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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2009

OR

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

Commission file number 001-33852

**VirnetX Holding Corporation**

(Exact name of registrant as specified in its charter)

Delaware

(State or Other Jurisdiction of Incorporation or Organization)

77-0390628

(I.R.S. Employer Identification No.)

5615 Scotts Valley Drive, Suite 110

Scotts Valley, California

(Address of Principal Executive Offices)

95066

(Zip Code)

(831) 438-8200

(Registrant's Telephone Number, Including Area Code)

**Not applicable**

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

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Act of 1934 during the preceding 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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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

The number of shares outstanding of the Registrant's Common Stock as of May 5, 2009 was 37,369,985.

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VIRNETX HOLDING CORPORATION

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## PART I — FINANCIAL INFORMATION

## ITEM 1. — FINANCIAL STATEMENTS.

VIRNETX HOLDING CORPORATION  
(a development stage enterprise)  
CONDENSED CONSOLIDATED BALANCE SHEETS

	<u>March 31,</u> <u>2009</u>	<u>December 31,</u> <u>2008</u>
	<u>(Unaudited)</u>	
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 1,526,042	\$ 457,155
Accounts receivable, net	2,730	1,154
Prepaid expense and other current assets	193,772	189,847
<b>Total current assets</b>	<b>1,722,544</b>	<b>648,156</b>
Property and equipment, net	28,895	32,565
Intangible and other assets	192,000	204,000
Deferred offering costs	—	94,261
<b>Total assets</b>	<b>\$ 1,943,439</b>	<b>\$ 978,982</b>

See accompanying notes to condensed consolidated financial statements

**VIRNETX HOLDING CORPORATION**  
**(a development stage enterprise)**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

	<b>March 31, 2009</b>	<b>December 31, 2008</b>
	<b>(Unaudited)</b>	
<b>LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)</b>		
Current liabilities		
Accounts payable and accrued expenses	\$ 2,123,351	\$ 1,669,333
Current portion of long-term obligation	40,000	44,000
<b>Total current liabilities</b>	<b>2,163,351</b>	<b>1,713,333</b>
Long-term obligation, net of current portion	120,000	160,000
Commitments and contingencies		
Stockholders' equity		
Preferred stock, par value \$0.0001 per share, authorized 10,000,000 shares issued and outstanding: 0 shares at March 31, 2009 and December 31, 2008, respectively	—	—
Common stock, par value \$0.0001 per share, authorized 100,000,000 shares, issued and outstanding: 37,369,985 shares at March 31, 2009 and 34,899,985 at December 31, 2008, respectively	3,737	3,489
Additional paid-in capital	26,107,520	22,150,321
Deficit Accumulated during the development stage	(26,451,169)	(23,048,161)
<b>Total stockholders' equity (deficit)</b>	<b>(339,912)</b>	<b>(894,351)</b>
<b>Total liabilities and stockholders' equity (deficit)</b>	<b>\$ 1,943,439</b>	<b>\$ 978,982</b>

See accompanying notes to condensed consolidated financial statements

**VIRNETX HOLDING CORPORATION**  
**(a development stage enterprise)**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(Unaudited)**

	<b>Three Months Ended</b>	<b>Three Months Ended</b>	<b>For the period</b>
	<b>March 31, 2009</b>	<b>March 31, 2008</b>	<b>August 2, 2005</b>
			<b>(Date of Inception)</b>
			<b>to March 31, 2009</b>
Revenue — royalties	\$ 3,154	\$ 33,306	\$ 211,764
Operating expense			
Research and development	221,699	177,714	2,361,526
General and administrative	3,186,690	2,957,908	24,417,558
<b>Total operating expense</b>	<b>(3,408,389)</b>	<b>(3,135,622)</b>	<b>(26,779,084)</b>
Loss from operations	(3,405,235)	(3,102,316)	(26,567,320)
Interest and other income, net	2,227	70,581	116,151
Net loss	\$ (3,403,008)	\$ (3,031,735)	\$ (26,451,169)
Basic and diluted loss per share	\$ (0.09)	\$ (0.09)	
Weighted average shares outstanding	37,016,763	34,810,099	

See accompanying notes to condensed consolidated financial statements

**VIRNETX HOLDING CORPORATION**  
**(a development stage enterprise)**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

	<u>Three Months Ended</u> <u>March 31, 2009</u>	<u>Three Months Ended</u> <u>March 31, 2008</u>	<u>Cumulative Period</u> <u>from</u> <u>August 2, 2005</u> <u>(Date of Inception)</u> <u>to March 31, 2009</u>
Cash flows from operating activities:			
Net loss	\$ (3,403,008)	\$ (3,031,735)	\$ (26,451,169)
Adjustments to reconcile net loss to net cash used in operating activities:			
Stock-based compensation	683,784	613,848	5,196,833
Depreciation and amortization	15,670	3,967	110,591
Changes in assets and liabilities:			
Prepaid expenses and other assets	(5,502)	26,363	(305,998)
Accounts payable and accrued liabilities	454,018	535,644	2,123,559
Net cash used in operating activities	<u>(2,255,038)</u>	<u>(1,851,913)</u>	<u>(19,326,184)</u>
Cash flows from investing activities:			
Purchase of property and equipment	—	(6,538)	(43,671)
Cash acquired in acquisition	—	—	(20,767)
Net cash used in investing activities	<u>—</u>	<u>(6,538)</u>	<u>(64,438)</u>
Cash flows from financing activities:			
Issuance of notes payable	—	—	250,000
Repayment of notes payable	—	—	(250,000)
Proceeds from issuance of preferred stock, net of issuance costs	—	—	1,147,625
Proceeds from issuance of restricted stock units	—	—	2,180
Proceeds from advance from preferred stockholders	—	—	230,000
Proceeds from exercise of options	—	—	30,000
Proceeds from convertible debt	—	—	1,500,000
Payment of royalty obligation less imputed interest	(44,000)	(48,000)	(92,000)
Proceeds from sale of common stock, net	3,367,925	—	18,098,859
Net cash provided by (used in) financing activities	<u>3,323,925</u>	<u>(48,000)</u>	<u>20,916,664</u>
Net increase in cash and cash equivalents	1,068,887	(1,906,451)	1,526,042
Cash and cash equivalents, beginning of period	457,155	8,589,447	—
Cash and cash equivalents, end of period	<u>\$ 1,526,042</u>	<u>\$ 6,682,996</u>	<u>\$ 1,526,042</u>
Supplemental disclosure of cash flow information:			
Cash paid during the period for taxes	<u>\$ 2,173</u>	<u>\$ —</u>	<u>\$ 12,174</u>
Cash paid during the period for interest	<u>\$ 6,000</u>	<u>\$ —</u>	<u>\$ 53,252</u>
Supplemental disclosure of noncash investing and financing activities:			
Conversion of advance into preferred stock	\$ —	\$ —	\$ 230,000
Royalty obligation assumed to obtain intangible assets	\$ —	\$ —	\$ 252,000

See accompanying notes to condensed consolidated financial statements

**VIRNETX HOLDING CORPORATION**  
**(a development stage enterprise)**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**Note 1 — Basis of Presentation**

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) have been condensed or omitted. Results of operations for the interim periods presented are not necessarily indicative of results which may be expected for any other interim period or for the year as a whole. The accompanying unaudited interim financial statements include all adjustments (consisting of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation. The information contained in this quarterly report on Form 10-Q should be read in conjunction with the audited financial statements and related notes for the year ended December 31, 2008 which are contained in our Annual Report on Form 10-K filed with the Securities and Exchange Commission (“SEC”), on March 31, 2009.

These financial statements are prepared on a going concern basis that contemplates the realization of assets and discharge of liabilities in the normal course of business. We have incurred net operating losses and negative cash flows from operations. At March 31, 2009, we had a deficit accumulated in the development stage of \$26,451,169. Management believes that the first half of 2009 average monthly cash requirement to fund our business is unlikely to change materially from our 2009 first quarter cash flow rate. As a result, we anticipate that our cash balance at March 31, 2009 will be insufficient to fund our operations for longer than through the end of our second quarter of 2009. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern.

**Note 2 — Formation and Business of the Company**

VirnetX Holding Corporation, a Delaware corporation (“we,” “us,” “our” or the “Company”) is a development stage company focused on commercializing a patent portfolio for providing solutions for secure real-time communications such as instant messaging (“IM”) and voice over internet protocol (“VoIP”).

In July 2007, we effected a merger between PASW, Inc., a company which had at the time of the merger, publicly traded common stock with limited operations, and VirnetX Inc., which became our principal operating subsidiary. As a result of this merger, the former securityholders of VirnetX Inc. came to own a majority of our outstanding common stock.

Under generally accepted accounting principles in the United States, the accompanying financial statements have been prepared as if VirnetX Inc., a company whose inception date was August 2, 2005 and who is our predecessor for accounting purposes, had acquired PASW, Inc. on July 5, 2007. Accordingly, the accompanying statement of operations include the operations of VirnetX Inc. from August 2, 2005 to March 31, 2009 and the operations of PASW, Inc. from July 5, 2007 to March 31, 2009. The historical share activity of VirnetX Inc. has been retroactively restated to account for the 12.454788-to-one exchange rate which was applicable to certain convertible instruments as explained in Note 10 and Note 11 to our Annual Report on Form 10-K for the year ended December 31, 2008 and for our one-for-three reverse stock split which was implemented on October 29, 2007.

Our principal business activities to date are our efforts to commercialize our patent portfolio. We also conduct the remaining activities of PASW, Inc., which are generally limited to the collection of royalties on certain internet-based communications through our wholly-owned Japanese subsidiary pursuant to the terms of a single license agreement. The revenue generated by this agreement is not significant.

Although we believe we may derive revenues in the future from our principal patent portfolio and are currently endeavoring to develop certain of those patents into marketable products, we have not done so to date. As such, we are in the development stage and consequently are subject to the risks associated with development stage companies, including the need for additional financings, the uncertainty that our licensing program development efforts will produce revenue-bearing licenses for us, the uncertainty that our development initiatives will produce successful commercial products as well as the uncertainty of marketing and customer acceptance of such products.



**Note 3 — Earnings Per Share**

SFAS No. 128 “Earnings Per Share” requires presentation of basic earnings per share and diluted earnings per share. Basic earnings per share are computed by dividing earnings available to common stockholders by the weighted average number of outstanding common shares during the period. Diluted earnings per share is computed by dividing net income by the weighted average number of shares outstanding including potentially dilutive securities such as options, warrants and convertible debt. Because we incurred a loss for each period presented, all such potentially dilutive securities have been excluded because their effect would be anti-dilutive.

**Note 4 — Patent Portfolio**

As of March 31, 2009, we had 12 issued U.S. technology related patents and eight issued foreign technology related patents. In addition, we have several pending U.S. and foreign patent applications. The expiration dates of our issued U.S. and foreign patents run from 2019 to 2024. Most of our issued patents were acquired by our principal operating subsidiary, VirnetX Inc., from Science Applications International Corporation (“SAIC”) pursuant to an Assignment Agreement dated December 21, 2006, and a Patent License and Assignment Agreement dated August 12, 2005, as amended on November 2, 2006, including documents prepared pursuant to the November amendment, and as further amended on March 12, 2008. We are required to make payments to SAIC based on the revenue generated from our ownership or use of the patents assigned to us by SAIC. Minimum annual royalty payments of \$50,000 are due beginning in 2008. Royalty amounts vary depending upon the type of revenue generating activities, and certain royalty categories are subject to maximums and other limitations. SAIC is entitled to receive a portion of the proceed revenues, monies or any form of consideration paid for the acquisition of VirnetX or from the settlement of certain patent infringement claims of ours. We have granted SAIC a security interest in some of our intellectual property, including the patents and patent applications we obtained from SAIC, to secure these payment obligations.

Generally upon our default of our agreement with SAIC and certain other events, we are required to convey to SAIC our interests in the patents and patent applications acquired from SAIC without consideration.

**Note 5 — Commitments**

We lease our office facility under a non-cancelable operating lease that was amended in 2008 and ends in 2012. We recognize rent expense on a straight-line basis over the term of the lease.

<b>For the Period</b>	<b>Minimum Required Lease Payments in Period</b>	
April 1 through December 31, 2009	\$	34,964
2010		54,595
2011		59,242
2012		30,202
	\$	<u>179,003</u>

**Note 6 — Stock Plan**

In 2005, VirnetX Inc. adopted the 2005 Stock Plan (the “Plan”), which was assumed by us upon the closing of the transaction between VirnetX Holding Corporation and VirnetX Inc. on July 5, 2007. Our Board of Directors renamed this Plan the VirnetX 2007 Stock Plan and our stockholders approved the Plan at our 2008 annual stockholders’ meeting. The Plan provides for the granting of stock options and restricted stock units to employees and consultants of ours. Stock options granted under the Plan may be incentive stock options or nonqualified stock options. Incentive stock options (“ISO”) may only be granted to our employees (including officers and directors). Nonqualified stock options (“NSO”) may be granted to our employees and consultants.

Options under the Plan may be granted for a period of up to ten years and at prices no less than 85% of the estimated fair market value of the shares on the date of grant as determined by the board of directors, provided, however, that the exercise price of an ISO and NSO shall not be less than 100% or 85% of the estimated fair market value of the shares at the date of grant, respectively, and the exercise price of an ISO and NSO granted to a 10% stockholder shall not be less than 110% of the estimated fair value of the shares on the date of grant.

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There were 4,468,595 options outstanding at March 31, 2009 and 4,468,595 at December 31, 2008 with an average exercise price of \$2.98 at March 31, 2009 and \$2.98 at December 31, 2008. As of March 31, 2009, there were 2,651,392 shares available to be granted under the Plan.

During the period January 1, 2009 through March 31, 2009, no options were exercised.

On April 3, 2009 there were 1,287,195 options granted to employees at a strike price of \$1.15. As of April 3, 2009 there were 5,755,790 options outstanding with an average exercise price of \$2.57. There are 1,364,197 shares available to be granted under the plan as of April 3, 2009.

### **Note 7 — Stock-Based Compensation**

We account for equity instruments issued to employees in accordance with the provision of Statement of Financial Accounting Standards (“SFAS”) 123(R) (“SFAS 123(R)”), which requires that such issuances be recorded at their fair value on the grant date. The recognition of the expense is subject to periodic adjustment as the underlying equity instruments vest.

We have elected to adopt the modified retrospective application method as provided by SFAS 123(R) and, accordingly, financial statement amounts for the periods presented herein reflect results as if the fair value method of expensing equity awards had been applied from inception.

Stock-based compensation expense is included in general and administrative expense for each period ended March 31, 2009. Total stock-based compensation expense was \$683,784 and \$613,848 for the three months ended March 31, 2009 and 2008, respectively.

As of March 31, 2009, the deferred stock-based compensation related to unvested stock options was \$6,693,045, which will be amortized as an expense over the related vesting period. As of March 31, 2009, the weighted average vesting period was approximately 2.25 years.

The fair value of option grants was estimated on the date of grant using the following assumptions:

	<b>Three Months Ended</b>	<b>Year Ended</b>
	<b>March 31, 2009</b>	<b>December 31, 2008</b>
Volatility	190.00%	190.00%
Risk-free interest rate	4.21%	4.21%
Expected life	6.1 years	6.7 years
Expected dividends	0.00%	0.00%
Weighted-average grant date fair value of stock options granted	\$ 2.98	\$ 3.09

The expected life was determined using the simplified method outlined in Staff Accounting Bulletin (“SAB”) 107 extended by SAB 110, using the average of the vesting term and the contractual term of the option. Expected volatility of the stock options was based upon historical data and other relevant factors, such as the volatility of comparable publicly-traded companies at a similar stage of life cycle. The Company has not provided an estimate for forfeitures because the Company has no history of forfeited options and believes that all outstanding options at March 31, 2009 will vest. In the future, the Company may change this estimate based on actual and expected future forfeiture rates.

**Note 8 — Warrants**

During 2007, we issued warrants to purchase 266,667 shares of our common stock at \$0.75 per share. The warrants expire in 2012. In 2008, these warrants were exercised in cashless exercise transactions, as a result of which a total of 232,771 shares of our common stock were issued.

During 2007, we issued warrants to purchase 300,000 shares of our common stock at \$4.80 per share to the underwriter of our December 2007 stock issuance. Those warrants expire in 2012.

In January 2009, we closed an underwritten public offering of 2,470,000 shares of our common stock. In addition to shares of common stock sold, we also issued warrants to the purchasers in the public offering to purchase 1,235,000 shares of our common stock at \$2.00 per share, warrants to purchase 1,235,000 shares of our common stock at \$3.00 per share, and warrants to purchase 1,235,000 shares of our common stock at \$4.00 per share.

Also in connection with the January 2009 offering, we issued a warrant to purchase 220,000 shares of our common stock at \$1.80 per share to the underwriter of that offering.

Copies of the forms of warrants issued to the purchasers and the underwriter of the January 2009 offering are filed as exhibits to this Quarterly Report on Form 10-Q.

**Note 9 — Litigation**

We believe Microsoft Corporation is infringing certain of our patents. Accordingly, we commenced a lawsuit against Microsoft on February 15, 2007 by filing a complaint in the United States District Court for the Eastern District of Texas, Tyler Division. Pursuant to the complaint, we allege that Microsoft infringes two of our U.S. patents: U.S. Patent No. 6,502,135 B1, entitled "Agile Network Protocol for Secure Communications with Assured System Availability," and U.S. Patent No. 6,839,759 B2, entitled "Method for Establishing Secure Communication Link Between Computers of Virtual Private Network Without User Entering Any Cryptographic Information." On April 5, 2007, we filed an amended complaint specifying certain accused products at issue and alleging infringement of a third, recently issued U.S. patent: U.S. Patent No. 7,188,180 B2, entitled "Method for Establishing Secure Communication Link Between Computers of Virtual Private Network." We are seeking both damages, in an amount subject to proof at trial, and injunctive relief. Microsoft answered the amended complaint and asserted counterclaims against us on May 4, 2007. Microsoft counterclaimed for declarations that the three patents are not infringed, are invalid and are unenforceable. Microsoft seeks an award of its attorneys' fees and costs. We filed a reply to Microsoft's counterclaims on May 24, 2007. Discovery has begun and the trial is scheduled to begin on October 12, 2009. We have served our infringement contentions directed to certain of Microsoft's operating system and unified messaging and collaboration applications. On March 31, 2008, Microsoft filed a Motion to Dismiss for lack of standing, which was denied by the court pursuant to an order dated June 3, 2008. Also pursuant to that court decision, on June 10, 2008, SAIC joined us in our lawsuit as a plaintiff. On November 19, 2008, the court granted our motion to amend our infringement contentions, permitting us to provide increased specificity and citations to Microsoft's proprietary documents and source code to support our infringement case against Microsoft's accused products, including, among other things, Windows XP, Vista, Server 2003, Server 2008, Live Communication Server, Office Communication Server and Office Communicator. Microsoft was ordered to provide further information regarding its non-infringement contentions and invalidity contentions in light of the amended infringement contentions. Microsoft was also ordered to provide additional e-mail discovery to us. On February 17, 2009, a Markman hearing on claim construction was conducted and we are currently awaiting the Court's order with respect to the hearing.

Although we believe Microsoft infringes three of our patents and we intend to vigorously prosecute this case, at this stage of the litigation the outcome cannot be predicted with any degree of reasonable certainty. Additionally, the Microsoft litigation will be costly and time-consuming, and we can provide no assurance that we will obtain a judgment against Microsoft for damages and/or injunctive relief. Should the District Court issue a judgment in favor of Microsoft, such judgment could be adverse to us.

Because the outcome of this litigation cannot be estimated at this time, we have made no provision for gain or expenses in the accompanying financial statements.

## ITEM 2 — MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

*This Quarterly Report on Form 10-Q, including this Management’s Discussion and Analysis of Financial Condition and Results of Operations contains “forward-looking” statements within the meaning of the Private Securities Litigation Reform Act of 1995, which provides a “safe harbor” for statements about future events, products and future financial performance that are based on the beliefs of, estimates made by and information currently available to our management. Except for the historical information contained herein, the outcome of the events described in these forward-looking statements is subject to risks and uncertainties. See “Risk Factors” for a discussion of these risks and uncertainties. The following discussion should be read in conjunction with and is qualified in its entirety by reference to our consolidated financial statements included elsewhere in this report. Actual results and the outcome or timing of certain events may differ significantly from those stated or implied by these forward-looking statements due to the factors listed under “Risk Factors,” and from time to time in our other filings with the Securities and Exchange Commission (“SEC”.) For this purpose, using the terms “believe,” “expect,” “expectation,” “anticipate,” “can,” “should,” “would,” “could,” “estimate,” “appear,” “based on,” “may,” “intended,” “potential,” “indicate,” “are emerging” and “possible” or similar statements are forward-looking statements that involve risks and uncertainties that could cause our actual results and the outcome and timing of certain events to differ materially from those stated or implied by these forward-looking statements. By making forward-looking statements, we have not assumed any obligation to, and you should not expect us to, update or revise those statements because of new information, future events or otherwise.*

*As used herein, “we,” “us,” “our,” or the “Company” means VirnetX Holding Corporation, together with its consolidated subsidiaries where applicable.*

### Company Overview

We are a development stage company focused on commercializing a patent portfolio for securing real-time communications over the Internet. These patents were acquired by our principal operating subsidiary, VirnetX Inc., from Science Applications International Corporation (“SAIC”.) SAIC is a FORTUNE 500® scientific, engineering, and technology applications company that uses its deep domain knowledge to solve problems of vital importance to the nation and the world, in national security, energy and the environment, critical infrastructure, and health.

In January 2009, we closed an underwritten public offering of 2,470,000 shares of our common stock, including 270,000 of which were issued pursuant to the underwriter’s over-allotment option, plus warrants to purchase 1,235,000 shares of common stock at \$2.00 per share, including 135,000 of which were issued pursuant to the underwriter’s over-allotment option, warrants to purchase 1,235,000 shares of common stock at \$3.00 per share, including 135,000 of which were issued pursuant to the underwriter’s over-allotment option, and warrants to purchase 1,235,000 shares of common stock at \$4.00 per share, including 135,000 of which were issued pursuant to the underwriter’s over-allotment option. The offering at \$1.50 per unit raised gross proceeds of approximately \$3,700,000 before deducting the underwriter’s fees and other costs of the offering. The net cash raised was approximately \$3,300,000.

In December 2007, we closed an underwritten public offering of 3.45 million shares of our common stock, raising gross proceeds of \$13.8 million before underwriting discounts and commissions and offering expenses. In connection with the 2007 offering, our common stock began trading on the American Stock Exchange under the ticker symbol “VHC.” After the acquisition of the American Stock Exchange by the New York Stock Exchange in 2008, our common stock now trades under the ticker symbol “VHC” on the NYSE Amex. Our principal business activities to date are our efforts to commercialize our patent portfolio. We also conduct the remaining activities of PASW, Inc., which are generally limited to the collection of royalties on certain Internet-based communications by a wholly-owned Japanese subsidiary of ours pursuant to the terms of a single license agreement. The revenue generated by this agreement is not significant.

Although we believe we may derive revenues in the future from our principal patent portfolio and are currently endeavoring to develop certain of those patents into marketable products, we have not done so to date. Because we have limited capital resources, our revenues are insignificant and our expenses, including but not limited to those we expect to incur in our patent infringement case against Microsoft, are substantial, we may be unable to successfully complete our business plans, our business may fail and your investment in our securities may become worthless. See “Risk Factors” for additional information.

We are in the development stage and consequently we are subject to the risks associated with development stage companies including: the need for additional financings; the uncertainty that our patent and technology licensing program development efforts will produce revenue bearing licenses for us; the uncertainty that our development initiatives will produce successful commercial products as well as the marketing and customer acceptance of such products; competition from larger organizations; dependence on key personnel; uncertain patent protection; and dependence on corporate partners and collaborators. To achieve successful operations, we will require additional capital to continue research and development and marketing efforts. No assurance can be given as to the timing or ultimate success of obtaining future funding.

#### **Recent Developments in the Three Months Ended March 31, 2009**

On January 30, 2009, we closed an underwritten public offering of 2,470,000 shares of our common stock at \$1.50 per share. As further described in the prospectus for the offering filed on SEC's EDGAR filing website, [www.sec.gov](http://www.sec.gov), for each share purchased in the offering, an investor received registered warrants to purchase 0.5 shares of our common stock at \$2.00 per share, 0.5 shares of our common stock at \$3.00 per share and 0.5 shares of our common stock at \$4.00 per share.

On February 10, 2009, VirnetX Inc., our wholly-owned subsidiary, was awarded U.S. patent number 7,490,151 by the United States Patent and Trademark Office. The new patent, titled "Establishment of a secure communication link based on a domain name service (DNS) request" describes a secure mechanism for communication over the Internet. In conjunction with the issuance of this patent, we will seek to commercialize these exclusive rights in the United States by establishing the secure domain name registry service for the Internet. Additional information about the patent can be found at the Internet website [www.uspto.gov](http://www.uspto.gov).

On February 19, 2009, the Markman hearing on claim construction was conducted in connection with the Microsoft litigation and we are currently awaiting the Court's order with respect to the hearing.

On March 13, 2009, the common stock warrants issued in connection with our public offering that closed on January 30, 2009 were approved for listing on the OTC Bulletin Board under the symbols VHCOW, VHCOZ and VHCOL.

#### **Application of Critical Accounting Policies**

There were no material changes in the application of the Company's critical accounting policies since the end of the most recent fiscal year. For further information, see the "Critical Accounting Policies" section of Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," in our Annual Report on Form 10-K for the year ended December 31, 2008, filed with the SEC on March 31, 2009.

#### **Recent Accounting Pronouncements**

There were no material updates to recent accounting pronouncements since the end of the most recent fiscal year. For further information, see the "Recent Accounting Pronouncements" section of Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," in our Annual Report on Form 10-K for the year ended December 31, 2008, filed with the SEC on March 31, 2009.

## Results of Operations

### Three Months Ended March 31, 2009 Compared with Three Months Ended March 31, 2008

#### *Revenue — Royalties*

Revenue generated decreased to \$3,154 for the three months ended March 31, 2009 from \$33,306 for the three months ended March 31, 2008. Our revenue in 2009 was solely limited to the royalties earned under our single license agreement through our Japanese subsidiary. We expect the revenue from this license to decrease substantially in the future. We do not intend to seek additional licenses or other revenue through our Japanese subsidiary.

#### *Research and Development Expenses*

Research and development costs include expenses paid to outside development consultants and compensation related expenses for our engineering staff. Research and development costs are expensed as incurred.

Our research and development expenses increased by \$43,985 to \$221,699 for the three months ended March 31, 2009, from \$177,714 for the three months ended March 31, 2008. This increase is primarily due to increased engineering activities for product development and the addition of one engineer. We expect research and development expenses to increase as employees are hired to provide in-house research and development. While we expect to use outside contractors for additional product development on a limited basis, we expect those costs to remain level or decline.

#### *Selling, General and Administrative Expenses*

Selling, general and administrative expenses include management and administrative personnel, as well as outside legal, accounting, and consulting services.

Our selling, general and administrative expenses increased by \$228,782 to \$3,186,690 for the three months ended March 31, 2009 from \$2,957,908 for the three month period ended March 31, 2008.

Within selling, general and administrative expenses, legal fees increased by \$158,737 to \$1,772,583 for the three months ended March 31, 2009 from \$1,613,846 for the three months ended March 31, 2008. The increase in fees incurred was due primarily to our patent infringement litigation against Microsoft and preparation of annual meeting and proxy statement.

In addition, during the three months ended March 31, 2009, we made our second minimum annual royalty payment of \$50,000 to SAIC pursuant to the patent license and assignment agreement, as amended, by and between VirnetX and SAIC. As of March 31, 2009, we had not received any royalty revenue on the patents.

Also within selling, general and administrative expenses, expenses increased by \$70,045 for the three months ended March 31, 2009. The increase was due principally to an increase in rent over the same period in 2008 and the number of staff and resources in order to comply with the requirements associated with being an SEC reporting company.

Once we begin to generate royalty revenues, we expect that our selling expenses will increase significantly as we must make payments to ipCapital Group and SAIC with respect to such revenues and as we begin to expand our sales force.

## **Liquidity and Capital Resources**

We are in the development stage and have raised capital since our inception through the issuance of our equity securities. As of March 31, 2009, we had approximately \$1,526,000 in cash. We expect to finance future cash needs primarily through proceeds from equity or debt financings, loans, and/or collaborative agreements with corporate partners. We have used the net proceeds from the sale of common and preferred stock for general corporate purposes, which have included funding research and development, litigation efforts and working capital needs.

We anticipate that our existing cash and cash equivalents are insufficient to fund our operations for longer than through the end of our second quarter of 2009. In order to obtain additional capital, we expect to evaluate alternative financing sources, including, but not limited to, the issuance of equity or debt securities, corporate alliances, joint ventures and licensing agreements; however, there can be no assurance that funding will be available on favorable terms, if at all. We cannot assure you that we will successfully commercialize our products and services or that our products and services will gain sufficient market acceptance to enable us to earn a profit. If we are unable to obtain additional capital or generate sufficient revenue from such efforts, we may be required to cease operations or to reduce cash used in our business, including the termination of commercialization efforts that may appear to be promising, the sale of our patent portfolio or other assets, the abandonment of our litigation with Microsoft or others and the reduction in overall operating activities.

During fiscal year 2008, the cash flow for our operations was approximately \$8,064,000 (an average of approximately \$672,000 per month.) During the first quarter of 2009, our cash used in operating activities averaged \$751,679 per month. We believe that, for the first half of 2009, our average monthly cash requirement to fund our operations is unlikely to change materially from our 2009 first quarter cash flow rate. As a result, we anticipate that our cash balance at March 31, 2009 of \$1,526,000 will be insufficient to fund our operations for longer than through the end of our second quarter of 2009. We anticipate that our monthly cash requirements will increase for the second half of 2009 as we increase our expenditures for:

- our lawsuit against Microsoft;
- infrastructure;
- sales and marketing;
- research and development;
- personnel; and
- general business enhancements.

We may exceed those projected amounts if we increase these expenditures in response to business conditions we do not currently expect or for other reasons. The process of developing new security solutions is inherently complex, time-consuming, expensive and uncertain. We must make long-term investments and commit significant resources before knowing whether our patented technology offerings will achieve market acceptance. We are unable to predict when we will begin to generate material net cash inflows from our patent and technology licensing program and our secure domain name registry service.

### **Off-Balance Sheet Arrangements**

As of March 31, 2009, we did not have any off-balance sheet arrangements except for operating lease commitments and the contingent portion of our royalty obligation under our royalty agreement with SAIC as discussed in Note 5 "Commitments" and Note 6 "Patent Portfolio" to the financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2008.

### **ITEM 3 — QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

Not Applicable.



**ITEM 4 — CONTROLS AND PROCEDURES.**

(a) *Disclosure controls and procedures.* Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such items are defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (“Exchange Act”)) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures as of the end of the period covered by this Quarterly Report are effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms.

(b) *Changes in internal control over financial reporting.* There was no change in our internal control over financial reporting during the quarter ended March 31, 2009 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II — OTHER INFORMATION**

**ITEM 1 — LEGAL PROCEEDINGS.**

We believe Microsoft Corporation is infringing certain of our patents. Accordingly, we commenced a lawsuit against Microsoft on February 15, 2007 by filing a complaint in the United States District Court of the Eastern District of Texas, Tyler Division. Pursuant to the complaint, we allege that Microsoft infringes two of our U.S. patents: U.S. Patent No. 6,502,135 B1, entitled “Agile Network Protocol for Secure Communications with Assured System Availability,” and U.S. Patent No. 6,839,759 B2, entitled “Method for Establishing Secure Communication Link Between Computers of Virtual Private Network Without User Entering Any Cryptographic Information.” On April 5, 2007, we filed an amended complaint specifying certain accused products at issue and alleging infringement of a third, recently issued U.S. patent: U.S. Patent No. 7,188,180 B2, entitled “Method for Establishing Secure Communication Link Between Computers of Virtual Private Network.” We are seeking both damages, in an amount subject to proof at trial, and injunctive relief. Microsoft answered the amended complaint and asserted counterclaims against us on May 4, 2007. Microsoft counterclaimed for declarations that the three patents are not infringed, are invalid and are unenforceable. Microsoft seeks an award of its attorneys’ fees and costs. We filed a reply to Microsoft’s counterclaims on May 24, 2007. We have served our infringement contentions directed to certain of Microsoft’s operating system and unified messaging and collaboration applications. On March 31, 2008, Microsoft filed a Motion to Dismiss for lack of standing, which was denied by the court pursuant to an order dated June 3, 2008. Also pursuant to that court decision, on June 10, 2008, SAIC joined us in our lawsuit as a plaintiff. On November 19, 2008, the court granted our motion to amend our infringement contentions, permitting us to provide increased specificity and citations to Microsoft’s proprietary documents and source code to support our infringement case against Microsoft’s accused products, including, among other things, Windows XP, Vista, Server 2003, Server 2008, Live Communication Server, Office Communication Server and Office Communicator. Microsoft was ordered to provide further information regarding its non-infringement contentions and invalidity contentions in light of the amended infringement contentions. Microsoft was also ordered to provide additional e-mail discovery to us. Discovery has begun, a Markman hearing on claim construction was conducted on February 17, 2009, and we are currently awaiting the Court’s order with respect to the hearing. The trial is scheduled to begin on October 12, 2009.

Notwithstanding anything to the contrary set forth in any of the Company’s filings under the Securities Act of 1933 or the Securities Exchange Act of 1934 that might incorporate future filings, the information set forth on the Public Access to Court Electronic Records (“PACER”) website shall not be deemed to be a part of or incorporated by reference into any such filings. The Company does not warrant the accuracy or completeness of the PACER website, or the adequacy of the PACER website and expressly disclaims liability for errors or omissions on such website.

Because we have determined that Microsoft’s alleged unauthorized use of our patents would cause us severe economic harm and the failure to cause Microsoft to discontinue its use of such patents could result in the termination of our business, we have dedicated a significant portion of our economic resources, to date, to the prosecution of the Microsoft litigation and expect to continue to do so for the foreseeable future.



Although we believe Microsoft infringes three of our patents and we intend to vigorously prosecute this case, at this stage of the litigation the outcome cannot be predicted with any degree of reasonable certainty. Additionally, the Microsoft litigation will be costly and time-consuming, and we can provide no assurance that we will obtain a judgment against Microsoft for damages and/or injunctive relief. Should the District Court issue a judgment in favor of Microsoft, such judgment could be adverse to us.

In the near term, we will dedicate significant time and resources to the Microsoft litigation. The risks associated with such dedication of time and resources are set forth in the “Risk Factors” section of this Quarterly Report on Form 10-Q.

One or more potential intellectual property infringement claims may also be available to us against certain other companies who have the resources to defend against any such claims. Although we believe these potential claims are worth pursuing, commencing a lawsuit can be expensive and time-consuming, and there is no assurance that we will prevail on such potential claims. In addition, bringing a lawsuit may lead to potential counterclaims which may preclude our ability to commercialize our initial products, which are currently in development.

Currently, we are not a party to any other pending legal proceedings, and are not aware of any proceeding threatened or contemplated against us by any governmental authority or other party.

#### **ITEM 1A — RISK FACTORS.**

You should carefully consider the following material risks in addition to the other information set forth in this Quarterly Report on Form 10-Q before making any investment in the offered securities. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently believe to be immaterial may also adversely affect our business. If any of these risk factors occurs, you could lose substantial value or your entire investment in the offered securities.

##### **Risks Related To Existing and Future Litigation**

***We have commenced legal proceedings against Microsoft, and we expect such litigation to be time-consuming and costly, which may adversely affect our financial condition and our ability to operate our business.***

On February 15, 2007, we initiated a lawsuit by filing a complaint against Microsoft in the United States District Court for the Eastern District of Texas, Tyler Division, pursuant to which we allege that Microsoft infringes two of our patents regarding the creation of virtual private networks (“VPNs”.) We seek damages and injunctive relief. On April 5, 2007, we filed an amended complaint, pursuant to which we allege that Microsoft infringes a third patent. On February 17, 2009, a Markman hearing on claim construction was conducted and the parties are currently awaiting the Court’s order with respect to the hearing. We anticipate that these legal proceedings may continue for several years and may require significant expenditures for legal fees and other expenses. The time and effort required of our management to effectively pursue the Microsoft lawsuit may adversely affect our ability to operate our business, since time spent on matters related to the lawsuit will take away from the time spent on managing and operating our business. Microsoft has counterclaimed for declarations that the three patents are not infringed, are invalid and are unenforceable. If Microsoft’s counterclaims are successful, they may preclude our ability to commercialize our initial products. Additionally, we anticipate that our legal fees will be material and will negatively impact our financial condition and results of operations and may result in our inability to continue our business.

***While we believe Microsoft infringes our patents, we can provide no assurance that we will be successful in our lawsuit.***

We believe that Microsoft infringes on three of our patents, but obtaining and collecting a judgment against Microsoft may be difficult or impossible. Patent litigation is inherently risky and the outcome is uncertain. Microsoft is a large, well-financed company with substantially greater resources than us. We believe that Microsoft will devote a substantial amount of resources in an attempt to prove that either their products do not infringe our patents or that our patents are not valid and are unenforceable. At this time, we cannot predict the outcome of this litigation.

***We are devoting a substantial amount of our financial and management resources to the Microsoft litigation, and if we are unsuccessful in this lawsuit, our financial condition may be adversely affected and we may not survive.***

Currently, we are devoting substantial time, effort and financial resources to our lawsuit against Microsoft. We are a development stage company with no finished product, and, although our business strategy is focused primarily on bringing patented products to market, our business strategy also depends greatly on obtaining a judgment in our favor from the courts and collecting such judgment before our financial resources are depleted. In the event we are not awarded and do not subsequently obtain monetary and injunctive relief, we may not have enough financial resources to continue our operations.

***The burdens of being a public company may adversely affect our ability to pursue the Microsoft litigation.***

As a public company, our management must devote substantial time, attention and financial resources to comply with U.S. securities laws. This may have a material adverse affect on management's ability to effectively pursue the Microsoft litigation as well as our other business initiatives. In addition, our disclosure obligations under U.S. securities laws require us to disclose information publicly that will be available to Microsoft as well as any other future litigation opponents. We may, from time to time, be required to disclose information that will have a material adverse affect on our litigation strategies. This information may enable our litigation opponents to develop effective litigation strategies that are contrary to our interests.

***We may commence additional legal proceedings against third parties who we believe are infringing on our intellectual property rights, and if we are forced to litigate to defend our intellectual property rights, or to defend claims by third parties against us relating to intellectual property rights, legal fees and court injunctions could adversely affect our financial condition or end our business.***

Disputes regarding the ownership of technologies and intellectual property rights are common and we may have intellectual property infringement claims against other parties in addition to our claims against Microsoft. If we decide to commence actions against any additional parties, doing so may be expensive and time-consuming, which may adversely affect our financial condition and results of operations. Moreover, there can be no assurance that we would be successful in these additional legal proceedings and the existence and outcome of any such litigation could harm our business. In addition, commencing lawsuits may lead to potential counterclaims which may preclude our ability to develop and commercialize our initial products.

#### **Risks Related to Our Business and Our Industry**

***We are a development stage company with virtually no revenues.***

We are a development stage company with a very small amount of revenue and do not expect to generate additional revenues unless and until our patent portfolio, or part of it, is commercialized. We anticipate that our existing cash and cash equivalents are insufficient to fund our operations for longer than through the end of our second quarter of 2009. We need to raise additional capital to fund our operations and our litigation against Microsoft and there can be no assurance that we will be successful in doing so on acceptable terms or at all. Our inability to generate sufficient cash flow or raise other funds to meet our expenses, obligations and sustain our operations raises substantial doubt about our ability to continue as a going concern. See the "Liquidity and Capital Resources" section in this Quarterly Report on Form 10-Q for additional information.

***We anticipate incurring operating losses and negative cash flows for the foreseeable future resulting in uncertainty of future profitability and limitations on our operations.***

We anticipate that we will incur operating losses and negative cash flows in the foreseeable future, and we will accumulate increasing deficits as we increase our expenditures for:

- our lawsuit against Microsoft;
- infrastructure;
- sales and marketing;
- research and development;
- personnel; and
- general business enhancements.

We need to significantly increase our revenue if we are to attain profitability and there is no assurance that we will be able to do so. As discussed in the notes to the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q, in the event that we are unable to achieve profitability or raise sufficient funding to cover our losses in the near term, we will be unable to meet our expenses and obligations as they come due, and this raises substantial doubts as to our ability to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

***Our business plan for commercializing our patents and technology is new and unproven, and therefore we can provide no assurance that we will be successful in pursuing it.***

We intend to develop products to provide a security platform for real-time communications; however, this is not a defined market. We expect to depend on our intellectual property licensing fees for the majority of our revenues. Our ability to generate licensing fees is highly dependent on mainstream market adoption of real-time communications based on SIP or using DNS lookup protocols as well as customer adoption of our GABRIEL Communication Technology™ and our secure domain name registry. We cannot assure you that customers will adopt our products and services, or that we will succeed in building a profitable business based on our business plan.

***We may or may not be able to capitalize on potential market opportunities related to our licensing strategy or our patent portfolio.***

Our business strategy calls for us to enter into licensing relationships with the leading companies in our target market in order to reach a larger end-user base than we could reach through direct sales and marketing efforts. We have engaged ipCapital Group to help develop our licensing strategy and to introduce the Company to five potential strategic licensees of the Company's technology. In connection with this engagement, we agreed to pay ipCapital Group 10% of the royalties of each resulting licensing arrangement, up to an aggregate maximum of \$2 million per licensee, or \$10 million in the aggregate. There can be no assurance that we will be able to capitalize on the potential market opportunity. Our inability to generate licensing revenues associated with the potential market opportunity could result from a number of factors, including, but not limited to:

- our capital resources may be insufficient;
- our management team may not have sufficient bandwidth to successfully capitalize on all of the opportunities identified by ipCapital Group;
- we may not be successful in entering into licensing relationships with our targeted customers on commercially acceptable terms; and
- the validity of our patents underlying the licensing opportunity is currently being challenged in our litigation against Microsoft.

***Our business greatly depends on the growth of IM, VoIP, mobile services, streaming video, file transfer and remote desktop and other next-generation Internet-based applications.***

We cannot assure you that next-generation Internet-based applications such as instant messaging (“IM”), voice over Internet protocol (“VoIP”), mobile services, streaming video, file transfer and remote desktop will continue to gain widespread market acceptance. The Internet may ultimately prove not to be a viable commercial marketplace for such applications for a number of reasons, including:

- unwillingness of consumers to shift to VoIP and use other such next-generation Internet-based applications;
- refusal to purchase security products to secure information transmitted through such applications;
- perception by the licensees of unsecure communication and data transfer;
- lack of concern for privacy by licensees and users;
- limitations on access and ease of use;
- congestion leading to delayed or extended response times;
- inadequate development of Internet infrastructure to keep pace with increased levels of use; and
- increased government regulations.

***If the market for IM, VoIP, mobile services, streaming video, file transfer and remote desktop does not grow as anticipated, our business would be adversely affected.***

The success of our products that secure IM, VoIP, mobile services, streaming video, file transfer and remote desktop, among other real-time communications applications, depends on the growth in the number of users, which in turn depends on the Internet gaining more widespread acceptance as the basis for these real-time communications applications. These real-time communications applications are still in early stages of market acceptance and we cannot assure you that they will continue to develop a broader audience. For example, potential new users may view VoIP as unattractive relative to traditional telephone services for a number of reasons, including the need to purchase computer headsets or the perception that the price advantage for VoIP is insufficient to justify the perceived inconvenience.

***While the use of IM and other next-generation Internet-based applications has grown rapidly in personal and professional use, there can be no assurance that users will pay to secure their use of such applications.***

Many services such as Microsoft, Yahoo! and America Online offer IM free of charge. However, security solutions for these services are not free, and OEMs may not want to adopt such security solutions if users of IM do not see the value and do not want to pay for such security solutions. If personal and professional users of IM and other next-generation Internet-based solutions do not want to pay for the security solutions, we will have difficulty marketing and selling our products and technologies.

***We expect that we will experience long and unpredictable sales cycles, which may impact our quarterly operating results.***

We expect that our sales cycles will be long and unpredictable due to a number of uncertainties such as:

- the need to educate potential customers about our patent rights and our product and service capabilities;
- customers’ willingness to invest potentially substantial resources and modify their network infrastructures to take advantage of our products;
- customers’ budgetary constraints;
- the timing of customers’ budget cycles; and
- delays caused by customers’ internal review processes.

***We expect that we will be substantially dependent on a concentrated number of customers. If we are unable to establish, maintain or replace our relationships with customers and develop a diversified customer base, our revenues may fluctuate and our growth may be limited.***

We expect that for the foreseeable future, a significant portion of our revenues will be generated from a limited number of customers. There can be no guarantee that we will be able to obtain such customers, or if we do so, to sustain our revenue levels from these customers. If we cannot establish, maintain or replace the limited group of customers that we anticipate will generate a substantial majority of revenues, or if they do not generate revenues at the levels or at the times that we anticipate, our ability to maintain or grow our revenues will be adversely affected.

***If we do not successfully develop our planned products and services in a cost-effective manner to customer demand in the rapidly evolving market for Internet and IP-based communications services, our business may fail.***

The market for communications services is characterized by rapidly changing technology, evolving industry standards, changes in customer needs and frequent new service and product introductions. We are currently focused on developing products to provide security solutions for real-time communications. Our future success will depend, in part, on our ability to use new technologies effectively, to continue to develop our technical expertise, to enhance our existing services and to develop new services that meet changing customer needs on a timely and cost-effective basis. We may not be able to adapt quickly enough to changing technology, customer requirements and industry standards. If we fail to use new technologies effectively, to develop our technical expertise and new services, or to enhance existing services on a timely basis, either internally or through arrangements with third parties, our product and service offerings may fail to meet customer needs, which would adversely affect our revenues and prospects for growth.

In addition, if we are unable, for technological, legal, financial or other reasons, to adapt in a timely manner to changing market conditions or customer requirements, we could lose customers, strategic alliances and market share. Sudden changes in user and customer requirements and preferences, the frequent introduction of new products and services embodying new technologies and the emergence of new industry standards and practices could render our existing products, services and systems obsolete. The emerging nature of products and services in the technology and communications industry and their rapid evolution will require that we continually improve the performance, features and reliability of our products and services. Our success will depend, in part, on our ability to:

- design, develop, launch and/or license our planned products, services and technologies that address the increasingly sophisticated and varied needs of our prospective customers; and
- respond to technological advances and emerging industry standards and practices on a cost-effective and timely basis.

The development of our planned products and services and other patented technology involves significant technological and business risks and requires substantial expenditures and lead time. We may be unable to use new technologies effectively. Updating our technology internally and licensing new technology from third-parties may also require us to incur significant additional expenditures.

***If our products do not gain market acceptance, we may not be able to fund future operations.***

A number of factors may affect the market acceptance of our planned products or any other products we develop or acquire, including, among others:

- the price of our products relative to other products that seek to secure real-time communication;
- the perception by users of the effectiveness of our products;
- our ability to fund our sales and marketing efforts; and
- the effectiveness of our sales and marketing efforts.

If our products do not gain market acceptance, we may not be able to fund future operations, including the development of new products and/or our sales and marketing efforts for our current products, which inability would have a material adverse effect on our business, financial condition and operating results.

***Our products are highly technical and may contain undetected errors, which could cause harm to our reputation and adversely affect our business.***

Our products are highly technical and complex and, when deployed, may contain errors or defects. In addition, we rely on third parties for software development and technology services, and there may be errors in the development processes used by our third party counterparts that may adversely affect our end products. Despite testing, some errors in our products may only be discovered after a product has been installed and used by customers. Any errors or defects discovered in our products after commercial release could result in failure to achieve market acceptance, loss of revenue or delay in revenue recognition, loss of customers and increased service and warranty cost, any of which could adversely affect our business, operating results and financial condition. In addition, we could face claims for product liability, tort or breach of warranty, including claims relating to changes to our products made by our channel partners. The performance of our products could have unforeseen or unknown adverse effects on the networks over which they are delivered as well as on third-party applications and services that utilize our services, which could result in legal claims against us, harming our business. Furthermore, we expect to provide implementation, consulting and other technical services in connection with the implementation and ongoing maintenance of our products, which typically involves working with sophisticated software, computing and communications systems. We expect that our contracts with customers will contain provisions relating to warranty disclaimers and liability limitations, which may not be upheld. Defending a lawsuit, regardless of its merit, is costly and may divert management's attention and adversely affect the market's perception of us and our products. In addition, if our business liability insurance coverage proves inadequate or future coverage is unavailable on acceptable terms or at all, our business, operating results and financial condition could be adversely impacted.

***Malfunctions of third-party communications infrastructure, hardware and software exposes us to a variety of risks we cannot control.***

In addition, our business will also depend upon the capacity, reliability and security of the infrastructure owned by third parties that we will use to deploy our offerings. We have no control over the operation, quality or maintenance of a significant portion of that infrastructure or whether or not those third parties will upgrade or improve their equipment. We depend on these companies to maintain the operational integrity of our connections. If one or more of these companies is unable or unwilling to supply or expand its levels of service to us in the future, our operations could be severely interrupted. Also, to the extent the number of users of networks utilizing our future products suddenly increases, the technology platform and secure hosting services which will be required to accommodate a higher volume of traffic may result in slower response times or service interruptions. System interruptions or increases in response time could result in a loss of potential or existing users and, if sustained or repeated, could reduce the appeal of the networks to users. In addition, users depend on real-time communications; outages caused by increased traffic could result in delays and system failures. These types of occurrences could cause users to perceive that our solution does not function properly and could therefore adversely affect our ability to attract and retain licensees, strategic partners and customers.

***System failure or interruption or our failure to meet increasing demands on our systems could harm our business.***

The success of our license and service offerings will depend on the uninterrupted operation of various systems, secure data centers and other computer and communication networks that we establish. To the extent the number of users of networks utilizing our future products suddenly increases, the technology platform and hosting services which will be required to accommodate a higher volume of traffic may result in slower response times, service interruptions or delays or system failures. Our systems and operations will also be vulnerable to damage or interruption from:

- power loss, transmission cable cuts and other telecommunications failures;
- damage or interruption caused by fire, earthquake, and other natural disasters;
- computer viruses or software defects; and
- physical or electronic break-ins, sabotage, intentional acts of vandalism, terrorist attacks and other events beyond our control.

System interruptions or failures and increases or delays in response time could result in a loss of potential or existing users and, if sustained or repeated, could reduce the appeal of the networks to users. These types of occurrences could cause users to perceive that our solution does not function properly and could therefore adversely affect our ability to attract and retain licensees, strategic partners and customers.

Any significant problem with our systems or operations could result in lost revenue, customer dissatisfaction or lawsuits against us. A failure in the operation of our secure domain name registration system could result in the inability of one or more registrars to register and maintain secure domain names for a period of time. A failure in the operation or update of the master directory that we plan to maintain could result in deletion or discontinuation of assigned secure domain names for a period of time. The inability of the registrar systems we establish, including our back office billing and collections infrastructure, and telecommunications systems to meet the demands of an increasing number of secure domain name requests could result in substantial degradation in our customer support service and our ability to process registration requests in a timely manner.

***If we experience security breaches, we could be exposed to liability and our reputation and business could suffer.***

We will retain certain confidential customer information in our secure data centers and secure domain name registry. It will be critical to our business strategy that our facilities and infrastructure remain secure and are perceived by the marketplace to be secure. Our secure domain name registry operations will also depend on our ability to maintain our computer and telecommunications equipment in effective working order and to reasonably protect our systems against interruption, and potentially depend on protection by other registrars in the shared registration system. The secure domain name servers that we will operate will be critical hardware to our registry services operations. Therefore, we expect to have to expend significant time and money to maintain or increase the security of our facilities and infrastructure.

Security technologies are constantly being tested by computer professionals, academics and “hackers.” Advances in the techniques for attacking security solutions could make some or all of our products obsolete or unmarketable. Likewise, if any of our products are found to have significant security vulnerabilities, then we may need to dedicate engineering and other resources to eliminate the vulnerabilities and to repair or replace products already sold or licensed to our customers. Despite our security measures, our infrastructure may be vulnerable to physical break-ins, computer viruses, attacks by hackers or similar disruptive problems. It is possible that we may have to expend additional financial and other resources to address such problems. Any physical or electronic break-in or other security breach or compromise of the information stored at our secure data centers and domain name registration systems may jeopardize the security of information stored on our premises or in the computer systems and networks of our customers. In such an event, we could face significant liability and customers could be reluctant to use our services. Such an occurrence could also result in adverse publicity and therefore adversely affect the market’s perception of the security of electronic commerce and communications over IP networks as well as of the security or reliability of our services.

***We may incur significant expenses and damages because of liability claims.***

An actual or perceived breach of our security solutions could result in a product liability claim against us. A substantial product liability claim against us could harm our operating results and financial condition. In addition, any actual or perceived breach of our security solution, whether or not caused by the failure of one of our products, could hurt our reputation and cause potential customers to turn to our competitors’ products.

***Our ability to sell our solutions will be dependent on the quality of our technical support, and our failure to deliver high-quality technical support services could have a material adverse effect on our sales and results of operations.***

If we do not effectively assist our customers in deploying our products, succeed in helping our customers quickly resolve post-deployment issues and provide effective ongoing support, or if potential customers perceive that we may not be able achieve to the foregoing, our ability to sell our products would be adversely affected, and our reputation with potential customers could be harmed. In addition, as we expand our operations internationally, our technical support team will face additional challenges, including those associated with delivering support, training and documentation in languages other than English. As a result, our failure to deliver and maintain high-quality technical support services to our customers could result in customers choosing to use our competitors' products instead of ours in the future.

***There has been increased competition for security solutions in the real-time communications industry, as more companies seek to provide products and services similar to our proposed products and services, and because larger and better-financed competitors may affect our ability to operate our business and achieve profitability, our business may fail.***

We expect competition for our products and services to be intense. We expect to compete directly against other companies offering similar security products and services that will compete directly with our proposed products and services. We also expect that we will compete against established vendors within the IP-telephony, mobility, fixed-mobile convergence and unified communications markets. These companies may incorporate other competitive technologies into their product offerings, whether developed internally or by third parties. For the foreseeable future, substantially all of our competitors are likely to be larger, better-financed companies that may develop products superior to our proposed products, which could create significant competitive advantages for those companies. Our future success depends on our ability to compete effectively with our competitors. As a result, we may have difficulty competing with larger, established competitor companies. Generally, these competitors have:

- substantially greater financial, technical and marketing resources;
- a larger customer base;
- better name recognition; and
- more expansive product offerings.

These competitors are likely to command a larger market share than us, which may enable them to establish a stronger competitive position, in part, through greater marketing opportunities. Further, our competitors may be able to respond more quickly to new or emerging technologies and changes in user preferences and to devote greater resources to developing and operating networks of affinity websites. These competitors may develop products or services that are comparable or superior. If we fail to address competitive developments quickly and effectively, we may not be able to remain a viable entity.

***If we are not able to adequately protect our patented rights, our operations would be negatively impacted.***

Our ability to compete largely depends on the superiority, uniqueness and value of our technology and intellectual property. To protect our intellectual property rights, we rely on a combination of patent, trademark, copyright and trade secret laws, confidentiality agreements with our employees and third parties, and protective contractual provisions. Further, we can give no assurances that infringement or invalidity claims (or claims for indemnification resulting from infringement claims) will not be asserted or prosecuted against us or that any such assertions or prosecutions will not materially adversely affect our business. Regardless of whether any such claims are valid or can be successfully asserted, defending against such claims could cause us to incur significant costs and could divert resources away from our other activities. In addition, assertion of infringement claims could result in injunctions that prevent us from distributing our products. Despite these efforts, any of the following may reduce the value of our intellectual property:

- our applications for patents, trademarks and copyrights relating to our business may not be granted and, if granted, may be challenged or invalidated;
- issued trademarks, copyrights, or patents may not provide us with any competitive advantages;
- our efforts to protect our intellectual property rights may not be effective in preventing misappropriation of our technology; or
- our efforts may not prevent the development and design by others of products or technologies similar to or competitive with, or superior to those we develop.



In addition, we may not be able to effectively protect our intellectual property rights in certain foreign countries where we may do business in the future or from which competitors may operate. While we have numerous pending international patents, obtaining such patents will not necessarily protect our technology or prevent our international competitors from developing similar products or technologies. Our inability to adequately protect our patented rights would have a negative impact on our operations and revenues.

In addition, legal standards relating to the validity, enforceability, and scope of protection of intellectual property rights in Internet-related businesses are uncertain and still evolving. Because of the growth of the Internet and Internet related businesses, patent applications are continuously and simultaneously being filed in connection with Internet-related technology. There are a significant number of U.S. and foreign patents and patent applications in our areas of interest, and we believe that there has been, and will likely continue to be, significant litigation in the industry regarding patent and other intellectual property rights.

***If we fail to meet our obligations to SAIC, we may lose our rights to key technologies on which our business depends.***

Our business depends on our rights to and under the patents we obtained from SAIC. Our agreements with SAIC impose various obligations on us, including payment obligations and minimum royalties that we must pay to SAIC. If SAIC believes that we have failed to meet these obligations, SAIC could seek to limit or reacquire the assigned patent rights, which could lead to costly and time-consuming litigation and, potentially, a loss of our rights in these patents. During the period of any such litigation, our ability to carry out the development and commercialization of potential products could be significantly and negatively affected. The loss or restriction of our rights in our patents would result in our inability to continue our business.

***When we attempt to implement our secure domain name registry services business, we may be subject to government and industry regulation and oversight which may impede our ability to achieve our business strategy.***

The U.S. government has historically controlled the authoritative domain name system (“DNS”) root server since the inception of the Internet. On July 1, 1997, the President of the United States directed the U.S. Secretary of Commerce to privatize the management of the domain name system in a manner that increases competition and facilitates international participation in its management.

On September 29, 2006, the U.S. Department of Commerce extended its delegation of authority by entering into a new agreement with the Internet Corporation for Assigned Names and Numbers (“ICANN”) a California non-profit corporation headquartered in Marina Del Rey, California. ICANN is responsible for managing the accreditation of registry providers and registrars that manage the assignment of top level domain names associated with the authoritative DNS root directory. Although other DNS root directories are possible to create and manage privately without accreditation from ICANN, the possibility of conflicting name and number assignments makes it less likely that users would widely adopt a top level domain name associated with an alternative DNS root directory provided by a non-ICANN-accredited registry service.

On June 26, 2008, ICANN announced that it will be relaxing its prior position and will begin to issue generic top level domain names (“gTLDs”) more broadly than it had previously. ICANN expects to begin to take applications for gTLDs in April or May of 2009 with an application fee of \$100,000 or more per application. ICANN expects the first of these customized gTLDs to be issued in the fourth quarter of 2009.

We are currently evaluating whether we will apply to become an ICANN-accredited registry provider with respect to one or more customized gTLDs, or create our own alternative DNS root directory to manage the assignment of non-standard secure domain names. We have not yet begun discussions with ICANN and we cannot assure you that we will be successful in obtaining ICANN accreditation for our registry service on terms acceptable to us or at all. Whether or not we obtain accreditation from ICANN, we will be subject to the ongoing risks arising out of the delegation of the U.S. government’s responsibilities for the domain name system to the U.S. Department of Commerce and ICANN and the evolving government regulatory environment with respect to domain name registry services.

***The laws governing online secure communications are largely unsettled, and if we become subject to various government regulations, costs associated with those regulations may materially adversely affect our business.***

The current regulatory environment for our services remains unclear. We can give no assurance that our planned product offerings will be in compliance with local, state and/or U.S. federal laws or other laws. Further, we can give no assurance that we will not unintentionally violate such laws or that such laws will not be modified, or that new laws will be enacted in the future which would cause us to be in violation of such laws.

VoIP services are not currently subject to all of the same regulations that apply to traditional telephony. The U.S. Federal Communications Commission has imposed some traditional telephony requirements on VoIP such as disability access requirements and other obligations. It is possible that federal and state legislatures may seek to impose increased fees and administrative burdens on VoIP, data and video providers. Such regulations could result in substantial costs depending on the technical changes required to accommodate the requirements, and any increased costs could erode the pricing advantage over competing forms of communication and adversely affect consumer adoption of VoIP products generally.

The use of the Internet and private IP networks to provide voice, video and other forms of real-time, two-way communications services is a relatively recent development. Although the provisioning of such services is currently permitted by U.S. law and is largely unregulated within the United States, several foreign governments have adopted laws and/or regulations that could restrict or prohibit the provisioning of voice communications services over the Internet or private IP networks. More aggressive domestic or international regulation of the Internet in general, and Internet telephony providers and services specifically, may materially and adversely affect our business, financial condition, operating results and future prospects, particularly if increased numbers of governments impose regulations restricting the use and sale of IP telephony services.

In addition to regulations addressing Internet telephony and broadband services, other regulatory issues relating to the Internet in general could affect our ability to provide our planned security solutions. Congress has adopted legislation that regulates certain aspects of the Internet, including online content, user privacy, taxation, liability for third-party activities and jurisdiction. In addition, a number of initiatives pending in Congress and state legislatures would prohibit or restrict advertising or sale of certain products and services on the Internet, which may have the effect of raising the cost of doing business on the Internet generally.

***Telephone carriers have petitioned governmental agencies to enforce regulatory tariffs, which, if granted, would increase the cost of online communication, and such increase in cost may impede the growth of online communication and adversely affect our business.***

The growing popularity and use of the Internet has burdened the existing telecommunications infrastructures, and many high traffic areas have begun to experience interruptions in service. As a result, certain local telephone carriers have petitioned governmental agencies to enforce regulatory tariffs on IP telephony traffic that crosses over the traditional telephone networks. If any of these petitions or the relief that they seek is granted, the costs of communicating online could increase substantially, potentially adversely affecting the growth in the use of online secure communications. Any of these developments could have an adverse effect on our business.

***The departure of Kendall Larsen, our Chief Executive Officer and President, and/or other key personnel could compromise our ability to execute our strategic plan and may result in additional severance costs to us.***

Our success largely depends on the skills, experience and efforts of our key personnel, including Kendall Larsen, our Chief Executive Officer and President. We have no employment agreements with any of our key executives that prevent them from leaving us at any time. In addition, we do not maintain key person life insurance for any of our officers or key employees. The loss of Mr. Larsen, or our failure to retain other key personnel, would jeopardize our ability to execute our strategic plan and materially harm our business.

***We will need to recruit and retain additional qualified personnel to successfully grow our business.***

Our future success will depend in part on our ability to attract and retain qualified operations, marketing and sales personnel as well as engineers. Inability to attract and retain such personnel could adversely affect our business. Competition for engineering, sales, marketing and executive personnel is intense, particularly in the technology and Internet sectors and in the regions where our facilities are located. We can provide no assurance that we will attract or retain such personnel.

***Growth of internal operations and business may strain our financial resources.***

We intend to significantly expand the scope of our operating and financial systems in order to build our business. Our growth rate may place a significant strain on our financial resources for a number of reasons, including, but not limited to, the following:

- the need for continued development of the financial and information management systems;
- the need to manage relationships with future licensees, resellers, distributors and strategic partners;
- the need to hire and retain skilled management, technical and other personnel necessary to support and manage our business; and
- the need to train and manage our employee base.

The addition of new infrastructure services, networks, vertical categories and affinity websites and the attention they demand, on top of the attention demanded by our pending litigation with Microsoft, may also strain our management resources. We cannot give you any assurance that we will adequately address these risks and, if we do not, our ability to successfully expand our business could be adversely affected.

***If we expand into international markets, our inexperience outside the United States would increase the risk that our international expansion efforts will not be successful, which would in turn limit our prospects for growth.***

We may explore expanding our business to outside the United States. Expansion into international markets requires significant management attention and financial resources. In addition, we may face the following risks associated with any expansion outside the United States:

- challenges caused by distance, language and cultural differences;
- legal, legislative and regulatory restrictions;
- currency exchange rate fluctuations;
- economic instability;
- longer payment cycles in some countries;
- credit risk and higher levels of payment fraud;
- potentially adverse tax consequences; and
- other higher costs associated with doing business internationally.

These risks could harm our international expansion efforts, which would in turn harm our business prospects.

***We will continue to incur significant costs as a result of being a public company.***

As a public company, we will continue to incur significant legal, accounting and other expenses that VirnetX Inc. did not incur as a private company. We expect the laws, rules and regulations governing public companies to increase our legal and financial compliance costs and to make some activities more time-consuming and costly, and these costs could be material to us.

***Failing to maintain the effectiveness of our internal control over financial reporting could cause the cost related to remediation to increase and could cause our stock price to decline.***

In the future, our management may identify deficiencies regarding the design and effectiveness of our system of internal control over financial reporting that we engage in pursuant to Section 404 of the Sarbanes-Oxley Act (“Section 404”) as part of our periodic reporting obligations. Such deficiencies could include those arising from turnover of qualified personnel or arising as a result of acquisitions, which we may not be able to remediate in time to meet the continuing reporting deadlines imposed by Section 404 and the costs of which may harm our results of operations. In addition, if we fail to maintain the adequacy of our internal controls, as such standards are modified, supplemented or amended from time to time, we may not be able to ensure that our management can conclude on an ongoing basis that we have effective internal controls. We also may not be able to retain an independent registered public accounting firm with sufficient resources to attest to and report on our internal controls in a timely manner. Moreover, our registered public accounting firm may not agree with our management’s future assessments and may deem our controls ineffective if we are unable to remediate on a timely basis. If in the future we are unable to assert that we maintain effective internal controls, our investors could lose confidence in the accuracy and completeness of our financial reports which could cause our stock price to decline.

***Our ability to sell our solutions will be dependent on the quality of our technical support, and our failure to deliver high-quality technical support services could have a material adverse effect on our sales and results of operations.***

If we do not effectively assist our customers in deploying our products, succeed in helping our customers quickly resolve post-deployment issues and provide effective ongoing support, or if potential customers perceive that we may not be able achieve the foregoing, our ability to sell our products would be adversely affected, and our reputation with potential customers could be harmed. In addition, as we expand our operations internationally, our technical support team will face additional challenges, including those associated with delivering support, training and documentation in languages other than English. As a result, our failure to deliver and maintain high-quality technical support services to our customers could result in customers choosing to use our competitors’ products instead of ours in the future.

**Risks Related to Our Stock**

***Our business is subject to risks associated with the ongoing financial crisis and weakening global economy.***

The recent severe tightening of the credit markets, turmoil in the financial markets, and weakening global economy impacts our ability to raise needed capital and enter into customer agreements. These slowdowns are expected to worsen if these economic conditions are prolonged or deteriorate further. Further, these conditions and uncertainty about future economic conditions make it challenging for us to forecast our operating results, make business decisions, and identify the risks that may affect our business, financial condition and results of operations. If we are not able to timely and appropriately adapt to changes resulting from the difficult macroeconomic environment, our business, financial condition, and results of operations may be significantly negatively affected.

***Trading in our common stock is limited and the price of our common stock may be subject to substantial volatility, particularly in light of the instability in the financial and capital markets, and we may be unable to maintain the standards for listing our common stock on the NYSE Amex.***

Our common stock is listed on NYSE Amex but its daily trading volume has been limited, sporadic and volatile, particularly in light of the ongoing financial crisis; economic uncertainty tends to exacerbate volatility in the financial markets. Over the past year, the market price of our common stock has experienced significant fluctuations. Between March 31, 2008 and March 31, 2009, the reported last sale price for our common stock has ranged from \$6.70 to \$1.06 per share. With such volatility, there can be no assurance that we will remain qualified to be listed on NYSE Amex. On April 30, 2009, we received notice from the staff of NYSE Amex, indicating that, based on the staff's review of publicly available information, we do not meet certain of NYSE Amex's continued listing standards. In order to maintain our listing on NYSE Amex, we must submit a plan of compliance by June 1, 2009 that addresses how we intend to regain compliance with the continued listing requirements. We will fully comply with the requests of NYSE Amex and submit such a plan.

If, however, NYSE Amex delists our securities from trading on NYSE Amex and we are unable to list our securities on another securities exchange, our securities could be listed on the OTC Bulletin Board or the "Pink Sheets," which may adversely affect the liquidity and price of our common stock. In addition, we expect the price of our common stock to continue to be volatile as a result of a number of factors, including, but not limited to, the following:

- developments in our pending litigation against Microsoft;
- quarterly variations in our operating results;
- large purchases or sales of common stock;
- actual or anticipated announcements of new products or services by us or competitors;
- general conditions in the markets in which we compete; and
- economic and financial conditions.

***Because ownership of our common shares is concentrated, you and other investors will have minimal influence on stockholder decisions.***

As of March 31, 2009, our officers and directors beneficially owned an aggregate of 10,604,413 shares, or 27.35% of our outstanding common stock. In addition, a group of stockholders that, as of December 31, 2007, held 4,766,666 shares, or 13.7% of our outstanding common stock, have entered into a voting agreement with us that requires them to vote all of their shares of our voting stock in favor of the director nominees approved by our Board of Directors at each director election going forward, and in a manner that is proportional to the votes cast by all other voting shares as to any other matters submitted to the stockholders for a vote. As a result, our existing officers and directors could significantly influence stockholder actions of which you disapprove or that are contrary to your interests. This ability to exercise significant influence could prevent or significantly delay another company from acquiring or merging with us.

***Our protective provisions could make it difficult for a third party to successfully acquire us even if you would like to sell your shares to them.***

We have a number of protective provisions that could delay, discourage or prevent a third party from acquiring control of us without the approval of our Board of Directors. Our protective provisions include:

- **A staggered Board of Directors:** This means that only one or two directors (since we have a five-person Board of Directors) will be up for election at any given annual meeting. This has the effect of delaying the ability of stockholders to effect a change in control of us since it would take two annual meetings to effectively replace at least three directors which represents a majority of the Board of Directors.
- **Blank check preferred stock:** Our Board of Directors has the authority to establish the rights, preferences and privileges of our 10,000,000 authorized, but unissued, shares of preferred stock. Therefore, this stock may be issued at the discretion of our Board of Directors with preferences over your shares of our common stock in a manner that is materially dilutive to existing stockholders. In addition, blank check preferred stock can be used to create a "poison pill" which is designed to deter a hostile bidder from buying a controlling interest in our stock without the approval of our Board of Directors. We have not adopted such a "poison pill;" but our Board of Directors has the ability to do so in the future, very rapidly and without stockholder approval.

- **Advance notice requirements for director nominations and for new business to be brought up at stockholder meetings:** Stockholders wishing to submit director nominations or raise matters to a vote of the stockholders must provide notice to us within very specific date windows and in very specific form in order to have the matter voted on at a stockholder meeting. This has the effect of giving our Board of Directors and management more time to react to stockholder proposals generally and could also have the effect of disregarding a stockholder proposal or deferring it to a subsequent meeting to the extent such proposal is not raised properly.
- **No stockholder actions by written consent:** No stockholder or group of stockholders may take actions rapidly and without prior notice to our Board of Directors and management or to the minority stockholders. Along with the advance notice requirements described above, this provision also gives our Board of Directors and management more time to react to proposed stockholder actions.
- **Super majority requirement for stockholder amendments to the By-laws:** Stockholder proposals to alter or amend our By-laws or to adopt new By-laws can only be approved by the affirmative vote of at least 66 2/3% of the outstanding shares.
- **Elimination of the ability of stockholders to call a special meeting of the stockholders:** Only the Board of Directors or management can call special meetings of the stockholders. This could mean that stockholders, even those who represent a significant block of our shares, may need to wait for the annual meeting before nominating directors or raising other business proposals to be voted on by the stockholders.

***Securities analysts may not cover our common stock and this may have a negative impact on our common stock's market price.***

The trading market for our common stock may depend on the research and reports that securities analysts publish about us or our business. We do not have any control over these analysts. There is no guarantee that securities analysts will cover our common stock. If securities analysts do not cover our common stock, the lack of research coverage may adversely affect our common stock's market price. If we are covered by securities analysts, and our stock is downgraded, our stock price would likely decline. If one or more of these analysts ceases to cover us or fails to publish regularly reports on us, we could lose or fail to gain visibility in the financial markets, which could cause our stock price or trading volume to decline.

***We may seek to raise additional funds, finance acquisitions or develop strategic relationships by issuing capital stock that would dilute your ownership.***

We have financed our operations, and we expect to continue to finance our operations, acquisitions and develop strategic relationships, by issuing equity or convertible debt securities, which could significantly reduce the percentage ownership of our existing stockholders. Furthermore, any newly issued securities could have rights, preferences and privileges senior to those of our existing stock. Moreover, any issuances by us of equity securities may be at or below the prevailing market price of our stock and in any event may have a dilutive impact on your ownership interest, which could cause the market price of stock to decline. We may also raise additional funds through the incurrence of debt or the issuance or sale of other securities or instruments senior to our common shares. The holders of any debt securities or instruments we may issue would have rights superior to the rights of our common stockholders.

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*We have no current intention of declaring or paying any cash dividends on our common stock.*

We do not plan to declare or pay any cash dividends on our common stock. Our current policy is to use all funds and any earnings in the operation and expansion of our business.

**ITEM 2 — UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.**

We had no issuance of unregistered securities during the three months ended March 31, 2009.

**ITEM 3 — DEFAULTS UPON SENIOR SECURITIES.**

None.

**ITEM 4 — SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

None.

**ITEM 5 — OTHER INFORMATION.**

None.

**ITEM 6 — EXHIBITS.**

<b>Exhibit Number</b>	<b>Description</b>
3.1	Amended and Restated Certificate of Incorporation of the Company. †
3.2	By-laws of the Company. †
4.1	Form of Common Stock Purchase Warrant Issued to Gilford Securities Incorporated. (1)
4.2	Form of Warrant Agency Agreement by and between the Company and Corporate Stock Transfer, Inc. as Warrant Agent.(2)
4.3	Form of Underwriter’s Warrant. (1)
31.1	Certification of the President and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
32.1	Certification of the President and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**

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† Incorporated by reference to the Company’s Form 8-K filed with the Securities and Exchange Commission on July 12, 2007 (File No. 000-26895).

(1) Incorporated by reference to the Company’s Form 8-K filed with the Securities and Exchange Commission on March 18, 2008 (File No. 001-3852).

(2) Incorporated herein by reference to the Company’s Registration Statement on Form S-1/A filed with the Securities and Exchange Commission on January 26, 2009 (File No. 333-153643).

\* Filed herewith.

\*\* Furnished herewith.



**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**VIRNETX HOLDING CORPORATION**

By: /s/ Kendall Larsen  
Kendall Larsen  
Chief Executive Officer (Principal Executive Officer)

By: /s/ William E. Sliney  
William E. Sliney  
Chief Financial Officer (Principal Accounting and Financial Officer)

Date: May 11, 2009

**EXHIBIT INDEX**

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\* Filed herewith.

\*\* Furnished herewith.

## CERTIFICATIONS

I, Kendall Larsen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of VirnetX Holding Corporation for the quarter ended March 31, 2009;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ KENDALL LARSEN

Kendall Larsen

*President and Chief Executive Officer*

*(Principal Executive Officer)*

Date: May 11, 2009

## CERTIFICATIONS

I, William E. Sliney, certify that:

1. I have reviewed this quarterly report on Form 10-Q of VirnetX Holding Corporation for the quarter ended March 31, 2009;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ William E. Sliney

William E. Sliney

Chief Financial Officer

(Principal Accounting and Financial Officer)

Date: May 11, 2009

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of VirnetX Holding Corporation (the "Company") on Form 10-Q for the quarter ended March 31, 2009 as filed with the Securities and Exchange Commission on May 11, 2009 (the "Report"), I, Kendall Larsen, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ KENDALL LARSEN

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Kendall Larsen

*President and Chief Executive Officer*

*(Principal Executive Officer)*

Date: May 11, 2009

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of VirnetX Holding Corporation (the "Company"), on Form 10-Q for the quarter ended March 31, 2009 as filed with the Securities and Exchange Commission on May 11, 2009 (the "Report"), I, William E. Sliney, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ WILLIAM E. SLINEY

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William E. Sliney

*Chief Financial Officer*

*(Principal Accounting and Financial Officer)*

Date: May 11, 2009