

FLIGHT SAFETY TECHNOLOGIES INC

Form 424B1

February 02, 2004

1,350,000 Units

each unit consisting of two shares of common stock and one redeemable public warrant to purchase one share of common stock

This is a public offering of securities of Flight Safety Technologies, Inc. Our securities are being offered in units, each unit consisting of two shares of our common stock and one public warrant to purchase one share of our common stock. The public warrants will trade only as a part of a unit for 30 days following the effective date of this offering unless the representative of the underwriters determines that separate trading of the public warrants should occur earlier. Each public warrant will entitle its owner to purchase one share of our common stock for \$3.30 per share subject to adjustment, including anti-dilution provisions for corporate events such as stock splits. Each public warrant may be exercised at any time after 30 days from the effective date of this offering or such earlier date as the public warrants become separately tradable and thereafter for five years after the effective date of this offering unless we have redeemed them. At any time after the first anniversary of the date of this offering, we may redeem some or all of the public warrants at a price of \$0.25 per warrant, upon 30 days' notice so long as the last reported sales price per share of our common stock as reported by the principal exchange or trading market on which our common stock trades equals or exceeds \$10.00 for twenty consecutive trading days ending on the tenth day prior to the date we give notice of redemption.

Before this offering, our common stock traded on the National Association of Securities Dealers Over-the-Counter Bulletin Board under the symbol "FSFY." Immediately after effectiveness of this offering, our common stock, units and public warrants have been approved for listing on the American Stock Exchange under the symbols "FLT," "FLT.u," and "FLT.ws," respectively.

The public offering price will be \$6.00 per unit. Unless otherwise indicated, all shares and per-share information in this prospectus gives retroactive effect to a 1-for-3 reverse split of our common stock that was effective December 31, 2003. The public offering price of the units is based on various factors, including the reported sales price per share of our common stock as reported on the Over-the-Counter Bulletin Board, and has been determined by negotiations between us and The Shemano Group, Inc., the representative of the underwriters.

Investing in these units involves significant risks. We urge you to read carefully the "Risk Factors" section beginning on page 6 where we describe specific risks you should consider before buying these units.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

	<u>Per Unit</u>	
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		<u>Total</u>
Public offering price	\$6.00	\$8,100,000
Underwriting discount	\$0.45	\$ 607,500
Proceeds to us, before expenses	\$5.55	\$7,492,500

We expect total cash expenses for this offering to be approximately \$499,500. This does not include a non-accountable expense allowance of 3% of the gross proceeds of this offering payable to The Shemano Group, Inc., as the representative of the underwriters. The units are being offered on a firm commitment basis. The underwriters expect to deliver the units to purchasers on February 4, 2004. We have granted the underwriters a 45-day option to purchase up to 202,500 additional units to cover over-allotments. We have also agreed to sell to the representative underwriters' warrants to purchase up to an additional 135,000 units.

The Shemano Group, Inc. [LOGO]

Prospectus dated January 30, 2004.

## YOUR RELIANCE ON INFORMATION CONTAINED IN THIS PROSPECTUS

We have not authorized anyone to provide you with information different from that contained in this prospectus. These securities may be sold only in jurisdictions where offers and sales are permitted. The information contained in this prospectus is accurate only as of the date of this prospectus, regardless of the time of delivery of this prospectus or of any sale of the securities. You must not consider that the delivery of this prospectus or any sale of the securities covered by this prospectus implies that there has been no change in our affairs since the date of this prospectus or that the information contained in this prospectus is current or complete as of any time after the date of this prospectus.

## FORWARD-LOOKING INFORMATION

### Cautionary Statement Pursuant to Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995:

Except for the historical information presented in this document, the matters discussed in this prospectus, or otherwise incorporated by reference into this document, contain "forward-looking statements" (as such term is defined in the Private Securities Litigation Reform Act of 1995). These statements are identified by the use of forward-looking terminology such as "believes", "plans", "intend", "scheduled", "potential", "continue", "estimates", "hopes", "goal", "objective", "expects", "may", "will", "should" or "anticipates" or the negative thereof or other variations thereon or comparable terminology, or by discussions of strategy that involve risks and uncertainties. The safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended, apply to forward-looking statements made by us. We caution you that no statements contained in this prospectus should be construed as a guarantee or assurance of future performance or results. These forward-looking statements involve risks and uncertainties, including those discussed in the "Risk Factors" section of this prospectus, which include risks and uncertainties associated with, among other things, the outcome of an informal inquiry by the SEC that appears to be in connection with certain analysts reports about us and our press releases. The actual results that we achieve may differ materially from any forward-looking statements due to such risks and uncertainties. These forward-looking statements are based on current expectations, and, except as required by law, we assume no obligation to update this information whether as a result of new information, future events or otherwise. Readers are urged to carefully review and consider the various disclosures made by us in this prospectus and in our other reports filed with the Securities and Exchange Commission that attempt to advise interested parties of the risks and factors that may affect our business.

SOCRATES (TM) and UNICORN (TM) are trademarks of ours. This prospectus also refers to trademarks and trade names of other companies and organizations.

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## PROSPECTUS SUMMARY

You must read the following summary together with the more detailed information regarding us and the securities being offered for sale by means of this prospectus and our financial statements and notes to those statements appearing elsewhere in this prospectus. The following summary highlights information contained elsewhere in this prospectus.

Unless the context indicates otherwise, all references in this prospectus to "we", "our", "us", "FST" or the "company" refer on a consolidated basis to Flight Safety Technologies, Inc., a Nevada corporation, or to its former subsidiary, Flight Safety Technologies Operating, Inc., a Delaware corporation (sometimes referred to as "FSTO") that was merged into FST on June 27, 2003.

Overview

We are developing two proprietary technologies designed to enhance aviation safety and reduce airport delays on which we have received United States and foreign patents.

Using our technology, known as SOCRATES (*S*ensor for *O*ptically *C*haracterizing *R*emote *A*tmospheric *T*urbulence *E*manating *S*ound), we are currently working on development of a sensor to detect and track air disturbances known as wake vortex turbulence, created by departing and arriving aircraft in the vicinity of airports. We are developing this sensor to be a component of a wake vortex advisory system, known as WVAS, that the National Aeronautics and Space Administration, or NASA, is developing. We believe that our SOCRATES wake vortex sensor, upon completion and deployment in concert with other components of WVAS, can:

Improve the safety of aircraft arrivals and departures;

Streamline the air traffic control process;

Reduce passenger delays; and

Generate substantial cost savings for the airline industry and other airport users.

A "proof of principle" test of our SOCRATES wake vortex sensor was conducted at JFK International Airport in May 1998. We completed controlled testing of an expanded and improved SOCRATES wake vortex sensor, using a NASA Boeing 757 as the source aircraft, at Langley Air Force Base in December 2000. In September 2003, we completed a three-week test of an improved SOCRATES wake vortex sensor at Denver International Airport. Based upon our analysis of initial data, this test demonstrated a major increase in the capability and reliability of the sensor.

We have conducted research, development, and testing of our SOCRATES wake vortex sensor in conjunction with Lockheed Martin Corporation pursuant to a ten-year teaming agreement dated May 1, 1997 under which we are the prime contractor.

We also are developing a collision avoidance and ground proximity warning system for small aircraft based on our technology referred to as UNICORN (*U*niversal *C*ollision *O*bviation and *R*educed *N*ear-*M*iss). We recently received a frequency assignment from the Federal Communications Commission for experimental purposes and development of UNICORN and have signed a contract with Georgia Tech Applied Research Corporation, or GTARC, under which GTARC has commenced work on the construction of our UNICORN antenna elements. We plan to integrate the antenna with electronics, displays, and processing elements into a collision alerting and ground proximity warning system aimed at the general aviation market. We also have begun exploring the application of this technology to unmanned air vehicles and other specialized commercial and government flight operations.

We have been awarded three successive contracts from various federal government agencies aggregating approximately \$13 million for research, development and testing of our SOCRATES wake vortex sensor. We have not had any revenues from commercial sales and we do not expect such sales for several years.

Our principal office is located in Mystic, Connecticut, and our phone number is (860) 245-0191.

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Units offered in this offering	1,350,000 units, each unit consisting of two shares of our common stock and one public warrant to purchase one share of our common stock. The public warrants will trade only as part of a unit for 30 days following the effective date of this offering unless the representative of the underwriters determines that separate trading of the public warrants should occur earlier.
Common stock to be outstanding after this offering	8,002,068 shares
Public warrants to be outstanding after this offering	Public warrants to purchase up to 1,350,000 shares of common stock.
Term of public warrants	The public warrants are exercisable at any time after 30 days from the effective date of this offering (or such earlier date as the public warrants become separately tradable) until they expire five years from the effective date of this offering, unless earlier redeemed.
Exercise price of public warrants	\$3.30
Redemption of public warrants	At any time after the first anniversary of the date of this offering, we may redeem some or all of the public warrants at a price of \$0.25 per warrant, upon 30 days' notice so long as the last reported sales price per share of our common stock as reported by the principal exchange or trading market on which our common stock trades equals or exceeds \$10.00 (subject to certain adjustments) for twenty consecutive trading days ending on the tenth day prior to the date we give notice of redemption.
American Stock Exchange symbols	Common stock: "FLT" Units: "FLT.u" Public warrants: "FLT.ws"
Risk factors	Investing in these securities involves a high degree of risk. As an investor, you should be able to bear a complete loss of your investment. You should carefully consider the information set forth in the "Risk Factors" section of this prospectus.
Use of proceeds	For general corporate purposes, including working capital, research and development, product development, certification/commissioning, marketing and distribution, and new product development. Please see "Use of Proceeds."

Unless the context indicates otherwise, all share and per-share information in this prospectus (i) is based on 5,302,068 shares of our common stock outstanding as of January 28, 2004, (ii) assumes no exercise of the public warrants, the over-allotment option to purchase up to 202,500 units, warrants to purchase up to 135,000 units granted to the representative in connection with this offering, outstanding options and warrants to purchase a total of 734,008 shares of common stock, which have a weighted average exercise price of \$6.00 per share, and (iii) gives retroactive effect to a 1-for-3 reverse split of our common stock that was effective December 31, 2003.

### Summary Financial Information

In the table below, we provide you with historical selected consolidated financial data for the two years ended May 31, 2003 and 2002, derived from our audited consolidated financial statements included elsewhere in this prospectus. We also provide below financial data for, and as of the end of, our second fiscal quarters of 2004 and 2003, derived from our unaudited financial statements included elsewhere in this prospectus. Historical results are not necessarily indicative of the results that may be expected for any future period. When you read this historical selected financial data, it is important that you read along with it the historical consolidated financial statements and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operation" included elsewhere in this prospectus.

#### Six Months Ended

<u>Year Ended May 31,</u>		November 30,	November 30,
<u>2002</u>	<u>2003</u>	<u>2002</u>	<u>2003</u>
		(unaudited)	(unaudited)

(in thousands)

#### Statement of Operations

Data:

Revenues	\$ 490	\$ 1,093	\$ 40	\$ 1,294
Gross profits	\$ 30	\$ 294	\$ 16	\$ 383
Operating loss	\$ (823)	\$ (948)	\$ (567)	\$ (445)
Net loss	\$ (809)	\$ (944)	\$ (564)	\$ (442)

The table below sets forth a summary of our consolidated balance sheet data as of May 31, 2003, derived from our audited consolidated financial statements included elsewhere in this prospectus. We also provide below financial data for, and as of the end of, our second fiscal quarter of 2004, derived from our unaudited financial statements included elsewhere in this prospectus on an actual basis and on an as adjusted basis. As adjusted data assume the receipt of approximately \$6,750,000 in net proceeds from this offering (excluding proceeds for any election of the overallotment option).

May 31, 2003

November 30, 2003

Actual                      As adjusted  
**(unaudited)**                      **(unaudited)**  
(in thousands)

## Balance Sheet Data:

Cash, cash equivalents and marketable securities	\$	1,040	\$	1,904	\$	8,654
Working capital	\$	905	\$	1,979	\$	8,729
Total assets	\$	1,520	\$	3,025	\$	9,775
Total stockholders' equity	\$	1,146	\$	2,422	\$	9,172

## RISK FACTORS

*Investment in our securities involves a high degree of risk. You should carefully consider the risks described below together with all of the other information included in this prospectus before making an investment decision. The risks and uncertainties described below are not the only ones we face. If any of the following risks actually occurs, our business, financial condition or results of operations could suffer. In that case, the trading price of our securities could decline, and you may lose all or part of your investment.*

### Risks Related to Our Business

#### **Our limited operating history and lack of commercial operations make it difficult to evaluate our prospects.**

Since we began operations in 1997, we have generated limited revenues solely from three SOCRATES technology research and development contracts with agencies of the federal government that fund, administer, and oversee these contracts. The federal government has funded these contracts from earmarked U.S. Congressional appropriations to agencies that have awarded these contracts to us on a sole source basis without competitive bidding. Under these contracts, we are reimbursed for certain allowable research and development costs and are paid a fee calculated as a percentage of costs.

We have not as yet received any revenue from the sale of any products. We do not anticipate receiving any such revenue unless and until our SOCRATES or UNICORN-based products become operational, which could take several years. Our estimates of the market size for the products we are developing are based on many assumptions and uncertainties. These estimates have not been evaluated by an independent party. The actual markets and price we can charge for our products, if and when we successfully complete their development, could be substantially less and our costs could be greater than our estimates. It therefore is difficult to assess our prospects for commercial sales, revenues and profitability.

We have incurred and, for the next several years, can be expected to incur operating losses.

To date, we have incurred significant net losses, including net losses of \$943,974 for our fiscal year ended May 31, 2003 and \$442,362 for the six months ended November 30, 2003. On May 31, 2003, we had an accumulated deficit of \$2,460,023. We anticipate that we may continue to incur significant operating losses for at least the next several years. We may never generate material revenues or achieve or maintain profitability. Substantially all our revenues have been devoted to payment of costs incurred in the research, development, and testing of our SOCRATES or UNICORN technology. Our ability to achieve, maintain, and/or increase profitability will depend in large part upon the successful further development and testing of our SOCRATES or UNICORN-based products, our ability to procure Congressional appropriations and obtain federal research and development contracts for SOCRATES, our ability to obtain additional financing, FAA approval of our SOCRATES or UNICORN-based products and systems by various agencies of the federal government, acquisition of our products and systems by the FAA, airports and the aviation industry, and the availability of funding to finance such acquisitions.



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Lack of future funding from the federal government to complete research and development of our SOCRATES wake vortex sensor could adversely affect our business.

Without notice to, or opportunity for prior review by us, the John A. Volpe National Transportation Systems Center of the U. S. Department of Transportation's Research and Special Programs Administration, or Volpe, circulated a draft report in October 2001 which recommended curtailing further government expenditure on our SOCRATES wake vortex sensor due to a high risk assessment of achieving operational feasibility. Because of this report and the events of September 11, 2001, the government did not fund our SOCRATES research and development contract from December 15, 2001 to November 19, 2002. Together with our major subcontractor, Lockheed Martin Corporation, we vigorously disputed and extensively discussed its assertions with Volpe and NASA. To our knowledge, Volpe did not issue a final report, and Volpe and NASA requested and we submitted a proposal for approximately \$2.2 million of additional SOCRATES technology research, development and testing with an immediate objective of better characterizing the wake acoustics and background noise. In November 2002, Volpe approved and funded a work order in the amount of \$1,229,650 for the first phase of this proposal, and in March 2003, a second work order was approved and funded in the amount of \$991,418. On September 19, 2003, we received notice of our third successive sole source contract from Volpe, titled Phase III SOCRATES, for an aggregate of \$3,975,000.

We believe the federal government has indicated a long-term interest in the development of a wake vortex advisory system and our SOCRATES wake vortex sensor for inclusion in such a system. However, the U.S. government may terminate our government contract at any time if it determines such termination is in the best interests of the government or may terminate, reduce or modify it because of budgetary constraints or any change in the government's requirements. Furthermore, the federal government has in the past delayed or reduced and may in the future delay, reduce, or eliminate funding for research and development of our SOCRATES wake vortex sensor or the wake vortex advisory system as a result of, among other things, a reduction in support or opposition from supervising agencies or the U.S. Congress, changes in budgetary priorities, fiscal constraints caused by federal budget deficits, or decisions to fund competing systems or components of systems. If this occurs, it will reduce our resources available for research and development of our proprietary technologies, new products or enhancements to SOCRATES or UNICORN technologies and to market our products. Reduction of contract funding from the federal government could delay achievement of or increases in profitability, if any, create a substantial strain on our liquidity, resources and product development, and have a material adverse effect on the progress of our research and development and our financial condition.

The government will not pay us for SOCRATES research and development if we do not perform on our contract.

We perform our government contracts pursuant to specific work orders from the government. Such work orders include, but are not limited to, analysis of data, research, development of our SOCRATES technology, planning and conduct of testing, and preparation of various reports. If we do not perform the contracts in accordance with their terms, the government may withhold payment on our bills that we submit monthly. Furthermore, if at any point the government considers a test to be a failure, it may cease to approve further work orders or fund further contracts. Loss of funding on our SOCRATES contract would have a material adverse effect on our business, financial condition, and results of operations.

Our success depends on our successful product development and testing.

Our future success will depend upon our ability to successfully complete the development, testing, and commercialization of our technologies and our ability to develop and introduce new products and services to meet industry, government, and client requirements. We are planning to eventually develop a number of products, based on our SOCRATES and UNICORN technologies. The process of developing such products contains significant technological and engineering hurdles and is extremely complex and expensive. In 2001, Volpe and associated federally funded research centers prepared reports which concluded it was unlikely SOCRATES would result in a sensor that could be used for any operational procedure and even for research because of technical unknowns relating to an understanding of wake vortices and the need to obtain acceptance of WVAS by controllers and pilots. We believe this conclusion was premature and based on an incomplete understanding of SOCRATES and its operational potential. In our opinion, the testing and analysis we have conducted has increasingly supported this potential and resulted in the continuation of funding for our government contracts for research, development and testing of our SOCRATES technology. However, there still are technical, engineering and program integration hurdles we must meet to develop SOCRATES into an operational sensor, including, but not limited to, expanding the sensor to at least 16 laser beams, integrating the sensor into and with the other components of WVAS, and developing operating protocols for WVAS that define how it would be used by air traffic controllers and pilots. In the case of UNICORN, we must successfully overcome development, engineering and testing hurdles to produce an operational product and obtain FAA approval of this product. Furthermore, we will need to extend the term of the experimental license the

FCC has granted us and, ultimately, obtain a permanent license from the FCC for the operation of UNICORN. We might not successfully complete the development of any of our SOCRATES or UNICORN technology into operational products and our products may not be commercially viable. Our failure to complete development of any such products and achieve market acceptance would have a material adverse effect on our business, financial condition, and results of operations.

In addition, certain of our products will require customized installation to address unique characteristics of their environments. Customization could place an additional burden on our resources or delay the delivery or installation of products which, in turn, could have a material adverse effect on our relationship with clients, our business, financial condition, and results of operations.

Our success depends on federal government approval of our products and related systems.

The airport and aviation industry is subject to extensive government oversight and regulation. To introduce our SOCRATES and UNICORN-based products for commercial sale, we must successfully complete research, development, and testing and obtain necessary governmental approvals for their installation. Upon approval by the Federal Aviation Administration, or FAA, our SOCRATES wake vortex sensor would be part of a multi-component wake vortex advisory system that also will require government approvals before it can be deployed. Any factor that delays or adversely affects this approval process, including delays in development or inability to obtain necessary government approvals, could have a material adverse effect on our business, financial condition, and results of operations.

Our business relies on a strategic alliance with Lockheed Martin Corporation and others to develop a complete system.

In May 1997, we signed a Teaming Agreement with Lockheed Martin Corporation to jointly develop and market SOCRATES-based products. This agreement will expire in May 2007, unless certain earlier termination provisions occur or the agreement is extended by mutual agreement. The agreement stipulates that we serve as prime contractor and Lockheed Martin Corporation as subcontractor in the development and any deployment of our SOCRATES wake vortex sensor. Although to date we have generally worked in close cooperation with Lockheed Martin Corporation, there is no assurance that this relationship will be sustained. Future disagreements as to work scope, revenue share, profit margins, ownership of intellectual property, or technical, marketing, or management philosophy, could adversely impact the relationship. Since we view our strategic partnership with Lockheed Martin Corporation as a vital element of our business plan, any erosion of this relationship could have a negative impact on our business and future value.

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We may need to raise additional capital.

Given the uncertainties of research and development and the timing of commercialization of our SOCRATES and UNICORN-based products, the availability and level of government funding, the FAA approvals required for our products, and the long sales cycle from initial customer contact to actual, if any, revenue generation, we might not be able to generate sufficient, if any, revenue or investment capital to fund our operations over the period of years we believe are required to commercialize our products. In each of our last three fiscal years, we have suffered substantial operating losses which we have funded, in part, with equity capital that we raised from new investors.

We will continue to incur significant expenses for research and development and testing of our SOCRATES and UNICORN technology and may continue to suffer such losses prior to commercialization and thereafter. If we cannot achieve commercialization of our SOCRATES and UNICORN technologies with the proceeds of this offering or if we are unable to generate sufficient working capital from revenue from government funding or private contracts for these

purposes, we would need to seek additional capital. In addition, other unforeseen costs and research and development costs of later generation SOCRATES and UNICORN-based products also could require us to seek additional capital. We do not have any credit facilities in place and, should the need for additional capital arise, we may not be able to obtain sufficient, if any, additional capital or raise such capital on acceptable terms. If we need to obtain additional debt or equity capital, it may include our entry into joint ventures or issuance of additional securities, which may cause dilution to our current capital structure and stockholders' ownership. Additional securities also could have a greater priority as to dividends, distributions and other rights than our common stock.

For the life of the public warrants, underwriter's warrants, and existing warrants, the holders thereof are given the opportunity to profit from a rise in the market for our common stock, with a resulting dilution in the interest of all other stockholders. So long as these warrants are outstanding, the terms on which we could obtain additional capital may be adversely affected. The holders of these warrants might be expected to exercise them at a time when we would, in all likelihood, be able to obtain any needed capital by a new offering of securities on terms more favorable than those provided by these warrants.

Loss of key personnel could adversely affect our business.

Our future success depends to a significant degree on the skills, experience and efforts of our executive officers, Samuel A. Kovnat, Chairman of the Board and Chief Executive Officer, William B. Cotton, President and Director, Frank L. Rees, Executive Vice President and Director, and David D. Cryer, Chief Financial Officer, Treasurer and Secretary. The sustained unavailability of any one or more of those individuals for any reason could have a material adverse impact on our operations and prospects. We anticipate hiring additional executive officers in the future. We may not be able to complete the hiring of these additional officers in a timely manner or at all. We also depend on the ability of our executive officers and other members of senior management to continue to work effectively as a team.

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Government regulation could adversely affect our business.

As a result of receiving contract funding from the federal government and our involvement in the field of aviation, our business and operations are subject to numerous government laws and regulations. In the near term, and for so long as we receive funding from the federal government, we will be subject to many procurement and accounting rules and regulations of the federal government. We are also subject to periodic audits by the Defense Contract Audit Agency, or DCAA. To date, we have incurred four audits by the DCAA, and reports have been issued to our government customer which have stated that we are performing in accordance with Federal Acquisitions Regulations. There is no assurance that any of the results or contents of any future audits will portray us favorably. These rules and regulations are complex in nature and sometimes difficult to interpret or apply. Adherence to these rules is reviewed by participating agencies of the federal government. If such agencies suspect or believe that violations of procurement or accounting rules and regulations have occurred, they may refer such matters to other enforcement divisions of the federal government, such as the U.S. Attorney's Office or the Inspector General's office. If we violate these rules and regulations, even if unintentionally, we may have to pay fines and penalties or, in severe cases, could be terminated from receiving further funding from the federal government. If we market, sell and install our products in foreign countries, the laws, rules and regulations of those countries, as well as certain laws of the United States, will apply to us. Existing as well as new laws and regulations of the United States and foreign countries which regulate aviation and airports could also adversely affect our business.

Our success depends on our ability to protect our proprietary technology.

Any failure by us to protect our intellectual property could harm our business and competitive position. For example, although we have sought patent protection for our technologies, the steps we have taken or intend to take with regard to protecting our technologies may not be adequate to defend and prevent misappropriation of our technology, including the possibility of reverse engineering and the possibility that potential competitors will independently develop technologies that are substantially equivalent or superior to our technology. Furthermore, any patent we have obtained or may obtain may subsequently be invalidated for any of a variety of reasons. In addition, even if we are issued a patent, we may not be able to gain any commercial advantage from such patent. Existing United States laws afford only limited intellectual property protection.

We intend to use a combination of patent, trade secret, copyright and trademark law, nondisclosure agreements, and technical measures to protect our proprietary technology. We intend to enter into confidentiality agreements with and obtain assignments of intellectual property from all of our employees, as well as with our clients and potential clients, and intend to limit access to and distribution of our technology, documentation and other proprietary information. However, the steps we take in this regard may not be adequate to deter misappropriation or independent third-party development of our technology. In addition, the laws of some foreign countries do not protect proprietary technology rights to the same extent as do the laws of the United States. If we resort to legal proceedings to enforce our intellectual property rights, the proceedings could be burdensome and expensive and could involve a high degree of risk to our proprietary rights if we are unsuccessful in such proceedings. Moreover, our financial resources may not be adequate to enforce or defend our rights in our technology. Additionally, any patents that we apply for or obtain may not be broad enough to protect all of the technology important to our business, and our ownership of patents does not in itself prevent others from securing patents that may block us from engaging in actions necessary to our business, products, or services.

Other companies may claim that we infringe their intellectual property or proprietary rights.

If our proprietary technology violates or is alleged to violate third party proprietary rights, we may be required to reengineer our technology or seek to obtain licenses from third parties to continue offering our technology without substantial reengineering. Any such efforts may not be successful or if successful could require payments that could have a material adverse effect on our profitability and financial condition. Any litigation involving infringement claims against us would be expensive and time-consuming, and an adverse outcome may result in payment of damages or injunctive relief that could materially and adversely affect our business.

We have received notice claiming that our name infringes upon the trademark rights of another company.

We have received notice, from counsel at another company, claiming that our name infringes upon the trademark rights of the other company regarding its name. Our patent and trademark counsel has reviewed this claim and believes it is without merit. Our counsel has notified the other company of our position, the reasons that support our position, and that we do not intend to change our name. We have not received any response. We believe that if the other company pursues this claim, we may be able to favorably resolve it and, if it is necessary to litigate the claim, we believe the result would be favorable to us. However, any such litigation could be costly to us and divert management's time and attention away from our business. Furthermore, we cannot exclude the possibility of an adverse outcome that could require us to pay damages and change our name.

Our future customers, including the FAA, may not accept the price of or be able to finance our products.

At present, we cannot precisely fix a price for the sale and installation of an initial SOCRATES wake vortex sensor at airports or UNICORN-based collision avoidance systems in small aircraft. We estimate that the cost of our SOCRATES wake vortex sensor will be \$6 million to \$15 million per airport installation, depending on, among other things, the number and configuration of runways, and the wholesale price of a UNICORN-based system will be approximately \$10,000 per aircraft. Because we have not completed the research, development, and testing of either product or received final approvals for either of them from the federal government, we have not commenced production or marketing efforts. We currently do not anticipate having these products ready for commercial sale for at least several years. We therefore are not yet in a position to gauge the reaction of potential customers to the pricing of these products or future products and whether such potential customers will be able to afford and finance our products.

We believe that the increase in efficiency and safety to airports, airlines, and private aircraft resulting from our products will justify the substantial anticipated cost of sales and installation of these products. However, our customers' ability to afford such costs will depend, in part, on the health of the overall economy, the financial condition and budget priorities of the federal government, particularly the FAA and NASA, profitability of airports, airlines, and aircraft manufacturers, and the availability of private and government sources of funding to finance the sales and acquisition of our products. While a variety of potential funding sources exist, inability of the FAA, airlines or airports to access or obtain funding for purchase and installation of our products could have a material adverse impact on sales of our SOCRATES or UNICORN-based products.

We may experience long sales cycles.

We expect to experience long time periods between initial sales contacts and the execution of formal contracts for our products and completion of product installations. The cycle from first contact to revenue generation in our business involves, among other things, selling the concept of our technology and products; developing and implementing a pilot program to demonstrate the capabilities and accuracy of our products; negotiating prices and

other contract terms; and, finally, installing and implementing our products on a full-scale basis. We anticipate this cycle will entail a substantial period of time, on average between seven to twelve months, and the lack of revenue experienced during this cycle and the expenses involved in bringing new sales to the point of revenue generation would put a substantial strain on our resources.

Our success will depend on our ability to create effective sales, marketing, production and installation forces.

At present and for the near future, we will depend upon a relatively small number of employees and subcontractors to complete the research and development of our SOCRATES wake vortex sensor and pursue research and development of other SOCRATES and UNICORN-based products. The marketing and sales of these products will require us to find additional capable employees or subcontractors who can understand, explain, market, and sell our technology and products to airports, airlines, and airplane manufacturers. We also will need to assemble new personnel and/or contractors for production and installation of our products. Upon successful completion of research and development, these demands will require us to rapidly increase the number of our employees, vendors, and subcontractors. There is intense competition for capable personnel in all of these areas, and we may not be successful in attracting, integrating, motivating, or retaining new personnel, vendors, or subcontractors for these required functions.

Our business could be adversely affected if our products fail to perform properly.

Products and systems as complex as ours may contain undetected errors or "bugs," which result in system failures, or failure to perform in accordance with industry expectations. Despite our plans for quality control and testing measures, our products including any enhancements may contain such bugs or exhibit performance degradation, particularly during the early stages of installation, and deployment. Product or system performance problems could result in loss of or delay in revenue, loss of market share, failure to achieve market acceptance, adverse publicity, injury to our reputation, diversion of development resources and claims against us by governments, airlines, airline customers, and others.

We could be subject to liability claims relating to malfunction of our technology.

Sale of our products will depend on their ability to improve airport, airline, and airplane safety and efficiency. We will take great care to test our products and systems after installation and before actual operation to insure accuracy and reliability. The FAA acquires air traffic control equipment for U.S. airports, and typically assumes the principal product liability risk for such equipment. However, unforeseen problems, misuse, or changing conditions could cause our products and systems to malfunction or exhibit other operational problems. Such problems could cause, or be perceived to cause, airplane accidents, including passenger fatalities. We may receive significant liability claims if governments, airlines, airports, passengers and other parties believe that our systems have failed to perform their intended functions. Liability claims could require us to spend significant time and money in litigation, pay substantial damages, and increase insurance premiums, regardless of our responsibility for such failure. Although we plan to maintain liability insurance, such coverage may not continue to be available on reasonable terms or be available in amounts sufficient to cover one or more large claims, and the insurer may disclaim coverage as to any claim.

We face significant competition from other companies.

The air safety systems and air traffic control industries are already highly competitive. Other industry participants could develop or improve their own systems to achieve the cost efficiencies and value that we believe our products will provide upon successful completion of research and development. Additional companies may enter the market with competing systems as the size and visibility of the market opportunity increases. Many of our potential competitors have longer operating histories, greater name recognition, substantially greater financial, technical,

marketing, management, service, support, and other resources than we do. Therefore, they may be able to respond more quickly than we can to new or changing opportunities, technologies, standards, or customer requirements.

New products or technologies will likely increase the competitive pressures that we face. Increased competition could result in pricing pressures, reduced margins, or the failure of our products to achieve or maintain market acceptance. The development of competing products or technologies by market participants or the emergence of new industry or government standards may adversely affect our competitive position. As a result of these and other factors, we may be unable to compete effectively with current or future competitors. Such inability would likely have a material adverse effect on our business, financial condition, or results of operations.

Rapid technological change could render our systems obsolete.

Our business in general is characterized by rapid technological change, frequent new product and service introductions and enhancements, uncertain product life cycles, changes in customer requirements, and evolving industry standards which make us susceptible to technological obsolescence. The introduction of new products embodying new technologies, the emergence of new industry standards, or improvements to existing technologies could render our products and systems obsolete or relatively less competitive. Our future success will depend upon our ability to continue to develop and introduce a variety of new products and to address the increasingly sophisticated needs of our customers. We may experience delays in releasing new products and systems or enhancements in the future. Material delays in introducing new products and systems or enhancements may cause customers to forego purchases of our products and systems and purchase products and systems of competitors instead.

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Failure to properly manage growth could adversely affect our business.

To implement our strategy, we believe that we will have to grow rapidly. Rapid growth may strain our management, financial, and other resources. To manage any future growth effectively, we must expand our sales, marketing, production, installation, and customer support organizations, invest in research and development of new products or enhancements to existing systems that meet changing customer needs, enhance our financial and accounting systems and controls, integrate new personnel or contractors, and successfully manage expanded operations. We may not be able to effectively manage and coordinate our growth so as to achieve or maximize future profitability.

We must hire and retain skilled personnel.

Our success depends in large part upon our ability to attract, train, motivate, and retain highly skilled employees, particularly sales and marketing personnel, scientists, engineers, and other technical support personnel. Our failure to attract and retain the highly trained technical personnel that are integral to our direct sales, product development, installation, support, and professional services may limit the rate at which we can generate sales or develop new products or system enhancements, which could have a material adverse effect on our business, financial condition, or results of operations.

Any acquisition we make could disrupt our business and harm our financial condition.

We may attempt to acquire businesses or technologies that we believe are a strategic fit with our business. We currently have no commitments for any acquisition. Any future acquisition may result in unforeseen operating difficulties and expenditures, and may absorb significant management attention that would otherwise be available for ongoing development of our business. Since we may not be able to accurately predict these difficulties and



expenditures, these costs may outweigh the value we realize from a future acquisition. Future acquisitions could result in issuances of equity securities that would reduce our stockholders' ownership interest, the incurrence of debt, contingent liabilities, amortization of expenses related to other intangible assets and the incurrence of large, immediate write-offs.

You should carefully read and evaluate this entire prospectus including the risks it describes and not consider or rely upon any statement, information or opinion about us that is not contained in this prospectus.

Certain statements, information and opinions about us have appeared and may continue to appear in published news reports, analysts reports, other media sources and our web site. Some of the information contained in these reports or sources was not material to understanding our business or was out of date, erroneous or inconsistent with that disclosed in this prospectus. In making a decision to invest in the units, you should not rely upon any of these statements, information or opinions and should only rely upon, consider and carefully evaluate the information and risks contained in this prospectus.

We currently are involved in an informal SEC investigation.

We recently learned that the staff of the SEC is conducting an informal investigation that appears to be looking into certain analyst reports about us and our press releases. To date, the SEC staff has not asserted that we have acted improperly or illegally. We have voluntarily agreed to cooperate fully with the staff's informal investigation. We believe that we have acted properly and legally with respect to these analyst reports and our press releases. However, we can neither predict the length, scope, or results of the informal investigation nor its impact, if any, on us or our operations. An adverse outcome, which we cannot predict, could negatively impact the market value of any securities we offer and sell under this prospectus and could divert the efforts and attention of our management team from our ordinary business operations.

### Risks Related to Investment in Our Securities

The price of our securities could be volatile and subject to wide fluctuations.

The market price of the securities of a pre-commercial, research and development stage aviation technology company, such as ours, can be especially volatile. Thus, the market price of our securities could be subject to wide fluctuations. In fact, the trading volume and price of our shares have fluctuated greatly. Subject to the information set forth in this prospectus, we are unaware of any specific reasons for this volatility and cannot predict whether or when it will continue.

If our revenues do not grow or grow more slowly than we anticipate, we are unable to procure federal contracts for our SOCRATES wake vortex sensor research and development, we encounter technical or engineering obstacles to the successful commercial development of SOCRATES or UNICORN, operating or capital expenditures exceed our

expectations and cannot be adjusted accordingly, or if some other event adversely affects us, the market price of our securities could decline. In addition, if the market for aviation technology stocks or the stock market in general experiences a loss in investor confidence or otherwise fails, the market price of our securities could fall for reasons unrelated to our business, results of operations, and financial condition. The market price of our securities also might decline in reaction to events that affect other companies in our industry even if these events do not directly affect us. Furthermore, the sale in the open market of recently sold securities or newly issued securities, which we may sell from time to time to raise funds for various purposes, and securities issuable upon the exercise of purchase rights under existing options and warrants may place downward pressure on the market price of our securities.

Speculative traders may anticipate a decline in the market price of our securities and engage in short sales of our securities. Such short sales could further negatively affect the market price of our securities.

Companies that have experienced volatility in the market price of their stock have been the subject of securities class action litigation. If we were to become the subject of securities class action litigation, it could result in substantial costs and a diversion of management's attention and resources.

The representative has limited experience as a managing underwriter.

Although certain officers of the representative have experience working on public offerings and other corporate finance matters, the representative has limited experience serving as a managing underwriter. Since the representative's experience in underwriting a firm commitment public offering is limited, there can be no assurance that the lack of experience will not adversely affect our securities and the subsequent development, if any, of a trading market in such securities.

An active trading market for our securities may not be developed or sustained which could limit the liquidity of an investment in our securities.

There is a limited trading market for our securities. From January 2002 through January 29, 2004, our common stock traded on the OTC Bulletin Board, an inter-dealer automated quotation system for equity securities. The units, shares and public warrants we sell in this offering, together with the shares that formerly traded on the OTC Bulletin Board, have been approved for listing on the American Stock Exchange. There is no assurance that we will be able to continue to meet the listing requirements and that our securities will remain listed on the American Stock Exchange. If we are delisted from the American Stock Exchange, an investor could find it more difficult to dispose of, or to obtain accurate quotations as to the market value of, our securities. Additionally, regardless of which exchange our securities may trade on, an active and liquid trading market may not develop or, if developed, may not be sustained, which could limit securityholders' ability to sell our securities at a desired price.

If any of our securities are delisted from the American Stock Exchange, we may be subject to the risks relating to penny stocks.

If any of our securities were to be delisted from trading on the American Stock Exchange and the trading price of such security remains below \$5.00 per share on the date such security was delisted, trading in such security would also be subject to the requirements of certain rules promulgated under the Securities Exchange Act of 1934. These rules require additional disclosure by broker-dealers in connection with any trades involving a security defined as a penny stock and impose various sales practice requirements on broker-dealers who sell penny stocks to persons other than established customers and accredited investors, generally institutions. The additional burdens imposed upon broker-dealers by such requirements may discourage broker-dealers from effecting transactions in our securities, which could severely limit the market price and liquidity of such securities and the ability of purchasers to sell our securities in the secondary market. A penny stock is defined generally as any non-exchange listed equity security that has a market price of less than \$5.00 per share, subject to certain exceptions.

A large number of shares may be sold in the market following this offering which may cause the price of our securities to decline.

Sales of a substantial number of shares of our common stock or other securities in the public markets, or the perception that these sales may occur, could cause the market price of our common stock or other securities to decline and could materially impair our ability to raise capital through the sale of additional securities. After this offering, we will have 8,002,068 shares of our common stock outstanding (including shares of our common stock comprising a part of the units that are the subject of this offering but excluding shares of our common stock issuable upon exercise of the public warrants comprising a part of those units), or 8,204,568 shares (including shares of our common stock comprising a part of the units that are the subject of this offering but excluding shares of our common stock issuable upon exercise of the public warrants comprising a part of those units) if the underwriters' over-allotment is exercised in full. We anticipate 5,703,581 of the shares will have been registered and eligible for public trading. The 1,350,000 units sold in this offering, or 1,552,500 units if the underwriters' over-allotment is exercised in full, will be freely tradable without restriction or further registration under the federal securities laws unless purchased by our affiliates. Not included in the foregoing are 125,677 shares of our common stock that we may register for certain of our stockholders.

Of the remaining 5,302,068 shares of our common stock outstanding after this offering, based upon shares currently outstanding, and assuming no exercise of options or warrants outstanding as of such date prior to completion of this offering, 1,179,295 shares are subject to contractual lock-up agreements with The Shemano Group, Inc., pursuant to which the holders of such shares have agreed not to sell their shares for 90 days after the effective date of this offering. Of the remaining shares, unless held by "affiliates," 1,021,150 will be freely tradable after September 1, 2004 and 98,042 will be freely tradable after June 27, 2005.

Certain events could result in a dilution of your ownership of our common stock.

We currently have 5,302,068 shares of common stock outstanding and 734,008 common stock equivalents outstanding, including warrants and options. The exercise price of all common stock equivalents is \$6.00 per share. Some of these warrants and options may provide antidilution protection to their holders which would result in our issuance of shares in addition to those under the warrant or option, upon the occurrence of sales of our common stock below certain prices, stock splits, redemptions, mergers, and other similar transactions. Furthermore, from time to time we may issue additional shares of common stock in private or public transactions to raise funds for working capital, research and development, acquisitions, or other purposes. If one or more of these events occurs, the number of outstanding shares of our common stock would increase and dilute your percentage ownership of our common stock.

If we do not maintain an effective registration statement or comply with applicable state securities laws, you may not be able to exercise the public warrants.

For you to be able to exercise the public warrants, the shares of our common stock underlying the public warrants must be covered by an effective and current registration statement and qualify or be exempt under the securities laws of the state or other jurisdiction in which you live. We cannot assure you that we will continue to maintain a current registration statement relating to the shares of our common stock underlying the public warrants or that an exemption from registration or qualification will be available throughout their term. This may have an adverse effect on demand for the public warrants and the prices that can be obtained from reselling them.

The public warrants may be redeemed on short notice. This may have an adverse impact on their price.

We may redeem the public warrants for \$0.25 per warrant, subject to adjustment in the event of a stock split, dividend or the like, upon 30 days' notice so long as the last reported sale price per share of our common stock as reported by the principal exchange or trading market on which our common stock trades equals or exceeds \$10.00 (subject to adjustment) for twenty consecutive trading days ending on the tenth day prior to the date we give notice of redemption. If we give notice of redemption, holders of our public warrants will be forced to sell or exercise the public warrants they hold or accept the redemption price. The notice of redemption could come at a time when, under specific circumstances or generally, it is not advisable or possible to sell or exercise the public warrants.

Our officers, directors and 5% stockholders will exercise significant control over us.

Our current officers, directors and 5% stockholders, in the aggregate, control approximately 35.5% of our outstanding common stock prior to this offering (including common stock issuable to such person or group within 60 days after January 28, 2004). As a result, these stockholders acting together will be able to exert significant control over matters requiring stockholder approval, including the election of directors, approval of mergers, and other significant corporate transactions. This concentration of ownership could delay, prevent, or deter a change in control, and could deprive our stockholders of an opportunity to receive a premium for their stock as part of a sale of us and could affect the market price of our stock.

We do not intend to pay cash dividends.

We have never paid cash dividends on our stock and do not anticipate paying any cash dividends in the foreseeable future.

We may spend the offering proceeds in ways with which our stockholders may not agree.

The use of proceeds from this offering reflects our current planning and is only an estimate that is subject to change in our discretion. Furthermore, a substantial portion of the net proceeds from this offering is not allocated for specific

uses. Consequently, our management can spend offering proceeds in ways with which our stockholders may not agree. We cannot predict that the proceeds will be invested or otherwise utilized to yield a favorable return. See "Use of Proceeds."

#### USE OF PROCEEDS

We estimate that the net proceeds from the sale of the 1,350,000 units that we are selling in this offering will be approximately \$6,750,000 based on a public offering price of \$6.00 per unit and after deducting \$850,500, reflecting the estimated underwriting discount and non-accountable expense allowance, and \$499,500, reflecting the estimated offering expenses payable by us. If the underwriters' over-allotment option is exercised in full, we estimate that we will receive net proceeds of approximately \$7,873,875.

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We expect to use the net proceeds of this offering approximately as follows:

<u>Use of Proceeds</u>	<u>Approximate Amount</u>	<u>Approximate Percentage of Net Proceeds</u>
Research and development	\$1,350,000	20%
Product development	1,250,000	19%
FAA certification/commissioning	1,250,000	19%
Marketing and distribution	400,000	6%
New product development	400,000	6%
Other working capital/general corporate purposes	<u>2,100,000</u>	<u>30%</u>
<b>TOTAL:</b>	<b><u>\$6,750,000</u></b>	<b><u>100%</u></b>

We intend to use the net proceeds of this offering to develop our proprietary SOCRATES technology as follows:

Acceleration of research and development to reach the operation readiness date for our SOCRATES wake vortex sensor sooner than with government funding alone;

Integration of our SOCRATES wake vortex sensor with other weather measurement, prediction and alerting tools into a full wake vortex advisory system;

Performance of operational trials of a wake vortex advisory system required for FAA commissioning and site adaptation of such systems, including our SOCRATES wake vortex sensor, for individual airport sales;

Worldwide promotion and marketing of a wake vortex advisory system containing our SOCRATES wake vortex sensor; and

Investigation and preliminary design of other new products employing our SOCRATES technology, for both aircraft and airport use.

We intend to use the net proceeds of this offering to develop our proprietary UNICORN technology as follows:

Acceleration of research and development to reach FAA certification sooner than with presently available funding;

Integration of our UNICORN antenna subsystem with existing and new displays and alerting devices, and threat logic software;

Performance of FAA tests required for certification of a UNICORN-based product for general aviation aircraft;

Internal efforts plus partnering arrangements with avionics and aircraft manufacturers; and

Shared funding efforts with government agencies to develop our UNICORN technology for unmanned air vehicles and other specialized government applications.

The above amounts are our current estimate of the allocation of the net proceeds. Because the future of our business is difficult to predict, it is likely that the actual amounts used for these purposes will vary significantly from our current estimates. Also, we may use offering proceeds for purposes not listed above in response to cash requirements or business opportunities that we do not now anticipate. In particular, we may use offering proceeds to acquire other businesses or technologies. Any such use could reduce proceeds available for the uses described above. Although we evaluate potential acquisitions in the ordinary course of business, we have no specific understandings, commitments or agreements to make any acquisition or investment at this time.

We anticipate that the net proceeds of this offering, together with projected government contract funding, will be sufficient to fund our operations and capital requirements for at least 24 months following this offering. We cannot assure you, however, that such funds will not be expended earlier due to unanticipated changes in economic conditions or other circumstances that we cannot foresee. In the event our plans change or our assumptions change or prove to be inaccurate, we could be required to seek additional financing sooner than currently anticipated.

Until we use the net proceeds of this offering in our business, we intend to invest the funds in short-term, investment grade, interest-bearing securities. We cannot predict whether the proceeds invested will yield a favorable return.

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We have never declared or paid any cash dividends on our common stock. For the foreseeable future, we intend to retain any earnings to finance the development and expansion of our business, and we do not anticipate paying any cash dividends on our common stock. Any future determination to pay dividends will be at the discretion of our Board of Directors and will be dependent upon then existing conditions, including our financial condition and results of operations, capital requirements, contractual restrictions, business prospects, and other factors that our Board of Directors considers relevant.

CAPITALIZATION

The following table sets forth our capitalization as of May 31, 2003, derived from our audited consolidated financial statements found elsewhere in this prospectus. The table also sets forth our capitalization as of November 30, 2003, derived from our unaudited consolidated financial statements found elsewhere in this prospectus on an actual basis and on an as adjusted basis. As adjusted data assume the receipt of \$6,750,000 in net proceeds from this offering.

	<u>May 31, 2003</u>		<u>November 30, 2003</u>	
			<u>Actual</u>	<u>As adjusted</u>
			(unaudited)	(unaudited)
	(in thousands, except per share data)			
Notes Payable	\$	_____	\$	_____
Stockholders equity (deficit)				
Preferred stock, \$0.001 par value; 5,000,000 shares authorized; no shares issued and outstanding				
Common stock, \$0.001 par value; 50,000,000 shares authorized; 4,919,035 and 5,300,413 shares issued and outstanding at May 31, 2003 and November 30, 2003, respectively		15	5	8
Additional paid-in capital		3,687	5,398	12,145
Deferred compensation		(96)	(79)	(79)
Accumulated deficit		<u>(2,460)</u>	<u>(2,902)</u>	<u>(2,902)</u>
Total stockholders' equity		<u>1,146</u>	<u>2,422</u>	<u>9,172</u>
Total capitalization	\$	<u>1,146</u>	\$	<u>2,422</u>
			\$	<u>9,172</u>

DILUTION

Purchasers of units in this offering will experience immediate and substantial dilution in the net tangible book value of the common stock from the public offering price, without ascribing any value to the warrant included in a unit. Net tangible book value per share represents the amount of our tangible assets reduced by the amount of our total liabilities, divided by the number of shares of common stock outstanding.

As of November 30, 2003, our net tangible book value (unaudited) was \$2,277,897, or approximately \$0.42 per share of common stock then outstanding. As of November 30, 2003, our pro forma net tangible book value (unaudited), as adjusted for the sale of the 1,350,000 units offered in this offering and application of the net proceeds of \$6,750,000 (at the public offering price of \$6.00 per unit and after deducting the underwriting discounts and commissions and estimated offering expenses), would have been approximately \$2.50 per share, without ascribing any value to the warrant included in a unit.

This represents an immediate increase in net tangible book value of \$0.71 per share to existing shareholders and an immediate and substantial dilution of \$1.87 per share or approximately 62.3% to new investors purchasing common stock in this offering.

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The following table illustrates this per share dilution:

	<u>Per Share of Common Stock</u>
Public offering price per share of common stock	\$3.00
Net tangible book value (unaudited) as of November 30, 2003	0.42
Increase attributable to new investors	0.71
Pro forma net tangible book value (unaudited) after this offering	<u>1.13</u>
Dilution of net tangible book value to investors in this offering	<u>\$1.87</u>

The following table summarizes on a pro forma basis, as of January 28, 2004 (giving retroactive effect to our 1-for-3 reverse stock split that was effective December 31, 2003), (i) the number of shares of common stock purchased from us, (ii) the total consideration paid for such shares (without ascribing any value to the warrant included in a unit) and (iii) the average price per share paid by existing holders of our common stock, and investors in this offering, assuming the sale of all 2,700,000 shares offered by this prospectus of common stock at the price indicated above and before deducting any underwriting discounts and offering expenses payable by us.

	<u>Shares</u>		<u>Total Consideration</u>		<u>Average Price per Share</u>
	<u>Number</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>	
Existing Shareholders	5,302,068	66.26%	\$ 5,403,556	40.02%	\$1.02
New Investors	<u>2,700,000</u>	<u>33.74%</u>	<u>8,100,000</u>	<u>59.98%</u>	3.00
Total	<u>8,002,068</u>	<u>100.00%</u>	<u>\$13,503,556</u>	<u>100.00%</u>	\$1.69

The above discussion and tables exclude:

202,500 shares of common stock issuable upon exercise of the underwriters' over-allotment option;

1,485,000 shares of common stock issuable upon the exercise of public warrants and the underwriters'



warrants; and

734,008 shares of common stock reserved for issuance upon exercise of outstanding warrants and options.

#### MARKET FOR COMMON STOCK AND RELATED STOCKHOLDER MATTERS

##### Market Information

On January 14, 2002, our common stock became eligible to trade on the NASD Over-the-Counter Bulletin Board, or OTCBB, under the symbol RELS. No reported trades of the stock on the OTCBB occurred prior to July 21, 2002. Effective September 6, 2002, the symbol changed to FLST. Effective December 31, 2003, the symbol changed to FSFY as a result of our 1-for-3 reverse stock split that was effective December 31, 2003. As of January 28, 2004, we had 5,302,068 shares of common stock outstanding, of which 3,003,581 shares traded on the OTCBB and in Europe on the Berlin Stock Exchange under the symbol "FLH." We have sent notice to the Berlin Stock Exchange to de-list our shares from that exchange and intend to achieve this de-listing as soon as practical. The following chart shows the high and low sales price of our common stock for each of our fiscal quarters since public trading started as quoted on the OTCBB and for the period ending on the day prior to the date of this prospectus (giving retroactive effect to the reverse stock split):

Fiscal Quarter/Period Ended	High	Low
8/31/02	\$10.50	\$5.25
11/30/02	\$6.90	\$4.23
2/28/03	\$6.72	\$2.70
5/31/03	\$3.00	\$1.74
8/31/03	\$18.72	\$2.22
11/30/03	\$9.90	\$6.36
1/29/04	\$7.95	\$3.00

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The quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission, and may not represent actual transactions.

As of January 28, 2004, we had 120 record holders of our common stock, as reflected on the books of our transfer agent. A significant number of shares were held in street name and, as such, we believe that the actual number of beneficial owners is significantly higher.

##### Equity Compensation Plans

The table below provides information relating to our equity compensation plans as of January 28, 2004.

<u>Plan category</u>	Number of securities to be issued upon exercise of outstanding options,	Weighted-average price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under compensation plans (excluding securities reflected
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	<u>warrants and rights</u>		<u>in first column)</u>
Equity compensation plans approved by shareholders	--	--	--
Equity compensation plans not approved by security holders	632,951	\$6.00	(a)

(a) The equity compensation plan not approved by shareholders is comprised of individual common stock option agreements issued to directors, consultants and employees of ours, as summarized below. The common stock options vest between one and three years of the date of issue and expire within three years of the vesting date. The exercise prices of all current outstanding options is \$6.00 per share. Since these options are issued in individual compensation arrangements, there are no options available under any plan for future issuance.

Options issued to:	<u>Number of options</u>	<u>Exercise price</u>	<u>Vesting dates</u>	<u>Expiration dates</u>
Employees		\$6.00	2002	
Consultants		\$6.00	2002	2005
Directors	104,167	\$6.00	2002-2005	2005
Total issued	278,784			2005-2008
	<u>250,000</u>			
	<u>632,951</u>			

#### SELECTED CONSOLIDATED FINANCIAL DATA

In the table below, we provide you with historical selected consolidated financial data for the two years ended May 31, 2003 and 2002, derived from our audited consolidated financial statements included elsewhere in this prospectus. We also provide below financial data for, and as of the end of, our second fiscal quarter of 2004, derived from our unaudited financial statements included elsewhere in this prospectus on an actual basis and on an as adjusted basis. As adjusted data assume the receipt of approximately \$6,750,000 in net proceeds from this offering. Historical results are not necessarily indicative of the results that may be expected for any future period or for a full year. When you read this historical selected financial data, it is important that you read along with it the historical consolidated financial statements and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this prospectus.

(in thousands)

	<u>Year Ended May 31,</u>		<u>Six Months Ended November 30, 2003</u>	
	<u>2002</u>	<u>2003</u>	<u>Actual</u>	<u>As adjusted</u>
			<b>(unaudited)</b>	<b>(unaudited)</b>
Statement of Operations Data:				
Revenues	\$ 490	\$ 1,093	\$ 1,294	\$ 1,294
Gross profits	\$ 30	\$ 294	\$ 383	\$ 383
Operating loss	\$ (823)	\$ (948)	\$ (445)	\$ (445)
Net loss	\$ (809)	\$ (944)	\$ (442)	\$ (442)
	<u>May 31, 2003</u>		<u>November 30, 2003</u>	
			<u>Actual</u>	<u>As adjusted</u>
			<b>(unaudited)</b>	<b>(unaudited)</b>

## Balance Sheet Data:

Cash, cash equivalents and marketable securities	\$ 1,040	\$ 1,904	\$ 8,654
Working capital	\$ 905	\$ 1,979	\$ 8,729
Total assets	\$ 1,520	\$ 3,025	\$ 9,775
Total stockholders' equity	\$ 1,146	\$ 2,422	\$ 9,172

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion of our financial condition and results of operations in conjunction with the financial statements and the notes to those statements included elsewhere in this prospectus. This discussion may contain forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, such as those set forth under "Risk Factors" and elsewhere in this prospectus.

## Overview

Our current operations, including those previously conducted by FSTO, our former subsidiary, have been funded substantially by U.S. Congressional appropriations resulting in three successive sole source contracts with agencies of the federal government for research, development, and testing of our SOCRATES wake vortex sensor and related work pertaining to a wake vortex advisory system, sometimes known as WVAS, that the FAA and NASA are developing. We estimate the appropriations to the FAA totaled approximately \$9.6 million in our fiscal years 1997 through 2000 for research and development of our SOCRATES wake vortex sensor; and NASA appropriations for research and development of our SOCRATES wake vortex sensor totaled approximately \$13.5 million in our fiscal years 2001 through 2003. From these amounts, we have received three contracts aggregating approximately \$13 million. As of November 30, 2003, we have recognized an aggregate of approximately \$9.2 million of contract revenue, of which we have been paid \$8.8 million. Our current SOCRATES government contract backlog is approximately \$3.9 million.

We have entered into these contracts with the Volpe National Transportation Systems Center of the U.S. Department of Transportation ("Volpe"). Volpe funds our contracts when, as, and if it and other sponsoring federal agencies approve a statement of work and specific task orders under the statement of work. When funded, we invoice the federal government monthly based on our direct costs, including overhead and general and administrative costs plus a fixed fee for that month and typically receive payment by electronic wire transfer within two weeks of invoicing. Certain costs we incur, such as (1) lobbying, product development, and business development expenses that are not allowable under these contracts, (2) research and development costs we incur over certain cost caps set by the U.S. government, or (3) costs incurred between contract fundings (collectively hereinafter referred to as "Non-contract Costs"), are not reimbursable under our government contracts. We have funded these Non-contract Costs primarily by proceeds of two private equity placements.

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Without notice to, or opportunity for prior review by us, Volpe circulated a draft report in October 2001 which recommended curtailing further government expenditure on our SOCRATES wake vortex sensor due to a high risk assessment of achieving operational feasibility. Together with our major subcontractor, Lockheed Martin Corporation, we vigorously disputed and extensively discussed its assertions with Volpe and NASA. To our knowledge, Volpe did not issue a final report, and Volpe and NASA requested and we submitted a proposal for approximately \$2,221,068 of additional SOCRATES wake vortex sensor research, development and testing with an immediate objective of better characterizing the wake acoustics and background noise. In November 2002, Volpe approved and funded a new work order in the amount of \$1,229,650 for the first phase of this proposal and in March 2003, a second work order was approved and funded in the amount of \$991,418. Included in the funding is a 7% fixed fee over and above our research and development costs plus overhead, general and administrative costs. The statement of work continued our previous contract to develop and test our SOCRATES wake vortex sensor. This funding ended an 11-month period, from December 15, 2001 to November 19, 2002, without government funding to develop our SOCRATES wake vortex sensor.

On September 30, 2003, we received our third successive sole source contract from Volpe, titled Phase III SOCRATES, for an aggregate of \$3.975 million. This contract initially will be funded from a U.S. fiscal year 2003 Omnibus Appropriation of \$4.5 million to the NASA budget for research, development and testing of our SOCRATES wake vortex sensor as part of a NASA/Department of Transportation/FAA development of WVAS for use at major airports.

For U.S. fiscal year 2004, an additional \$5 million NASA appropriation specifically for continued work on project SOCRATES has been enacted into law. If and when our sponsoring agencies approve an extension of our contract, statements of work and appropriate work orders, we expect we would receive a contract extension for a substantial portion of this funding which would include a major airport test of an expanded 8 to 16-beam, and possibly 32-beam,

SOCRATES wake vortex sensor.

We believe the federal government has indicated a long-term interest in the development of a wake vortex advisory system and our SOCRATES wake vortex sensor for inclusion in such a system. However, the federal government has in the past delayed or reduced and may in the future delay, reduce, or eliminate funding for research and development of our SOCRATES wake vortex sensor or the wake vortex advisory system as a result of, among other things, a reduction in support or opposition from supervising agencies or the U.S. Congress, changes in budgetary priorities, fiscal constraints caused by federal budget deficits, or decisions to fund competing systems or components of systems. If this occurs, it will reduce our resources available for research and development of our proprietary technologies, new products or enhancements to SOCRATES or UNICORN technologies and to market our products. Reduction of contract funding from the federal government could delay achievement of or increases in profitability, if any, create a substantial strain on our liquidity, resources and product development, and have a material adverse effect on the progress of our research and development and our financial condition.

We have experienced significant losses from our inception. The net loss for our fiscal year ended May 31, 2003 of \$943,974 compares unfavorably to the net loss of \$809,100 in our fiscal year ended May 31, 2002. For our fiscal year ending May 31, 2004, net losses for the three month and six month periods ended November 30, 2003 were \$215,721 and \$442,362. The loss for our fiscal year 2003 was caused primarily by three factors: (1) the delay in government contract funding for SOCRATES research and development; (2) rate ceilings; and (3) unallowable expenses. As described below, the loss for the first six months of our fiscal year 2004 ended November 30, 2003 was caused primarily by two of the foregoing factors: (1) rate ceilings and (2) unallowable expenses. We received our third consecutive government contract on September 30, 2003. This contract does not include rate ceilings. Although we will continue to incur certain unallowable expenses, this is a significant change in our contract terms and conditions.

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#### Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based on our financial statements that have been prepared according to accounting principles generally accepted in the United States. In preparing these financial statements, we are required to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosures of contingent assets and liabilities. We evaluate these estimates on an on-going basis. We base these estimates on historical experiences and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions. Our management has discussed these estimates and assumptions with our finance and audit committee. At this point in our operations, subjective judgments do not have a material impact on our financial statements. We refer you to the footnotes to our financial statements for additional information on application of accounting methods and procedures to our financial statements.

Results of Operations

For the periods ended November 30, 2003 and November 30, 2002

*Revenues.* To date, our revenues have consisted almost entirely of revenues earned from our three successive SOCRATES wake vortex sensor research and development contracts with the federal government. Revenues under our government contracts are booked as contract sales when earned.

On September 30, 2003, we received our third government contract for \$3,975,004. Revenues for the three month period ending November 30, 2003 were \$762,252 which was a 43% increase over revenues of \$532,215 for the three month period ending August 31, 2003. This increase is the result of the new government contract we received in the second quarter of our fiscal year 2003. Contract revenue for the three month and six month period ending November 30, 2003 was \$762,252 and \$1,294,467, respectively. This is a significant increase compared to the contract revenue of \$39,832 for both the three and six month periods ending November 30, 2002 and is due to the lack of government contract funding for SOCRATES during the eleven month period ending November 19, 2002. As of November 30, 2003, our contract receivables against our government contracts are \$359,289.

*Direct Contract Costs.* Subcontractor, consultant and direct labor expenses comprise our direct contract costs. Direct contract costs for the three and six month period ending November 30, 2003 were \$552,928 and \$911,812, respectively, compared to \$24,090 for the three and six month periods ending November 30, 2002. These results principally reflect the lack of government contract funding during the six month period ending November 30, 2002.

When our government contract is funded, changes in direct costs do not generally impact our operating income because each contract covers its own direct costs. However, during periods when our government contract is not funded, any such costs we may incur are not reimbursable and must be funded from our own resources.

*Operating Expenses.* Government contractors are required to categorize operating expenses as overhead expenses or general and administrative expenses. These two indirect "cost pools" are then divided by their appropriate "direct cost base" combinations of direct contract cost, which determines the contractors overhead and general and administrative rates. These rates, for our first two government contracts, have been subject to ceilings, which were set at 70% for overhead and 20% for general and administrative. Our third contract is not limited by rate ceilings. Instead, we have negotiated provisional billing rates of 73% for overhead and 28% for general and administrative which we based on forecasted direct and indirect costs. Starting with the end of our fiscal year 2004 our actual rates, based on actual allowable costs incurred, will be submitted to the government for audit at the end of our fiscal year. When our actual rates have been audited, we will adjust our government contract billings higher or lower to reflect the audited actual rates versus the previous estimated provisional billing rates. Our historical rates are shown below.

	For Year Ended <u>5-31-02</u>	For Year Ended <u>5-31-03</u>	For Six Months Ended <u>11-30-03</u>
Overhead Rates			

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General and Admin. Rates	73%	89%	71%
	67%	67%	44%