and incorporation of new technologies to improve performance and manufacturability; (ii) design of new product lines for standard products and additional specialized applications; and (iii) expansion and adaption of existing products to accommodate the requirements of customer needs. Research and development efforts are conducted in-house, by contracted consultants and with unique exclusive relationships developed with some of our suppliers.

### **Intellectual Property**

Our company owns and operates the duly registered internet domain name: [www.HS3Tech.com](http://www.HS3Tech.com). The information contained in our website is not part of this current report.

### **Employees**

As of December 31, 2006, our company had 6 full-time employees and no part-time employees. Of those employees, none are covered by collective bargaining agreements.

### **Description of Property**

Our principal executive offices are located at 1800 Boulder Street Suite 600, Denver, Colorado, USA 80211. The 3,000 square foot space is leased for \$4,000 per month from a company owned by a major stockholder of the Company, for a 3-year term that commenced on October 1, 2005. We believe that our principal office will be adequate for our needs for the next 3 years.

### **Critical Accounting Policies**

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

#### *Revenue Recognition*

We believe our revenue recognition policies are in compliance with all applicable accounting regulations. In summary, we recognize revenues from the sale of products and services when it can be determined that pervasive



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evidence of an arrangement exists, delivery and acceptance has occurred, the revenues are established or determinable and collectability is probable.

*Inventory*

Inventory consists of finished goods purchased from third-party manufacturers and is valued at the lower of average cost or market. Average cost is determined using the first-in, first-out method of accounting.

**Plan of Operation And Cash Requirements**

We are a development stage company that has generated minimal revenues.

Our operating expenses consist mostly of sales and marketing and general and administrative expenses. The amount incurred by our company during the period from inception to December 31, 2006 was \$758,928 and \$743,366, respectively. We anticipate that we will require up to \$1,160,000 for the 12 months ending December 31, 2007 to develop our internet and wireless technology products and provide for the expansion and adaptation of existing products to accommodate the requirements of customer needs.

*Purchase of Significant Equipment*

We do anticipate the purchase or sale of any plant or significant equipment during the next twelve-month period. This could include equipment for increased bandwidth requirements, and equipment for monitoring services.

*Personnel Plan*

We do anticipate significant changes in the number of employees during the next twelve-month period.

*Off-Balance Sheet Arrangements*

There are no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

Our principal capital resources have been through the subscription and issuance of common stock, although we may use stockholder loans, advances from related parties, or borrowing in the future.

*Cash Requirements*

We will require additional funds to implement our growth strategy in exploration operations. These funds may be raised through equity financing, debt financing, or other sources, which may result in further dilution in the equity ownership of our shares. There is still no assurance that we will be able to maintain operations at a level sufficient for an investor to obtain a return on his investment in our common stock. Further, we may continue to be unprofitable.

Estimated Funding Required During the Twelve Month Period Ending December 31, 2007

Operating expenses		
Sales and Marketing	\$	250,000
Research and Development		150,000
Consulting and Professional Fees and Wages		60,000



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Product Development	50,000
Public Relations	150,000
Travel and Promotion	200,000
General and Administrative	200,000
Total Operating Expenses	1,060,000
Working Capital	100,000
<b>Total</b>	<b>\$ 1,160,000</b>

We currently anticipate that revenues will commence and increase in the long-term as we increase our sales and marketing activities and introduce new products relating to internet services and wireless technology. We expect to keep our operating costs to a minimum until cash is available through operating or financing activities. We anticipate that we will start generating modest revenues from internet services and wireless technology within the next three months, however, we are not in a position to predict whether we will be able to generate sufficient sales revenues to meet operating expenses.

There can be no assurance that additional financing will be available to us when needed or, if available, that it can be obtained on commercially reasonable terms. If we are not able to obtain the additional financing on a timely basis, if and when it is needed, we will be forced to scale down or perhaps even cease the operation of our business.

#### *Going Concern*

Due to our being a development stage company and not having generated significant revenues, in the Report of our Independent Registered Public Accounting Firm for the year ended June 30, 2006, our independent auditors included an explanatory paragraph regarding substantial doubt about our ability to continue as a going concern.

We have historically incurred losses, and through December 31, 2006 have incurred losses of \$3,657,848 since our inception. Because of these historical losses, we will require additional working capital to develop our business operations. We intend to raise additional working capital through private placements, public offerings, bank financing and/or advances from related parties or stockholder loans.

The continuation of our business is dependent upon obtaining further financing and achieving a break even or profitable level of operations. The issuance of additional equity securities by us could result in a significant dilution in the equity interests of our current or future stockholders. Obtaining commercial loans, assuming those loans would be available, will increase our liabilities and future cash commitments.

There are no assurances that we will be able to either (i) achieve a level of revenues adequate to generate sufficient cash flow from operations; or (ii) obtain additional financing through either private placements, public offerings and/or bank financing necessary to support our working capital requirements. To the extent that funds generated from operations and any private placements, public offerings and/or bank financing are insufficient, we will have to raise additional working capital. No assurance can be given that additional financing will be available, or if available, will be on terms acceptable to us. If adequate working capital is not available we may not increase our operations.

These conditions raise substantial doubt about our ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might be necessary should we be unable to continue as a going concern.

## RISK FACTORS

Much of the information included in this quarterly report includes or is based upon estimates, projections or other forward-looking statements. Such forward-looking statements include any projections or estimates made by us and our management in connection with our business operations. While these forward-looking statements, and any assumptions upon which they are based, are made in good faith and reflect our current judgment regarding the direction of our business, actual results will almost always vary, sometimes materially, from any estimates, predictions, projections, assumptions, or other future performance suggested herein. We undertake no obligation to update forward-looking statements to reflect events or circumstances occurring after the date of such statements.

Such estimates, projections or other forward-looking statements involve various risks and uncertainties as outlined below. We caution readers of this quarterly report that important factors in some cases have affected and, in the future, could materially affect actual results and cause actual results to differ materially from the results expressed in any such estimates, projections or other forward-looking statements. In evaluating us, our business and any investment in our business, readers should carefully consider the following factors.

Our new business operations will be subject to a number of risks and uncertainties, including those set forth below:

### RISKS RELATED TO OUR BUSINESS

*We will require significant additional financing, the availability of which cannot be assured, and if our company is unable to obtain such financing, our business may fail.*

Our business plan calls for significant expenses necessary to continue the development of our business and expand our position in the market. There is no assurance that actual cash requirements will not exceed our estimates. We may need to raise additional funds to:

- support our planned growth;
- develop or enhance new and existing products;
- increase our marketing efforts;
- acquire complementary businesses, products or technologies; and/or
- respond to competitive pressures or unanticipated requirements.

We have not yet achieved sustainable positive cash flows. As such, we will depend to a large extent on outside capital over the near-term to fund our capital needs. Such outside capital may be obtained from additional debt or equity financing. We do not currently have any arrangement for financing and there is no assurance that capital will be available to meet our operating costs or, if the capital is available, that it will be on terms acceptable to us. The issuance of additional equity securities by us would result in a dilution in the equity interests of our current shareholders. Obtaining commercial loans, assuming those loans would be available, will increase our liabilities and future cash commitments. If we are unable to obtain financing in the amounts and on terms deemed acceptable to us, we may be unable to implement our business and growth strategies, respond to changing business or economic conditions, withstand adverse operating results, consummate desired acquisitions or compete effectively.

*We operate in a highly-competitive industry and our failure to compete effectively may adversely affect our ability to generate revenue.*

Management is aware of similar products which compete directly with our products and some of the companies developing these products have significantly greater financial, technical and marketing resources, larger distribution networks, and generate greater revenue and have greater name recognition than us. These companies may develop products superior to those of our company. Such competition will potentially affect our chances of achieving profitability, and ultimately adversely affect our ability to continue as a going concern.





Some of our competitors conduct more extensive promotional activities and offer lower prices to customers than we do, which could allow them to gain greater market share or prevent us from increasing our market share. In the future, we may need to decrease our prices if our competitors continue to lower their prices. Our competitors may be able to respond more quickly to new or changing opportunities, technologies and customer requirements. To be successful, we must carry out our business plan, establish and strengthen our brand awareness through marketing, effectively differentiate our product line from those of our competitors and build our distribution network. To achieve this we may have to substantially increase marketing and research and development in order to compete effectively. Such competition will potentially affect our chances of achieving profitability, and ultimately adversely affect our ability to continue as a going concern.

*Rapid technological changes in our industry could render our products or services non-competitive or obsolete and consequently affect our ability to generate revenues.*

We will derive all of our revenues from the sale of internet services and related security products. Such products and services are characterised and affected by rapid technological change, evolving industry standards and regulations and changing client preferences. Our success will depend, in significant part, upon our ability to make timely and cost-effective enhancements and additions to our technology and to introduce new products and services that meet customer demands. We expect new products and services to be developed and introduced by other companies that compete with our products and services. The proliferation of new and established companies offering similar services and products may reduce demand for our particular products. There can be no assurance that we will be successful in responding to these or other technological changes, to evolving industry standards or regulations or to new products and services offered by our current and future competitors. In addition, we may not have access to sufficient capital for our research and development needs in order to develop new products and services.

*We could lose our competitive advantages if we are not able to protect our proprietary technology and intellectual property rights against infringement, and any related litigation could be time-consuming and costly.*

Our success and ability to compete depends in part on our proprietary technology incorporated in our products. If any of our competitors copy or otherwise gain access to our proprietary technology or develop similar technologies independently, we would not be able to compete as effectively. We consider our technologies invaluable to our ability to continue to develop and maintain the goodwill and recognition associated with our brand. The measures we take to protect our technologies, and other intellectual property rights, which presently are based upon registered trade marks in addition to trade secrets, may not be adequate to prevent their unauthorized use. Although we rely, in part, on contractual provisions to protect our trade secrets and proprietary know-how, there is no assurance that these agreements will not be breached, that we would have adequate remedies for any breach or that our trade secrets will not otherwise become known or be independently developed by competitors. Further, the laws of foreign countries may provide inadequate protection of intellectual property rights. We may need to bring legal claims to enforce or protect our intellectual property rights. Any litigation, whether successful or unsuccessful, could result in substantial costs and a diversion of corporate resources. In addition, notwithstanding any rights we have secured to our intellectual property, other persons may bring claims against us claiming that we have infringed on their intellectual property rights, including claims that our intellectual property rights are not valid. Adverse determinations in litigation in which we may become involved could subject us to significant liabilities to third parties, require us to grant licenses to or seek licenses from third parties and prevent us from manufacturing and selling our products. Any claims against us, with or without merit, could be time-consuming and costly to defend or litigate, divert our attention and resources, result in the loss of goodwill associated with our trademarks or require us to make changes to our technologies. Furthermore, we cannot assure you that any pending patent application made by us will result in an issued patent, or that, if a patent is issued, it will provide meaningful protection against competitors or competitor technologies.

*We may not be able to hire and retain qualified personnel to support our growth and if we are unable to retain or hire such personnel in the future, our ability to improve our products and implement our business objectives could be adversely effected.*

To continue our growth, we will need to recruit additional senior management personnel, including persons with financial and sales experience. In addition, we must hire, train and retain a significant number of other skilled personnel, including persons with experience in sales and marketing. We have encountered competition for these

personnel. We may not be able to find or retain qualified personnel, which will have a material adverse impact on our business.

#### RISKS RELATED TO OUR INDUSTRY

*Risks relating to satellite launch and operations could prevent us from commencing operations or further expanding our business.*

If we fail to negotiate contracts with one or more of our satellite providers, we might not be able to offer our services. A significant percentage of satellites never become operational because of launch failure, satellite destruction or damage during launch, or improper orbital placement. Whomever we enter into an agreement with for satellite services might not be able to successfully launch or operate the satellites, and our contractual remedies will not adequately compensate us for lost revenue. We will not be able to offer any service and generate any revenue until we have access to satellite bandwidth.

*Delays in the construction and launch of satellites are common, and performance failure by satellite and launch contractors could delay the introduction or expansion of our services and ability to meet our revenue projections.*

We might not be able to timely introduce and expand our services and meet our revenue expectations if there is a delay in manufacturing or launching satellites that we will depend upon for satellite bandwidth. Delays in the construction and launch of satellites are common, and there are limited suppliers of these services. We must rely on third parties to construct and launch satellites and then provide us with access to them. If any of these parties become insolvent or fail to perform their obligations for us in a timely manner, the introduction, operation or expansion of our services could be delayed. If any of these parties default on their contracts, our contractual remedies will not adequately compensate us for our lost revenue and our anticipated competitive advantage.

*Failure to develop key vendor and service-provider relationships for essential components of our business on acceptable terms or in a timely manner could delay the introduction of our services and result in greater expenses than we expect.*

We will depend on third parties to provide us with many services that will be essential for the conduct of our business. If we fail to establish key service-provider relationships on acceptable terms or in a timely manner, the commencement of our services could be delayed and our costs could significantly increase. We are in various stages of discussions with third parties to provide these essential services, which most importantly, includes access to satellite bandwidth at cost-effective prices. These relationships will be vital to our ability to provide our services, to grow and add customers and to efficiently operate our business. We might not be able to enter into these relationships or do so on commercially reasonable terms or within the time necessary to launch our services. If we do enter into these relationships, our service providers and vendors might not be sufficiently responsive to our needs or meet our performance standards, which could increase our expenses, delay the introduction of our services or impair the quality of our services.

*Our services depend on the development and integration of complex technologies in a novel configuration that might not function as designed, which might prevent us from offering our services as planned, or at all.*

Our services will require new applications of existing technology and the complex integration of different technologies, which might not operate as designed. Components of satellite, gateway and related technologies are still being developed and have not yet been tested in actual operations. Hardware or software errors in space or on the ground could increase costs, delay our ability to offer our services, cause us to lose customers or prevent us from offering our services at all, each of which could limit our ability to generate revenue and become profitable.

*Premature failure of satellites that we will rely upon could hurt our business reputation and projected revenue and earnings.*

Satellites have limited useful lives, and if one of the satellites were to prematurely fail, it could adversely affect the quality of our services, our business reputation, and our projected revenue and earnings. Any of the satellites could

fail before the end of their useful lives. There are many causes for the in-orbit failure of satellites, including: - component failure; - loss of power or fuel; - construction defects; - unexpected degradation of solar panels; - mistakes in issuing commands to the satellite; - inability to control the position, altitude, or orientation of the satellite; - disruptive military actions or acts of war; and - damage or destruction due to solar storms or other astronomical events, or collisions with space debris. Any premature failure could hurt market acceptance of our services and our competitive position.

*Satellite technology has inherent limitations that could adversely affect the quality of our service, customer retention, revenue growth and profitability.*

The satellites that we will rely upon will operate in the Ka-band portion of the radio-frequency spectrum. Satellites of this type have inherent technological limitations, the most significant being latency and an occurrence known as rain fade. In addition, two-way communications satellites generally have a fixed capacity limitation. Each of these limitations could cause us to lose customers and could adversely affect the quality of our service, revenue and ability to achieve or sustain profitability. Latency: Latency is the delay caused by the time it takes for data traveling in a network to travel up to one of the satellites and back to earth. GEO satellites have a relatively high round-trip latency compared to satellite systems closer to the earth or broadband systems located on the earth. While the latency of low-orbit satellite and terrestrial-based broadband signals is approximately 30 to 70 milliseconds, the latency of GEO satellite signals is approximately 250 milliseconds, or one-quarter of a second. This relatively high latency will prevent our satellite system from supporting, in a high-quality fashion, time-sensitive services such as toll-quality voice calls and highly interactive games, or similar products and services that may be developed and introduced over broadband networks in the future. This limitation could affect our ability to compete with other broadband internet services, such as terrestrial broadband services, that do not experience similar latency. Rain Fade: Rainfall affects Ka-band signals more severely than signals in the lower frequency satellite communication bands currently in use, such as Ku-band. This occurrence is known as rain fade. Our service could slow down or even stop during periods of heavy rain. This limitation could adversely impact the quality and market acceptance of our services. Fixed Capacity: Satellites have a fixed amount of capacity to handle two-way data traffic. As a result, we might not be able to meet our customers' transmission speed expectations. The transmission speeds we can deliver to our customers at any particular time depend on several factors that we cannot predict, such as the number of customers online at any one time, the connection speeds used by these customers, their usage patterns, the types and quantity of content accessed over our system and the geographic location of our customers. Although we have designed our system to account for anticipated usage patterns, we might not be able to provide a satisfactory broadband experience for our customers at all times due to capacity constraints. If we do not have sufficient capacity on a particular satellite or in a specific geographic region to meet the peak demand levels, some of our customers will experience service degradation, such as slower than expected access speeds, which could damage our business reputation, cause customer dissatisfaction and result in a loss of customers. Installing additional capacity or reallocating existing capacity could be expensive and time consuming. As a result, our fixed-capacity limitation could negatively affect our revenue.

*Our services will face intense competition from providers of terrestrial broadband services and other satellite system operators, and if we cannot effectively compete, we might be unable to expand our business and achieve profitability.*

We will face competition from companies providing a wide variety of wireless and wireline internet access services, some of which could have distinct advantages over our service. We might not be able to effectively compete with these companies, which could limit our revenue and our ability to achieve, sustain or grow profitability. Some of these services require little or no start-up costs for consumers, and they do not require consumers to install a satellite dish. We could also experience increased competition from new terrestrial wireless technologies, such as local multi-point distribution services and multi-channel multi-point distribution services. Mergers, joint ventures and alliances among franchise, wireless or private cable television operators, regional Bell operating companies and others could result in providers offering bundled telecommunications services in competition with us. Increased competition might result in our inability to obtain significant market share or compel us to reduce prices to remain competitive, which could result in lower gross margins.

Many of our competitors and potential competitors have widespread brand recognition, existing partnerships with industry participants and greater financial, marketing, distribution, technical and other resources than we do. As a

result, they might be able to respond more quickly than we can to new opportunities and technologies. In addition, many of these competitors already offer, or will offer, internet access packages integrated with other communications services. Our ability to compete with these companies will depend on our ability to provide substantially similar or better service at prices that are competitive with those offered by these companies and to effectively market our services.

*If we are not able to provide our service at competitive prices, our sales will suffer.*

We might not be able to offer our services at prices competitive with other broadband service providers, which could limit our sales and revenue growth. The manufacturing and distribution costs of our system could be more expensive than we anticipate, making it difficult for us to offer our service to customers at prices that will induce them to purchase our services and allow us to become profitable. Pricing of services to consumers in the telecommunications and internet access industries, both of which have similarities to the broadband service industry, have historically fallen, and we expect this to happen in the broadband internet access industry as well. We initially intend to subsidize the cost of acquiring and installing our CPE to encourage customers to make an initial investment in our services. As competition to provide broadband internet access services increases, we could be forced to lower prices for our services if our competitors engage in volume-based pricing and other forms of price competition. As a result, we might not be able to compete successfully with existing or potential competitors in the broadband internet access market.

*Our revenue growth depends on our ability to implement a successful distribution strategy for our services.*

We intend to sell our services primarily through local satellite television dealers, DBS service providers, national electronics and department store chains and through wholesale channels such as communications service providers. We might not be able to establish or maintain these relationships, which could decrease our revenue. We have limited experience in developing distribution relationships of this type. If we are unsuccessful in developing additional distribution relationships, or if parties with which we develop relationships do not perform as expected, our services might not achieve broad market acceptance and our ability to grow our business could be significantly harmed.

*Demand for our services might be insufficient for us to become profitable.*

We cannot predict with certainty the potential consumer demand for our services or the degree to which we will meet that demand. If demand for our services does not develop as expected and achieve consumer market acceptance, we might not be able to generate enough revenue to become profitable or to sustain our operations. Among other things, we believe that consumer acceptance of our services will depend upon our ability to: - provide a competitively priced, high-quality satellite broadband service; - successfully brand, market and sell our services on a nationwide basis; - efficiently use established DBS distribution channels; and - enter into and capitalize on additional strategic distribution relationships. We will initially focus our sales and marketing efforts to target the U.S. households and industries that will not have access to terrestrial broadband services, such as DSL or cable modem service, at the time we commence our services. We have based our strategy to target these consumers on a number of assumptions, some or all of which could prove to be incorrect. Even if markets for our service develop, we could achieve a smaller share of these markets than we currently anticipate.

*Rapid technological and industry changes could make our services obsolete or outdated, which could cause our sales to suffer.*

The broadband communications industry is characterized by rapid technological change, frequent product innovations, changes in customer requirements and expectations, and evolving industry standards. If we are unable to keep pace with these changes, our sales will suffer. Competitors could have access to technologies not available to us, which might enable them to build a system that is more appealing to consumers. Products and services using new technologies, or emerging industry standards, could make our technologies obsolete. Our success will depend in part on our ability to bring our services to our target markets before competing technologies become widely accepted, as well as our ability to adapt and implement new technologies and services.

*Failure to comply with existing, changing or new regulatory requirements could prevent or delay our ability to implement our current business plan.*

We are subject to the regulatory authority of the FCC, the frequency coordination process of the International Telecommunication Union, or ITU, and the regulatory requirements of other countries in which we plan to offer our services. Failure to comply with existing, changing or new regulations could prevent us from implementing our current business plan. Regulatory changes could significantly impact our operations by, among other things: - adding terms and conditions to the continuing effectiveness of our licenses; - changing blanket licensing requirements for our CPE; - imposing fees or other charges, thereby raising our compliance costs; - requiring that we relocate one or more of our satellites to a different orbital location; - allocating remaining Ka-band spectrum favorably to our competitors; and - making current products obsolete. We might need to modify our services or operations to comply with new or changed regulations. These modifications could be expensive and time consuming, and could adversely affect our ability to provide our services cost effectively or at all.

#### RISKS RELATED TO OUR COMMON STOCK

*A decline in the price of our common stock could affect our ability to raise further working capital and adversely impact our operations.*

A prolonged decline in the price of our common stock could result in a reduction in the liquidity of our common stock and a reduction in our ability to raise capital. Because our operations have been financed through the sale of equity securities, a decline in the price of our common stock could be especially detrimental to our liquidity and our continued operations. Any reduction in our ability to raise equity capital in the future would force us to reallocate funds from other planned uses and would have a significant negative effect on our business plans and operations, including our ability to develop new products and continue our current operations. If the stock price declines, there can be no assurance that we can raise additional capital or generate funds from operations sufficient to meet our obligations. We believe the following factors could cause the market price of our common stock to continue to fluctuate widely and could cause our common stock to trade at a price below the price at which you purchase your shares of common stock:

- actual or anticipated variations in our quarterly operating results;
- announcements of new services, products, acquisitions or strategic relationships by us or our competitors;
- trends or conditions in the internet service provider and satellite wireless industry;
- changes in accounting treatments or principles;
- changes in earnings estimates by securities analysts and in analyst recommendations;
- changes in market valuations of other internet service provider and satellite wireless companies; and
- general political, economic, regulatory and market conditions.

The market price for our common stock may also be affected by our ability to meet or exceed expectations of analysts or investors. Any failure to meet these expectations, even if minor, could materially adversely affect the market price of our common stock.

*If we issue additional shares of common stock in the future, it will result in the dilution of our existing shareholders.*

Our certificate of incorporation authorizes the issuance of 50,000,000 shares of common stock. Our board of directors has the authority to issue additional shares of common stock up to the authorized capital stated in the certificate of incorporation. Our board of directors may choose to issue some or all of such shares of common stock to acquire one or more businesses or to provide additional financing in the future.



The issuance of any such shares of common stock will result in a reduction of the book value or market price of the outstanding shares of our common stock. If we do issue any such additional shares of common stock, such issuance also will cause a reduction in the proportionate ownership and voting power of all other shareholders. Further, any such issuance may result in a change of control of our corporation.

*If a market for our shares of common stock does not develop, shareholders may be unable to sell their shares of common stock.*

There is currently a limited market for our common stock, which trades through the Over-the-Counter Bulletin Board quotation system. Trading of stock through the Over-the-Counter Bulletin Board is frequently thin and highly volatile. There is no assurance that a sufficient market will develop in the stock, in which case it could be difficult for shareholders to sell their stock.

*Trading of our stock may be restricted by the Securities and Exchange Commission's penny stock regulations which may limit a stockholder's ability to buy and sell our stock.*

The Securities and Exchange Commission has adopted regulations which generally define "penny stock" to be any equity security that has a market price (as defined) less than \$5.00 per share or an exercise price of less than \$5.00 per share, subject to certain exceptions. Our securities are covered by the penny stock rules, which impose additional sales practice requirements on broker-dealers who sell to persons other than established customers and accredited investors. The term "accredited investor" refers generally to institutions with assets in excess of \$5,000,000 or individuals with a net worth in excess of \$1,000,000 or annual income exceeding \$200,000 or \$300,000 jointly with their spouse. The penny stock rules require a broker-dealer, prior to a transaction in a penny stock not otherwise exempt from the rules, to deliver a standardized risk disclosure document in a form prepared by the Securities and Exchange Commission which provides information about penny stocks and the nature and level of risks in the penny stock market. The broker-dealer also must provide the customer with current bid and offer quotations for the penny stock, the compensation of the broker-dealer and its salesperson in the transaction and monthly account statements showing the market value of each penny stock held in the customer's account. The bid and offer quotations, and the broker-dealer and salesperson compensation information, must be given to the customer orally or in writing prior to effecting the transaction and must be given to the customer in writing before or with the customer's confirmation. In addition, the penny stock rules require that prior to a transaction in a penny stock not otherwise exempt from these rules, the broker-dealer must make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser's written agreement to the transaction. These disclosure requirements may have the effect of reducing the level of trading activity in the secondary market for the stock that is subject to these penny stock rules. Consequently, these penny stock rules may affect the ability of broker-dealers to trade our securities. We believe that the penny stock rules discourage investor interest in and limit the marketability of, our common stock.

*The National Association of Securities Dealers Inc., or NASD, has adopted sales practice requirements, which may limit a stockholder's ability to buy and sell our shares of common stock.*

In addition to the "penny stock" rules described above, the NASD has adopted rules requiring that in recommending an investment to a customer, a broker-dealer must have reasonable grounds for believing that the investment is suitable for that customer. Prior to recommending speculative low-priced securities to their non-institutional customers, broker-dealers must make reasonable efforts to obtain information about the customer's financial status, tax status, investment objectives and other information. Under interpretations of these rules, the NASD believes that there is a high probability that speculative low-priced securities will not be suitable for at least some customers.

The NASD requirements make it more difficult for broker-dealers to recommend that their customers buy our common stock, which may limit our shareholders' ability to buy and sell our stock and which may have an adverse effect on the market for our shares of common stock.

### **Item 3. Controls and Procedures**

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as of the end of the period covered by the quarterly report, being September 30, 2006, we have carried out an evaluation of the effectiveness of the design and operation of our company's disclosure controls and procedures. This evaluation was carried out under the supervision and with the participation of our company's management, including our company's president and chief executive officer and our chief operating officer. Based upon that evaluation, our company's president concluded that our company's disclosure controls and procedures are effective as at the end of the period covered by this report. There have been no changes in our internal controls over financial reporting that occurred during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect our internal controls over financial reporting.

Disclosure controls and procedures and other procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time period specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934 is accumulated and communicated to management, including our president and chief executive officer and our chief operating officer as appropriate, to allow timely decisions regarding required disclosure.

## **PART II - OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

We know of no material, existing or pending legal proceedings against our company, nor are we involved as a plaintiff in any material proceeding or pending litigation. There are no proceedings in which any of our directors, officers or affiliates, or any registered or beneficial stockholder, is an adverse party or has a material interest adverse to our interest. The outcome of open unresolved legal proceedings is presently indeterminable. Any settlement resulting from resolution of these contingencies will be accounted for in the period of settlement. We do not believe the potential outcome from these legal proceedings will significantly impact our financial position, operations or cash flows.

### **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None

### **Item 3. Defaults Upon Senior Securities**

None.

### **Item 4. Submission of Matters to a Vote of Security Holders**

None.

### **Item 5. Other Information**

Our Common stock is quoted on the OTC Bulletin Board under the Symbol HSTH. Our stock was originally approved for trading on the OTC Bulletin Board under the symbol ZNNO. On November 25, 2005 our symbol was changed to HSTT in connection with a change of name. On September 6, 2006 our symbol was changed to HSTH in connection with a forward stock split.



**Item 6. Exhibits.**

*Exhibits required by Item 601 of Regulation S-B*

Exhibit Number/Description

**(3) Articles of Incorporation and Bylaws**

3.1 Articles of Incorporation (incorporated by reference from our Registration Statement on Form SB-2 filed on August 2, 2004).

3.2 By-laws (incorporated by reference from our Registration Statement on Form SB-2 filed on August 2, 2004).

**(4) Instruments Defining the Rights of Security Holders, Including Indentures**

4.1 2005 Stock Option Plan of HS3 Technologies, Inc. (incorporated by reference from our Current Report on Form 8-K filed on November 10, 2005).

**(10) Material Contracts**

10.1 Share Purchase Agreement dated March 5, 2005 among Zeno Inc., Linda Smith, Acropolis Investment Holdings, LLC and Gregory S. Yanke Law Corporation (incorporated by reference from our Current Report on Form 8-K filed on March 10, 2005).

10.2 Asset Purchase Agreement dated August 31, 2005, between Zeno Inc. and IP-Colo, Inc. (incorporated by reference from our Current Report on Form 8-K filed on September 16, 2005).

10.3 Surveillance Instalment and Training Agreement dated December 20, 2005 (incorporated by reference from our Current Report on Form 8-K filed December 23, 2005).

**(16) Letter on Change in Certifying Accountant**

16.1 Letter from Amisano Hanson, Chartered Accountants regarding change in certifying accountant (incorporated by reference from our Form 8-K/A filed on January 17, 2006).

**(31) Section 302 Certifications**

31.1 Section 302 Certification (filed herewith).

**(32) Section 906 Certification**

32.1 Section 906 Certification (filed herewith).

**SIGNATURES**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**HS3 TECHNOLOGIES, INC.**

By: /s/ Mark Lana  
Mark Lana

President, Chief Executive Officer and Director

(Principal Executive Officer)

Dated February 12, 2007