

TELKONET INC
Form S-3
March 05, 2007

As filed with the Securities and Exchange Commission on March 5, 2007
Registration No. 333-

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

FORM S-3

REGISTRATION STATEMENT
Under
The Securities Act of 1933

TELKONET, INC.

(Exact Name of Registrant as Specified in Its Charter)

Utah

(State or Other Jurisdiction of Incorporation or
Organization)

87-0627421

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

20374 Seneca Meadows Parkway, Germantown, Maryland 20876
(240) 912-1800

(Address, Including Zip Code, and Telephone Number, Including Area Code
of Registrant's Principal Executive Offices)

Ronald W. Pickett

Chief Executive Officer

20374 Seneca Meadows Parkway
Germantown, Maryland 20876

(Name and Address, Including Zip Code, of Agent for Service)

(240) 912-1800

(Telephone Number, Including Area Code, of Agent for Service)

copy to:

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APPROXIMATE DATE OF COMMENCEMENT OF PROPOSED SALE TO THE PUBLIC: Upon effectiveness of this registration statement.

If the only securities being registered on this form are being offered pursuant to dividend or interest reinvestment plans, please check the following box.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box.

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.

CALCULATION OF REGISTRATION FEE

Title of each Class of Securities To Be Registered	Amount To Be Registered	Proposed Maximum Offering Price Per Share	Proposed Maximum Aggregate Offering Price	Amount Of Registration Fee
Common Stock, \$0.001 par value	6,600,000(1)	\$2.77(2)	\$18,282,000(2)	\$1,956.00

(1) Pursuant to Rule 416(a), this Registration Statement shall also cover any additional shares of the registrant's common stock that become issuable by reason of any stock splits, stock dividends or similar transactions.

(2) Estimated in accordance with Rule 457 solely for the purpose of determining the registration fee.

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the registration statement shall become effective on such date as the Securities and Exchange Commission (SEC), acting pursuant to said Section 8(a), may determine.

The information in this prospectus is not complete and may be changed. The selling stockholders named in this prospectus may not sell these securities until the Securities and Exchange Commission declares our registration statement effective. This prospectus is not an offer to sell the securities and is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

Subject to completion, dated March 5, 2007

PROSPECTUS

TELKONET, INC.

6,600,000 Shares

Common Stock

This prospectus covers 6,600,000 shares of our common stock that may be offered and sold from time to time by the selling stockholders. We will not receive any proceeds from the sale of the shares of our common stock pursuant to this prospectus. We will bear the costs relating to the registration of the shares of our common stock, which we estimate to be approximately \$24,956.

The selling stockholders may sell the shares of our common stock through ordinary brokerage transactions or through any other means described in this prospectus under "PLAN OF DISTRIBUTION." The price at which the selling stockholders may sell the shares will be determined by the prevailing market price for the shares or in negotiated transactions.

Our common stock is listed on the American Stock Exchange ("AMEX") under the symbol "TKO." On February 27, 2007, the last reported sale price of our common stock was \$2.77.

Investing in shares of our common stock involves risks. See "RISK FACTORS" beginning on page 4 of this prospectus.

Neither the SEC nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

No dealer, salesperson or other person has been authorized to give any information or to make any representations other than those contained in or incorporated by reference into this prospectus in connection with the offer contained in this prospectus and, if given or made, such information or representations must not be relied upon as having been authorized by us. Neither the delivery of this prospectus nor any sale made hereunder shall under any circumstances create an implication that there has been no change in our affairs since the date hereof. The selling stockholders named in this prospectus are offering to sell, and seeking offers to buy, shares of our common stock only in jurisdictions where such offers and sales are permitted. The information contained in, and incorporated by reference into, this prospectus speaks only as of the date of this prospectus unless the information specifically indicates that another date applies.

The date of this prospectus is _____, 2007.

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THE COMPANY

This summary highlights selected information contained elsewhere in this prospectus and incorporated into this prospectus by reference. This summary may not contain all of the information that may be important to you in considering an investment in our common stock. You should carefully read the entire prospectus, including the documents that are incorporated by reference into this prospectus, before making an investment decision. Unless the context requires otherwise, references in this prospectus to "Telkonet," the "company," "we," "us," and "our" refer to Telkonet, Inc.

Overview

The Company was formed in 1999 to develop products for use in the powerline communications (PLC) industry. PLC products use existing electrical wiring in commercial and residential buildings to carry high speed data communications signals, including the Internet. Since its formation, the Company has focused on development and marketing of its PLC technology. Following the acquisition of Microwave Satellite Technologies (MST) in January 2006, the Company began offering complete sales, installation, and service of VSAT and business television networks, and became a full-service national Internet Service Provider (ISP). The acquisition of the MST business enabled the Company to begin offering a complete "triple-play" solution to subscribers of HDTV, VoIP telephony and NuVision Broadband Internet access, in commercial multi-dwelling units and hotels.

Our powerline communications technology, the "Telkonet iWire System™" product suite (formerly referred to as the PlugPlus™ product suite), consists of four primary components, the Gateway, the eXtender, the Coupler and the iBridge. The Gateway, the hub of the Telkonet iWire System™, is a modular, self-contained unit that accepts data from an existing network on one port and distributes it via a second port. The Gateway integrates a communications processor that runs a series of proprietary applications under Linux. The signal generated by the Gateway can be directly coupled into low voltage wiring via the Coupler, which interfaces directly between the Gateway and the building's electrical panel. Multi-panel buildings typically require multiple Couplers, which are connected to the Gateway via inexpensive coaxial cable and concentrated using standard radio frequency splitters. A suite of software applications running on the Gateway can perform communications functions or system management functions. The iBridge serves as the user's network access device and connects to a user's personal computer through a standard Ethernet cable. The iBridge's AC line cord serves as its power source as well as its network interface. The eXtender™ is used to extend the reach of the Gateway in larger buildings or campus environments.

The Telkonet iWire System™ product suite delivers data to the user at speeds in excess of 7 Mega bits per second (Mbps), with burst speeds of 12.6 Mbps. The Telkonet iWire System™ product suite is installed by connecting an incoming broadband signal (DSL, TL, satellite or cable modem) into the Gateway and connecting the Gateway to the building's electrical panel using one or more Couplers. Once installed, the Gateway distributes the high-speed Internet signal throughout the entire existing network of electrical wires within the building. The user may access a high-speed Internet signal by plugging the iBridge into any electrical outlet and connecting a personal computer to the iBridge using the computer's built-in Ethernet port. Multiple personal computers connected to the iBridge™ can communicate with one another and can share a single broadband resource via the Gateway.

We are a member of the HomePlug™ Powerline Alliance, an industry trade group that engages in marketing and educational initiatives, and sets standards and specifications for products in the powerline communications industry.

We are a Utah corporation and our principal executive offices are located at 20374 Seneca Meadows Parkway, Germantown, Maryland 20876.

Business History

In January 2002, we announced that we had shifted our management emphasis from research and development to product sales and marketing in order to move our initial proprietary products into the commercial market. In January 2002, the Board of Directors, Founders and executive management of the Company also reassessed the Company's capital structure. In order to attract additional management and marketing expertise, and to raise the necessary capital for manufacturing, sales, and marketing, the Board of Directors approved a plan authorizing the repurchase of certain shares of, and options to purchase, Telkonet common stock held by each of David Grimes, L. Peter Larson and Stephen Sadle who, at the time of the stock repurchase, each owned in excess of five percent of the issued and outstanding capital stock and were directors and executive officers of Telkonet. The net effect of the recapitalization was to reduce the number of shares of issued and outstanding common stock from approximately 22,100,000 shares to 13,900,000 shares.

In May 2002, we concluded an offering of Series A convertible debentures pursuant to which we raised approximately \$1.7 million dollars for working capital purposes. In the fourth quarter of 2002, we announced the successful installation of our Telkonet iWire System™ product suite at a historic inn in Augusta, Georgia and installation of a product field trial in Wilmington, North Carolina.

In the first quarter of 2003, we concluded an offering of Series B convertible debentures pursuant to which we raised approximately \$2.5 million dollars for working capital purposes. We also executed a strategic alliance agreement with Choice Hotels International (NYSE: CHH), one of the largest hotel franchise companies in the world, pursuant to which we agreed to become a Choice Hotels-endorsed vendor.

In the second quarter of 2003, we concluded an offering of Senior Notes pursuant to which we raised approximately \$5,000,000, exclusive of placement costs and fees. The proceeds of the Senior Note offering were designated for working capital purposes.

In January 2004, the Board of Directors determined to permit the Senior Noteholders, for a limited period of time, to convert their Senior Notes into the Company's common stock at a conversion price of \$2.10 per share. In connection with this transaction, Senior Noteholders converted Senior Notes having an aggregate principal value of \$2,539,000. As of June 30, 2006, the Senior Notes have been paid in full.

In February 2004, we completed a private offering of our common stock resulting in net proceeds of \$12.8 million. We sold 6,387,600 shares of our common stock in the private offering. The proceeds of the private placement were designated for working capital purposes.

In October 2005, we announced that we completed a convertible senior debt financing of \$20 million. The proceeds of this financing were reserved for general working capital needs. The convertible senior notes were purchased by two institutional investors in the face amount of \$10 million each. In connection with this financing, the Company agreed to certain financial covenants in the Note evidencing such indebtedness which required the Company to achieve minimum revenue of \$2 million for each fiscal quarter during the term of the Note. The Company failed to meet this financial covenant for the period ended June 30, 2006 and, therefore, was required to pay the noteholders an aggregate accelerated principal payment of \$1,000,000 on or before September 1, 2006. Although the Company believes that the failure to meet this covenant did not constitute an event of default under the Senior Convertible Note, one of the noteholders informed the Company that it believed an event of default had occurred. As a result of this dispute, on August 14, 2006, the Company executed separate settlement agreements with the noteholders. Pursuant to the settlement agreements the Company paid to the noteholders on August 15, 2006 \$9,910,392, in the aggregate, plus accrued but unpaid interest of \$23,951 and certain premiums specified in the Notes in satisfaction of the amounts then outstanding under the Notes. The Company also issued 862,452 warrants to purchase shares of the Company's common stock at the exercise price of \$2.58 per share. Registration statements covering the shares underlying the warrants, were filed with the Securities and Exchange Commission on Form S-3 on September 29, 2006 and October 13, 2006 and were declared effective on October 16, 2006 and October 24, 2006, respectively. As a result of the execution of the settlement agreements and the payments required thereby, the Company fully believes it repaid and satisfied all of its obligations under the Notes.

Each settlement agreement provides that the number of shares issued to the noteholders shall be adjusted based upon the arithmetic average of the weighted average price of the Company's common stock on the American Stock Exchange for the twenty trading days immediately following the settlement date. The Company has concluded that, based upon the weighted average of the Company's common stock between August 16, 2006 and September 13, 2006, the Company is entitled to a refund from the two noteholders. One of the noteholders has informed the Company that it does not believe such a refund is required. As a result, the Company has declined to deliver to the noteholders certain stock purchase warrants issued to them pursuant to the settlement agreement pending resolution of this disagreement. One noteholder has alleged that the Company has failed to satisfy its obligations under the settlement

agreement by failing to deliver the warrants. In addition, the noteholder maintains that the Company has breached certain provisions of the Registration Rights Agreement (executed simultaneously with the settlement agreement) and, as a result of such breach, such noteholder claims that it is entitled to receive liquidated damages from the Company. As of February 23, 2007, no legal claim has been filed by the Noteholder.

In January 2006, the Company acquired, for \$9 million, a 90% interest in Microwave Satellite Technologies (MST), a communications technology company that offers complete sales, installation, and service of Very Small Aperture Terminal (VSAT) and business television networks, and is a full-service national Internet Service Provider (ISP). Following this acquisition the Company began providing a “triple-play” solution to HDTV, VoIP telephony and Internet subscribers. The \$9 million purchase price is payable \$1.8 million in cash and 1.6 million unregistered shares of the Company’s common stock. With respect to the cash portion of the purchase price, \$900,000 was paid at the closing and the remaining \$900,000 was paid in February 2007. With respect to the stock portion of the purchase price, 600,000 shares of Telkonet common stock were paid at the closing and in the second quarter 2006 and the remaining 1,000,000 shares are currently held in escrow and shall be released upon the achievement of 3,300 “triple play” subscribers over a three year period. The Company plans to expand MST's existing operations, which currently are concentrated in Manhattan, throughout New York and increase its presence in other major metropolitan cities using the New York system as a template.

On August 31, 2006, the Company completed a private placement of 2.4 million shares of its common stock to Enable Capital Management for gross proceeds of \$6.0 million. No underwriting commissions were paid in connection with this transaction. The proceeds of this offering are being used for general working capital needs. In connection with this offering, the Company also issued to this investor warrants to purchase 1.56 million shares of common stock at an exercise price of \$4.17 per share. These warrants expire five years from the date of issuance.

Technology

We have applied for patents that cover the unique technology integrated into the Telkonet iWire System™ product suite. We also continue to identify, design and develop enhancements to our core technologies that will provide additional functionality, diversification of application and desirability for current and future users of the Telkonet iWire System™ product suite.

In January 2003, we received Federal Communications Commission (FCC) approval to market the Telkonet iWire System™ product suite. FCC rules permit the operation of unlicensed digital devices that radiate radio frequency emissions if the manufacturer complies with certain equipment authorization procedures, technical requirements, marketing restrictions and product labeling requirements. An independent, FCC-certified testing lab has verified that our Gateway complies with the FCC technical requirements for Class A digital devices. No further testing of this device is required and the device may be manufactured and marketed for commercial use.

In March 2005, we received final certification of our Telkonet iWire System™ product suite from European Union (EU) authorities, which certification was required before we could sell and permanently install our products in EU countries. As a result of the certification, Telkonet products that will be sold and installed in EU countries will bear the Conformance Europeene (CE) mark, a symbol that demonstrates that the product has met the EU's regulatory standards and is approved for sale within the EU. We now have satisfied the governmental requirements for product safety and certification in the EU and are free to sell and install the Telkonet iWire System™ product suite in the EU.

In June 2005, we received the National Institute of Standards and Technology (NIST) Federal Information Processing Standard (FIPS) 140-2 validation for the Gateway. In July 2005, we received FIPS 140-2 validation for the eXtender and iBridge. The U.S. federal government requires, as a condition to purchasing certain information processing applications, that such applications receive FIPS 140-2 validation. U.S. federal agencies use FIPS 140-2 compliant products for the protection of sensitive information. As a result of the foregoing validations, as of July 2005, all of Telkonet's powerline carrier products have satisfied all governmental requirements for security certification and are eligible for purchase by the U.S. federal government. In addition to the foregoing, Canadian provincial authorities use FIPS 140-2 compliant products for the protection of sensitive designate information. The Communications-Electronics Security Group (CESG) also has stated that FIPS 140-2 compliant products meet its security criteria for use in data traffic categorized as "Private." CESG is part of the United Kingdom's National Technical Authority for Information Assurance, which is a government agency responsible for validating the security of information processing applications for the government of the United Kingdom, financial institutions, healthcare organizations, and international governments, among others.

In December 2005, the United States Patent and Trademark Office issued patent number 6,975,212 titled "Method and Apparatus for Attaching Power Line Communications to Customer Premises" (U.S. Pat. App. No. 10/219, 811). The patent application covers our proprietary Coupler technology, which enables the conversion of electrical outlets into high-speed data ports without costly installation, additional wiring, or significant disruption of business activity. The Coupler is an integral component of the Telkonet iWire System™ product suite.

In November 2005, we received the Norma Oficial Mexicana (NOM) certification, enabling our Telkonet iWire System™ product suite to be sold in Mexico. NOM certification is required for our products to be sold in Mexico, and no further certifications are required for us to sell the Telkonet iWire System™ product suite in Mexico.

In September 2006, the United States Patent and Trademark Office issued patent number 7,091,831, titled "Method and Apparatus for Attaching Power Line Communications to Customer Premises". The patented technology incorporates a safety disconnect circuit breaker into the Telkonet Coupler, creating a single streamlined unit. In doing so, installation of the Telkonet iWire System(TM) is faster, more efficient, and more economical than with separate disconnect switches, delivering optimal signal quality. The Telkonet Integrated Coupler Breaker patent covers the unique technique used for interfacing and coupling its communication devices onto the three-phase electrical systems that are predominant in commercial buildings.

Private Placement of Common Stock and Warrants to Purchase Common Stock

On February 2, 2007, we completed a private placement of 4.0 million shares of our common stock to Enable Capital Management and Hudson Bay Capital Management, whose affiliates are selling stockholders under this prospectus, for gross proceeds of \$10 million. The Company incurred \$390,000 in private placement fees in connection with this transaction. The proceeds of this offering will be used for general working capital needs and to assist in funding the Company's strategic initiatives. Telkonet also has issued to the purchasers in the private placement warrants to purchase 2.6 million shares of common stock at an exercise price of \$4.17 per share. Additionally, the Company agreed to issue to the placement agent warrants to purchase 79,000 shares of its common stock at an exercise price of \$4.17 per share. These warrants expire five years from the date of issuance.

The shares of our common stock sold in the private placement and those issuable pursuant to the warrants are included in the shares being registered for resale by the selling stockholders pursuant to this prospectus. See "SELLING STOCKHOLDERS" beginning on page 9 of this prospectus.

The common stock and warrants issued in the offering were sold pursuant to the exemption provided by Section 4(2) of the Securities Act of 1933 and/or Rule 506 of Regulation D promulgated thereunder on the basis that the purchaser is an "accredited investor" as such term is defined in Rule 501 of Regulation D.

RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the following risk factors and other information contained in or incorporated by reference into this prospectus and any accompanying prospectus supplement before deciding to purchase any shares of our common stock.

The Company has a history of operating losses and an accumulated deficit and expects to continue to incur losses for the foreseeable future.

Since inception through September 30, 2006, the Company has incurred cumulative losses of \$65,290,482 and has never generated enough funds through operations to support its business. Additional capital may be required in order to provide working capital requirements for the next twelve months. The Company's losses to date have resulted principally from:

- research and development costs relating to the development of the Telkonet iWire System™ product suite;
- costs and expenses associated with manufacturing, distribution and marketing of the Company's products;
- general and administrative costs relating to the Company's operations; and
- interest expense related to the Company's indebtedness.

The Company is currently unprofitable and may never become profitable. Since inception, the Company has funded its research and development activities primarily from private placements of equity and debt securities, a bank loan and short term loans from certain of its executive officers. As a result of its substantial research and development expenditures and limited product revenues, the Company has incurred substantial net losses. The Company's ability to achieve profitability will depend primarily on its ability to successfully commercialize the Telkonet iWire System™ product suite. If the Company is not successful in generating sufficient liquidity from operations or in raising sufficient capital resources on terms acceptable to the Company, this could have a material adverse effect on the

Company's business, results of operations, liquidity and financial condition.

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Potential fluctuations in operating results could have a negative effect on the price of the Company's common stock.

The Company's operating results may fluctuate significantly in the future as a result of a variety of factors, most of which are outside the Company's control, including:

- the level of use of the Internet;
- the demand for high-tech goods;
- the amount and timing of capital expenditures and other costs relating to the expansion of the Company's operations;
- price competition or pricing changes in the industry;
- technical difficulties or system downtime;
- economic conditions specific to the internet and communications industry; and
- general economic conditions.

The Company's quarterly results may also be significantly impacted by certain accounting treatment of acquisitions, financing transactions or other matters. Such accounting treatment could have a material impact on the Company's results of operations and have a negative impact on the price of the Company's common stock.

The Company's directors and executive officers own a substantial percentage of the Company's issued and outstanding common stock. Their ownership could allow them to exercise significant control over corporate decisions.

As of December 31, 2006, the Company's officers and directors owned 18.8% of the Company's issued and outstanding common stock. This means that the Company's officers and directors, as a group, exercise significant control over matters upon which the Company's stockholders may vote, including the selection of the Board of Directors, mergers, acquisitions and other significant corporate transactions.

Further issuances of equity securities may be dilutive to current stockholders.

Although the funds raised in the Company's debenture offerings, the note offerings and the private placement of common stock are being used for general working capital purposes, it is likely that the Company will be required to seek additional capital in the future. This capital funding could involve one or more types of equity securities, including convertible debt, common or convertible preferred stock and warrants to acquire common or preferred stock. Such equity securities could be issued at or below the then-prevailing market price for the Company's common stock. Any issuance of additional shares of the Company's common stock will be dilutive to existing stockholders and could adversely affect the market price of the Company's common stock.

The exercise of options and warrants outstanding and available for issuance may adversely affect the market price of the Company's common stock.

As of December 31, 2006, the Company had outstanding employee options to purchase a total of 8,520,929 shares of common stock at exercise prices ranging from \$1.00 to \$5.97 per share, with a weighted average exercise price of \$2.06. As of December 31, 2006, the Company had outstanding non-employee options to purchase a total of 1,815,937 shares of common stock at an exercise price of \$1.00 per share. As of December 31, 2006, the Company had warrants outstanding to purchase a total of 4,557,850 shares of common stock at exercise prices ranging from

\$2.59 to \$4.87 per share, with a weighted average exercise price of \$4.20. The exercise of outstanding options and warrants and the sale in the public market of the shares purchased upon such exercise will be dilutive to existing stockholders and could adversely affect the market price of the Company's common stock.

The powerline communications industry is intensely competitive and rapidly evolving.

The Company operates in a highly competitive, quickly changing environment, and the Company's future success will depend on its ability to develop and introduce new products and product enhancements that achieve broad market acceptance in commercial and governmental sectors. The Company will also need to respond effectively to new product announcements by its competitors by quickly introducing competitive products.

Delays in product development and introduction could result in:

- loss of or delay in revenue and loss of market share;
- negative publicity and damage to the Company's reputation and brand; and
- decline in the average selling price of the Company's products.

Government regulation of the Company's products could impair the Company's ability to sell such products in certain markets.

FCC rules permit the operation of unlicensed digital devices that radiate radio frequency emissions if the manufacturer complies with certain equipment authorization procedures, technical requirements, marketing restrictions and product labeling requirements. Differing technical requirements apply to "Class A" devices intended for use in commercial settings, and "Class B" devices intended for residential use to which more stringent standards apply. An independent, FCC-certified testing lab has verified that the Company's Telkonet's iWire System™ product suite complies with the FCC technical requirements for Class A and Class B digital devices. No further testing of these devices is required and the devices may be manufactured and marketed for commercial and residential use. Additional devices designed by the Company for commercial and residential use will be subject to the FCC rules for unlicensed digital devices. Moreover, if in the future, the FCC changes its technical requirements for unlicensed digital devices, further testing and/or modifications of devices may be necessary. Failure to comply with any FCC technical requirements could impair the Company's ability to sell its products in certain markets and could have a negative impact on its business and results of operations.

Products sold by the Company's competitors could become more popular than the Company's products or render the Company's products obsolete.

The market for powerline communications products is highly competitive. The HomePlug(TM) Powerline Alliance has grown over the past year and now includes many well recognized brands in the networking and communications industries. These include Linksys (a Cisco company), Intel, GE, Motorola, Netgear, Sony and Samsung. With the exception of Motorola, who recently introduced a commercial product, these companies do not presently represent a direct competitive threat to the Company since they only market and sell their products in the residential sector. There can be no assurance that other companies will not develop PLC products that compete with the Company's products in the future. Some of these potential competitors have longer operating histories, greater name recognition and substantially greater financial, technical, sales, marketing and other resources. These potential competitors may, among other things, undertake more extensive marketing campaigns, adopt more aggressive pricing policies, obtain more favorable pricing from suppliers and manufacturers and exert more influence on the sales channel than the Company can. As a result, the Company may not be able to compete successfully with these potential competitors and these potential competitors may develop or market technologies and products that are more widely accepted than those being developed by the Company or that would render the Company's products obsolete or noncompetitive. The Company anticipates that potential competitors will also intensify their efforts to penetrate the Company's target markets. These potential competitors may have more advanced technology, more extensive distribution channels, stronger brand names, bigger promotional budgets and larger customer bases than the Company does. These

companies could devote more capital resources to develop, manufacture and market competing products than the Company could. If any of these companies are successful in competing against the Company, its sales could decline, its margins could be negatively impacted, and the Company could lose market share, any of which could seriously harm the Company's business and results of operations.

The failure of the internet to continue as an accepted medium for business commerce could have a negative impact on the Company's results of operations.

The Company's long-term viability is substantially dependent upon the continued widespread acceptance and use of the Internet as a medium for business commerce. The Internet has experienced, and is expected to continue to experience, significant growth in the number of users. There can be no assurance that the Internet infrastructure will continue to be able to support the demands placed on it by this continued growth. In addition, delays in the development or