COMMODORE APPLIED TECHNOLOGIES INC
Form 10-K
April 17, 2007

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

FORM 10-K

[X] **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2006
or

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

Commission File number 001-11871

Commodore Applied Technologies, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**11-3312952**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification
507 Knight Street, Suite B	
Richland, Washington	**99352**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code: **(509) 943-2565**

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which
Common stock, par value $0.001 per share	**NASD Over the Counter Bulletin B**

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes [ ] No [**X**]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes [ ] No [**X**]

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [**X**] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [**X**]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [**X**]

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

As of March 31, 2007, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was $1,192,857 based upon the last sale price of the common stock on March 31, 2007 as reported by the NASD Over the Counter Bulletin Board.

There were 8,116,342 shares of the Registrant's common stock outstanding on March 31, 2007.

DOCUMENTS INCORPORATED BY REFERENCE
None

COMMODORE APPLIED TECHNOLOGIES, INC.

ANNUAL REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2006

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PART I

This Annual Report on Form 10-K contains forward-looking statements." These forward-looking statements can generally be identified as such because the context of the statement will include words such as the Company "believes," "anticipates," "expects" or words of similar import. Similarly, statements that describe the Company's projected future results, future plans, objectives, goals, future conditions or events are also forward-looking statements. Actual results are inherently difficult to predict. Any such forward-looking statements are subject to the risks and uncertainties that could cause actual results of operations, financial condition, acquisitions, financing transactions, expenditures, expansion and other events to differ materially from those expressed or implied in such forward-looking statements. Any such forward-looking statements would be subject to a number of assumptions regarding, among other things, future economic, competitive and market conditions. Such assumptions would be based on facts and conditions as they exist at the time such statements are made as well as predictions as to future facts and conditions, the accurate prediction of which may be difficult and involve the assessment of events beyond the Company's control.

Further, the Company's business is subject to a number of risks and uncertainties that would affect any such forward-looking statements. These risks and uncertainties include, but are not limited to:

. the Company s critical need for additional cash to sustain existing operations and meet existing obligations and capital requirements (the Company s auditor s opinion on our fiscal 2002, 2003, 2004, 2005 and 2006 financial statements contains a going concern qualification in which they express doubt about the Company s

ability to continue in business);

- the ability to generate profitable operations from a large scale remediation project;
- the ability of the Company to implement its waste processing operations, including obtaining commercial waste processing contracts and processing waste under such contracts in a timely and cost effective manner.
- the timing and award of contracts by the U.S. Department of Energy for the cleanup of waste sites administered by it;
- the acceptance and implementation of the Company's waste treatment technologies in the government and commercial sectors;
- the Company's ability to obtain and perform under other large technical support services projects;
- developments in environmental legislation and regulation;
- the ability of the Company to obtain future financing on favorable terms;
- other circumstances affecting anticipated revenues and costs;
- the expiration of the Company's nationwide EPA permit in September 2001 (The Company believes that the permit may be renewed subject to providing additional information. The Company has not resubmitted information for a new permit); and
- the ability of the Company to replicate on a large scale, economically viable basis, the results of its technology test results.

These risks and uncertainties could cause actual results of the Company to differ materially from those projected or implied by such forward-looking statements.

ITEM 1.

BUSINESS

GENERAL

Commodore Applied Technologies, Inc. (the "Company") is an environmental solutions company offering a range of environmental and technical services to the public and private sectors related to (i) providing services related to, environmental management for on-site and off-site identification, investigation remediation and management of hazardous, mixed and radioactive waste and (ii) remediating contamination in soils, liquids and other materials and disposing of or reusing certain waste by-products by utilizing our Solvated Electron Technology ("SET").

The Company's corporate mission is to serve the *environmental remediation market* from its primary operating center to profitably provide government and industry with environmental and remediation solutions to legacy waste environmental problems. Our strategy focuses the Company on the unique and high profit niches of hazardous materials conversion and waste remediation.

The Company was incorporated in Delaware in March 1996. As used in this Annual Report, and except as the context otherwise requires, the "Company" means Commodore Applied Technologies, Inc. and its subsidiaries,

including Commodore Solutions, Inc., Government Environmental Technologies, Inc., and Commodore Advanced Sciences, Inc. The Company's principal executive offices are located at 507 Knight Street, Suite B, Richland, Washington 99352, and its telephone number at that address is (509) 943-2565.

SEGMENT INFORMATION

The Company currently has identified two operating segments. These two segments are as follows:

. Commodore Advanced Sciences, Inc., which primarily provides various environmental and regulatory services to Government agencies on a fixed rate and lump sum basis; and

. Commodore Solutions, Inc., which is commercializing technologies to treat mixed and hazardous wastes, principally the Company's SET technology.

Additional information regarding the business of each segment is set forth below, and the information in Note 16 to the Company's Consolidated Financial Statements included in this Annual Report on Form 10-K is incorporated into this Part I by reference.

COMMODORE ADVANCED SCIENCES, INC. - ENVIRONMENTAL MANAGEMENT

The Company, through Commodore Advanced Sciences, Inc. ("Advanced Sciences"), provides specialized technical and project management products and services primarily to government-sector customers, including the Department of Energy ("DOE") and the Department of Defense ("DOD"), and also to private-sector domestic industrial customers. Advanced Sciences engages in all aspects of environmental regulation and compliance, as well as access to leading technologies and innovative skills related to the identification, investigation, remediation and management of hazardous, mixed and radiological waste sites. Advanced Sciences currently operates a network of three offices located in three states, with its principal executive offices located in Richland, Washington.

Services

Environmental Services Advanced Sciences is a nationwide firm specializing in environmental characterization, regulatory compliance technical support and waste management. Advanced Sciences qualifies as a small business under seven NAICS codes. This subsidiary employs approximately 30 professionals who are expert in providing environmental sample collection, transportation, and analyses, meeting rigorous quality assurance requirements while performing in accord with equally rigorous personnel health and safety requirements.

Advanced Sciences' history of program management and technical services include:

- Environmental Site Restoration Planning
- Preliminary Assessments/Site Investigations
- Environmental Audits & Assessments
- Underground-Storage-Tank Site Investigation

- D & D Planning & Implementation Support
- Waste Minimization
- Health & Safety Oversight & Planning
- Biological Sampling and Characterization

- Environmental Impact Assessments & Statements & Remediation

- Structural Engineering Analysis
- Deconstruction Planning
- Regulatory Compliance
- Remedial Investigations/Feasibility Studies
- Environmental Pollution Control
- Hazardous, Radioactive, Toxic & Mixed-Waste

- Federal & State Agency Coordination Management Including Treatment

- Public Involvement Support

- Hazardous Waste Site Remediation

The two most significant clients Advanced Sciences has had over the past 10 years have been the DOD and the DOE, while also providing services to private industry. Advanced Sciences largest office provides environmental characterization and management, building decontamination and decommissioning (D&D), environmental protection, remediation, restoration, safety & health, and environmental regulatory compliance for the Department of Energys Oak Ridge Complex.

In addition to the Oak Ridge Complex in Tennessee, the Company has performed environmental monitoring and remediation services at Rocky Flats in Colorado, Los Alamos in New Mexico, Chatfield Basin in Colorado and other significant sites, predominantly nuclear energy sites run by the DOD or DOE.

Remediation Services Having already established a market position in the consulting and front-end analysis phase, Advanced Sciences plans to follow market demand into remediation services. After an environmental problem is identified, Advanced Sciences offers alternative remediation approaches that may involve providing on-site waste containment or management of on-site/off-site remediation and waste removal. Advanced Sciences can also redesign its customers' ongoing production processes and develop technical specifications to minimize or eliminate the generation of hazardous waste. The Company believes that Advanced Sciences' integration of environmental skills, plus its access to innovative technologies, provide Advanced Sciences with a competitive advantage in redesigning production processes.

Technical Services New technologies play a critical role in both the remediation of existing waste sites and in the reduction of waste generated by ongoing production processes. Advanced Sciences has access to the SET technology and all its derivatives. Additionally, Advanced Sciences has access to the Supported Liquid Membrane (SLiM) technology held by Commodore Separation Technologies, Inc. (Separation). This technology has the ability to selectively extract heavy metals and radioactive nuclides from liquids and gasses. The SLiM technology is held in an 85% owned subsidiary of Commodore Environmental Services, which owns 4.95 % of the Company. Advanced Sciences has at its disposal, on a per project basis, what it believes are among the most qualified professionals in the environmental consulting business. Advanced Sciences' scientists have participated on national boards for risk assessment and quality assurance, were instrumental in the development of environmental regulations for the DOE and the DOD, and have served as expert witnesses before the U.S. Congress and the Nuclear Regulatory Commission. To maintain its competitive position, Advanced Sciences intends to continue to develop viable remediation technologies and attract and retain qualified personnel.

Contracts

EDAM Advanced Sciences was awarded an Environmental Data Acquisition and Management contract (EDAM) by Bechtel Jacobs Company LLC of Oak Ridge, TN (BJC) in September 2004. During 2004 , 2005 and most of 2006, Advanced Sciences was the lead small business member of the Commodore Advanced Sciences Team (CAST), which also includes team members Science Applications International, Inc. (SAIC), and RCS Corporation (RCS).

CAST performed and managed the EDAM contract through its renewal in August 2006, when Advanced Sciences alone was awarded the full contract of reduced services, with BJC self-performing most tasks previously subcontracted to SAIC as part of the original contract. RCS continues as a teaming partner and subcontractor. BJC also assumed management and invoicing for 13 analytical laboratories that were subcontracted through Advanced Sciences. Analytical laboratory costs, although included as revenue of Advances Sciences, were a zero-margin pass-through activity as a condition to the EDAM contract in place for 2005 and most of 2006. As a result, gross contract revenues decreased in 2006, as well as for the balance of the contract period; however, Advanced Sciences expects better profit margin percentages because the pass-through subcontract to SAIC was a very low margin activity for Advanced Sciences. This program is continuously monitored and audited for safety, quality, productivity, efficiency, and value to BJC and Department of Energy-Oak Ridge.

Sampling activities under the EDAM contract include collection of multiple sample types from hundreds of monitoring locations and packaging and shipping of samples to appropriate analytical laboratories for analysis. Locations and environments include abandoned burial grounds and hazardous waste sites, fields and forests, streams, lakes, and ponds. Sampling tasks support a variety of ongoing monitoring programs, including the Water Resource Restoration Program (WRRP) to determine the effectiveness of remedial actions conducted under CERCLA and the ETTP Environmental Monitoring Program. Regulatory compliance data acquisition and management projects include Resource Conservation and Recovery Act (RCRA) and National Pollution Discharge Elimination System (NPDES) permit compliance, the Biological Monitoring and Abatement Program, and Stormwater Pollution Prevention Program (SWPPP) activities. All of these compliance sampling programs are closely monitored by regulators, stakeholders, BJC, and DOE-OR.

The Company believes the EDAM contract may attract more DOE client groups than are contemplated in the base scope of the contract. The Company is seeking to extend its environmental monitoring service capabilities to other DOE sites, such as Portsmouth, OH and Paducah, KY. The EDAM contract, in which Advanced Sciences participates as a subcontractor, is for a total of approximately $29 million through September of 2008, of which Advanced Sciences portion is approximately $2.1 million and is reflected in the Company s backlog.

Energy Solutions Advanced Sciences was awarded a one-year contract from Duratek Federal Services, Inc. (now Energy Solutions) beginning in January 2005, which was renewed in January 2006 and 2007 for additional one-year periods, to perform environmental monitoring services at two engineered landfills on the Oak Ridge Reservation. Environmental monitoring services include sample collection, packaging and shipping to offsite analytical laboratories. Samples are collected from surface water, groundwater, and landfill leachate collection locations on storm event, weekly, monthly, and quarterly bases.

Chatfield Watershed Authority Advanced Sciences is contracted annually to implement the Chatfield Water Quality Monitoring Program that involves sample and data collection, laboratory subcontract management, and data management for the entire Chatfield Basin watershed located southwest of Denver. The contract is ongoing through 2007 and has been renewed annually with Advanced Sciences since 1986.

Tetra Tech Contract Advanced Sciences provides engineering support under Tetra Tech's general engineering support contract with BJC. BJC is responsible for environmental oversight of the U.S. DOE's Oak Ridge, TN site. Advanced Sciences provided 1 to 3 engineering personnel on a time and material basis to Tetra Tech on a contract basis. This contract expired March 31, 2007.

WESKEM Advanced Sciences was awarded a one-year contract in March 2005 from WESKEM LLC., of Oak Ridge to support their sampling efforts with the Waste Disposition Services Project. The Sample Management Office (SMO) services required to meet the needs of this project are: (i) Assistance with the preparation of analytical statement of works (SOW), (ii) Maintenance of laboratory performance metrics, (iii) Procurement of best value laboratories, (iv) Performance of contract verification of data, and (v) Tracking of samples and sample residue. This contract expired in October 2006.

COMMODORE SOLUTION TECHNOLOGIES, INC. -DECONTAMINATION

The Company, through Commodore Solutions, Inc. (Solutions), has developed and has commercialized its patented process known as SET. Based on the results of its extensive testing and commercial processing activities, the Company believes that SET is capable of effectively treating and decontaminating soils and other materials, including sludges, sediments, oils and other hydrocarbon liquids, metals, clothing and porous and non-porous structures and surfaces, by destroying PCBs, pesticides, dioxins, chlorinated substances and other toxic contaminants to an extent sufficient to satisfy current federal environmental guidelines. The Company also believes that, based on the results of additional tests, SET is capable of neutralizing substantially all known chemical weapons materials and warfare agents, explosives and concentrating certain radioactive wastes for more effective disposal.

The Company believes that SET is the only patented, non-thermal, portable and scalable process that is currently available for treating and decontaminating soils, liquids and other materials containing PCBs,

pesticides, dioxins, chemical weapons and warfare agents and other toxic contaminants.

SET Contracts

The Company was awarded an Advanced Remediation Demonstration contract by the Department of Energy's Office of Environmental Management (DOE-EM) for the Company's technology for the separation of radioactive (surrogate) and RCRA heavy metals from sludges and other waste matrices.

The DOE-EM awarded 12 contracts totaling $3.3 million, of which the Company's demonstration was a part, to support the development of technologies that have the potential to reduce cleanup costs and increase the safety and efficiency of treating and disposing of various waste streams, including radioactive waste at such sites as Hanford, Idaho, Savannah River, and others.

The Company's Phase I contract was performed over a six month period, concluding in January 2007. Phase I activities included: laboratory/pilot-scale test results, developing a technical approach for demonstration, scale-up

and implementation schedule, detailed system design, and a detailed cost estimate for implementation in Phase II. The results of Phase I are under review and Phase II of the contract is expected to be awarded in 2007.

The SET Technology

The Company, its subsidiaries and predecessors have researched, developed, acquired, tested and proven the SET technology, including its processes and equipment, over several years.

The process is based upon a chemical phenomenon discovered by Sir Humphrey Davy in 1865, shown below for the liquid phase of a sodium and potassium solution:

The solution has been called solvated electrons since the dissolved metal releases electrons to the solution in huge numbers. These electrons, also know as free radicals, are the most powerful reducing agents known, quickly reacting with many compounds. Most of the alkali metals readily dissolve in anhydrous ammonia releasing their valance electrons into the ammonia in a relatively rare but stable state unassociated with any atom. In this state, both the electrons and the metal atoms are available to react with other elements and compounds.

The SET technology, which is based upon solvated electron chemistry, mixes anhydrous liquid ammonia and/or other similar solvents with reactive metals and contaminated elements to effect the selective destruction or neutralization of organic compounds (such as PCBs, pesticides and dioxins). The Company has demonstrated that SET can achieve consistently high levels of contaminant destruction when working with PCBs, dioxins and pesticides. SET has treated soils containing up to 10,000 parts per millions ("ppm") of contaminants, and oils containing up to 250,000 ppm, leaving residual soils and oils with contamination levels of less than one ppm. In addition, SET has been successfully applied to other PCB-contaminated surfaces such as concrete. The SET process can be used in conjunction with selected post-treatment processes such that no hazardous or toxic residues will result from the use of SET, nor will there be any toxic emissions into the air, water, soils or other surfaces. For example, most contaminated soils treated with SET can (subject, in some instances, to re-blending the soil with organic matter) be used subsequently for planting or for any other use for which non-contaminated soils are appropriate.

Equipment utilized in the SET process consists of tanks, pumps and piping to handle anhydrous ammonia and other solvents in liquid and vapor forms, and treatment vessels for holding contaminated materials and for the introduction of solvating solutions. The system can be transported to field sites and configured in numerous sizes.

The SET process requires placing the contaminated materials into a treatment vessel where they are mixed with a solvent and charged with a base metal (e.g. sodium). The chemical reaction produces metal salts such as calcium chloride, calcium hydroxide and non-halogenated inert organics. The ammonia within the treatment

vessel is then removed to a discharge tank for later reuse. The materials are removed, sampled for residual traces of PCB or other halogenated organic compounds, and placed in storage for disposal. In many cases, the decontaminated soil and metals can be replaced in their original location, recycled or reused. The solvents do not enter the chemical reaction, but merely serve as dissolving liquids for the solvated electron solution.

Operational Characteristics Substantially all existing systems in use for the destruction of PCBs and other halogenated compounds involve incineration or other thermal processes, and either the permanent installation of highly complex and expensive incinerators and waste disposal equipment at the affected site, or the removal of contaminated materials to off-site facilities. The Company believes that SET represents an approach to resolving serious environmental remediation issues that does not create or entail the safety risks of air pollution and transportation of hazardous materials. The Company believes that SET is more effective than incineration and other destruction processes for toxic substances in that:

. SET does not emit toxic fumes into the atmosphere, as is sometimes the case with thermal or incineration methods;

. SET is portable and can be moved directly to the contaminated site, thereby reducing the risk of off-site contamination;

· SET equipment can be customized and configured for various treatment applications;

. SET's reaction time is substantially less than that of alternative processes, such as thermal destruction and other forms of chemical treatment;

. SET equipment can be installed and operated inside industrial plant facilities to treat hazardous wastes "on-line" as a continuation of the manufacturing process;

. SET, when used to treat soils, yields nitrogen-enriched soils that can be reused on-site, avoiding replacement and the post-treatment costs of off-site disposal; and

. SET has been shown to neutralize or destroy all chemical weapons material and warfare agents in the United States stockpile, and Lewisite (the primary chemical weapons material and warfare agent of the former Soviet Union), in tests conducted by an independent, federally certified surety laboratory.

The Company believes that SET is the only technology currently available that possesses all of these features and is capable of treating a wide variety of contaminants. The above characteristics (non-thermal, no air emissions, mobile) are particularly applicable when dealing with mixed waste. Wastes that contain radioactive material and hazardous waste regulated by RCRA and TSCA are particularly difficult to treat and have extremely limited disposal options. By applying the SET process to remove the RCRA and TSCA components, leaving only radioactive waste material, disposal options expand. SET not only removes the hazardous components but also does so by an efficient, non-thermal process that can control and contain the radioactive material so that it remains in the treated material and does not enter the environment in an uncontrolled fashion.

EPA Nationwide Permit The Company has previously qualified for a permit from the EPA to enable it to treat PCBs within the United States on all non-Superfund sites. Most EPA permits granted to date for PCB destruction are solely for single-site incineration treatment centers. Commodore's initial EPA Nationwide Permit was the first (and only) to be issued for nationwide use as a totally enclosed, non-thermal, chemical destruction process for PCB contaminated organic material. The permit authorized treatment of soils at contamination levels greater than 1,000 ppm PCBs, and also authorized treatment of miscellaneous metallic materials. The test results, confirmed by EPA's contract program laboratory, indicated organics contaminated with PCBs exceeding 5,000 ppm, were treated to non-detect levels of PCBs. In addition to soil treatment, the Nationwide Permit allows the Company to treat PCB contaminated metallic surfaces and waste oils, as well as wastewater (the wastewater is treated by a non-SET process). The Company has also successfully demonstrated SET as a treatment process for organic materials contaminated with PCBs and radionuclides and has received a draft revised EPA permit for these matrices. This permit revision covers the destruction of PCBs in soils, waste oils, organic materials, water, and on metallic surfaces.

Prior to securing a significant contract which utilizes the SET technology, the Company will be required to renew this permit, which expired in 2001. The renewal process may require the Company to provide additional information to the EPA at the time of renewal.

Based on currently published lists of EPA national operating permits, the Company believes that it possesses the only non-thermal PCB treatment technology for multiple applications permitted under the EPA's Alternate Destruction Technology Program. The EPA's Alternative Destruction Technology Program is designed to encourage remediation technologies as an alternative to incineration. EPA regulations governing permitting have been in effect for more than 15 years, and according to the latest EPA published list of non-thermal destructive processes, only seven companies have met EPA's stringent requirements for commercial operation. Of these, only the Company has been permitted for the chemical destruction of such a wide range of PCB contaminated materials.

Test Results The Company has performed treatability studies and actual commercial applications of the SET process that have resulted in successful treatment of over 120 regulated compounds. In more than 1,500 tests using SET, various high levels of contaminants, including PCBs, were reduced to levels approaching non-detectable with the destruction process occurring in a matter of minutes.

The Company has performed various treatability studies and processed commercial quantities of waste utilizing the SET process. Additionally, the Company has conducted several thousand tests of the SET technology on limited quantities of contaminated material, and there can be no assurance that SET will be able to replicate any of these test results on a large-scale commercial basis or on any specific project.

Discussions and selected test results are available at the Company's website at www.commodore.com.

MARKETS AND CUSTOMERS

General

The Company markets its services and technologies to governmental and industrial customers throughout the United States. The Company also plans to target customers in markets abroad, particularly in Eastern Europe and the Middle East. A majority of the Company's sales are technical in nature and involve senior technical and management professionals, supported by the Company's marketing groups. During the year ended December 31, 2006, sales of approximately 100% of the Company's environmental management services were derived from contracts with federal, state and municipal government agencies. Contracts with governmental customers generally may be terminated at any time at the option of the customer. In 2006, two contracts with a single customer, BJC, accounted for approximately 90.2% of Advanced Sciences' revenues. In 2005, BJC accounted for approximately 98.5% of Advanced Sciences revenues. In 2004, the Company had three customers which accounted for 38%, 28%, and 9%, respectively of the Advanced Sciences revenues. The loss of Bechtel Jacobs as a customer would have a material adverse effect upon the Company.

Demand for our environmental technologies is anticipated to arise principally from the following sources:

. Stricter legislation and regulations mandating new or increased levels of air and water pollution control and solid waste management; and

. the need for alternative environmental treatment and disposal methods for toxic substances (such as the SET technology), which involve limited safety risks with respect to air pollution and transportation of hazardous materials and do not result in large volumes of residual waste that require further treatment prior to disposal.

Our business strategy is to expand our environmental technologies businesses by:

. establishing additional collaborative joint working and marketing arrangements with established engineering and environmental service organizations to pursue commercial opportunities in the public and

private sector;

- diversifying the types of service and products offered to clients and potential new customers; and

- implementing the SET technology in selected niche markets within certain strategic environmental market segments, such as government mixed waste remediation and chemical weapons demilitarization.

Decontamination

The Company anticipates that the initial market for commercial applications of SET will be the hazardous and mixed waste and industrial by-products treatment and disposal market. Mixed waste is material that contains both a hazardous and radioactive component. The most common methods of treatment and disposal of hazardous wastes and industrial by-products include landfilling, chemical and biological treatment and incineration. Most of the current treatment and disposal methods entail air pollution and transportation risks. In a mixed waste, both hazardous and nuclear regulations apply, making disposal difficult, if not impossible. Currently, there exists very limited disposal options and these may not provide a permanent solution. Certain of these treatment and disposal methods result in large volumes of residual waste, which may require further treatment prior to disposal. As a result, a number of these methods are encountering increased public resistance and added regulatory oversight.

As with any new technology or process, there has been initial resistance to the use of SET on a large scale, especially in connection with a strong vested interest on the part of the U.S. Military (based on substantial expenditures and commitments previously made) to use incineration for the destruction of chemical weapons. In addition, other prospective projects for the Company have already been committed to other forms of destruction technology, including incineration, plasma arc, vitrification, molten metal, molten salt, chemical neutralization, biological treatment, catalytic electrochemical oxidation and supercritical wet oxidation. The Company, and its collaborative partners, have been attempting to overcome such competition by introducing SET in smaller clean-up projects and through feasibility studies demonstrating its applicability to larger projects, such as the Initial Harrisburg Contract during the years 2000 and 2001, and the WCS Fixed Facility Processing Contract during the year 2001. The SET process provides a significant advantage by allowing the processed material to be disposed of as a non-mixed waste by destroying the hazardous component.

It may also be anticipated that, over an extended period, the market for decontamination of hazardous materials will continue to decline as past environmental degradation is corrected, and as the private and public sectors limit further pollution through prohibitions on production and use of a broad range of hazardous materials and through the modification and improved efficiency of various manufacturing processes. The mixed waste market is one of the few areas that shows growth and has limited competition when compared to the general hazardous waste market. The Company believes the SET process brings a unique solution to the problem of remediating mixed waste.

Environmental Management

Based on market data compiled by Advanced Sciences, the largest market for environmental services today within the United States is the U.S. Government. Government-wide spending levels for environmental services exceed $10 billion per year. The DOD and DOE are expected to account for approximately 66% of such expenditures and together expect to spend in excess of $200 billion for environmental work over the next twenty years. Advanced Sciences has a long-term record for providing environmental services to the U.S. Government with the DOD and DOE being its primary customers.

RAW MATERIALS

The Company has historically experienced no difficulty in obtaining components used in the SET process for which it relies on a broad range of suppliers. Nevertheless, business disruptions or financial difficulties of such suppliers, shortages or other causes beyond the Company's control, could adversely affect the Company by increasing the cost of goods sold or reducing the availability of such components. If the Company was unable to obtain a sufficient supply of required components, it could experience significant delays in the furnishing of components used in the SET process, which could result in the loss of orders and customers and could have a

material adverse affect on the Company's business, financial condition and results of operations. In addition, if the cost of finished components were to increase, there can be no assurance that the Company would be able to pass such increase on to its customers. The use of outside suppliers also entails risks of quality control and disclosure of proprietary information.

BACKLOG

At December 31, 2006, total potential backlog for the Company was approximately $2.1 million as compared with approximately $9.8 million as of December 31, 2005. The total backlog represents work for which the Company has entered into a signed agreement or purchase order with respect thereto or has received an order to proceed with work up to a specified dollar amount. The Company estimates that all of the total backlog represents work that will be completed in the next 12 months. Backlog amounts have historically resulted in revenues; however, no assurance can be given that all amounts included in backlog will ultimately be realized, even if covered by written contracts or work orders.

RESEARCH AND DEVELOPMENT

Research and development activities are ongoing and utilize internal technical staff, as well as independent consultants retained by the Company and its subsidiaries. All such activities are company-sponsored. Research and development expenditures for the Company and its subsidiaries were approximately $0, $5 thousand, and $9 thousand for the years ended December 31, 2006, 2005, and 2004, respectively.

INTELLECTUAL PROPERTY

The Company currently has sixteen (16) issued U.S. and foreign patents. The average life expectancy for the currently issued patents is 10.67 years. As patents are issued, the U.S. Patent and Trademark Office assigns the Company a twenty (20) year patent-life for each patent issued.

The Company believes that its patent portfolio provides the Company the necessary "proprietary turf" in which it can market, distribute, and license the full range of the SET technology and all of its derivatives. Additionally, the Company's strength of its patent portfolio may operate as an effective "barrier to entry" in several of the markets in which the Company is presently conducting business.

To protect its trade secrets and the un-patented proprietary information in its development activities, the Company requires its employees, consultants and contractors to enter into agreements providing for the confidentiality and the Company's ownership of such trade secrets and other un-patented proprietary information originated by such persons while in the employ of the Company. The Company also requires potential collaborative partners to enter into confidentiality and non-disclosure agreements.

There can be no assurance that any patents that may hereafter be obtained, or any of the Company's confidentiality and non-disclosure agreements, will provide meaningful protection of the Company's confidential or proprietary information in the case of unauthorized use or disclosure. In addition, there can be no assurance that the Company will not incur significant costs and expenses, including the costs of any future litigation, to defend its rights in respect of any such intellectual property.

COMPETITION

Decontamination

The Company anticipates that the market for commercial private sector applications of SET will be hazardous and non-hazardous waste and industrial by-products treatment and disposal, in particular the more recalcitrant "mixed" wastes (wastes containing a radioactive element). Several large domestic and international companies and numerous small companies, many of whom have substantially greater financial and other resources than the Company, compete with the Company in this market. The Company primarily competes in the hazardous waste treatment market in the U.S. The top ten competitors in this market account for over 70 percent of the revenues for this market sector. The dominant companies in this sector include companies with permitted waste treatment and disposal sites, including Energy Solutions, Pacific EcoSolution, and American Ecology, as well as other

treatment companies such as PermaFix. The Company s revenues for 2005 account for less than 1 percent of the dollar volume of the hazardous waste market. Any one or more of the Company's competitors or other enterprises not presently known may develop technologies which are superior to the technologies utilized by the Company. To the extent that the Company's competitors are able to offer comparable services at lower prices or of higher quality, or more cost-effective remediation alternatives, the Company's ability to compete effectively could be adversely affected.

The domestic and international governmental public sector of the market is dominated by many large multinational corporations who are presently engaged in providing incineration and other conventional technologies in decontaminating chemical weapons and warfare agents, concentration of nuclear wastes and the decontamination of military vessels and other hardware. These competitors include Raytheon Corporation (the current general contractor for the Johnston Atoll incinerator), EG&G, Inc. (the general contractor for the Tooele Army Depot), Mason and Hanger (the general contractor for the Newport News Naval Facility), Waste Management Corporation (a bidder for domestic "large burial" stockpile weapons decontamination), and others, including Browning-Ferris Industries, Inc., Jacobs Engineering, Inc., Fluor Daniel Corporation and Lockheed Martin Marietta Corporation. All of these corporations have substantially greater financial, personnel and other resources than the Company. In addition, many prospective users of SET have already committed substantial resources to other forms of environmental remediation technology, including incineration, plasma arc, vitrification, bio-remediation, molten salt, chemical neutralization, catalytic electrochemical oxidation and supercritical wet oxidation.

The Company believes that its ability to compete in both the commercial private and governmental public sectors is dependent upon SET being accepted in these sectors as a superior, more cost-effective method to achieve decontamination of a variety of materials.

Environmental Management

In the hazardous waste management market, Advanced Sciences' competitors include such firms as Energy Solutions, Jacobs Engineering, Science Applications International Corp., CH2M Hill and CDM, all of whom have greater financial and other resources than the Company. In providing environmental impact assessment services, Commodore Advanced Sciences' principal competitors in this market sector include RSI, North Wind, Stoller, Weston Solutions, The Earth Technology Corp., Battelle, URS and Woodward-Clyde.

Commodore Advanced Sciences currently occupies a position in the waste management and environmental services arena by virtue of its long-term record for providing environmental services to the United States

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government. Primary factors affecting Advanced Sciences' competitiveness in this market are its ability to continue to attract and retain qualified technical and professional staff with quality project performance records and to control its costs of doing business.

In an effort to maintain its competitive position, Advanced Sciences believes that it has developed a solid infrastructure, acquired a qualified professional staff, and developed aggressive marketing objectives to provide hazardous waste management and environmental sciences to the United States government and private sector industrial customers. The Company believes its competitive position with the United States government is enhanced by the physical proximity of Advanced Sciences' plants to DOE and DOD sites, its skilled professional staff, prior project experience with the United States government, numerous existing multi-year contracts with the United States government, integrated services and high quality performance.

ENVIRONMENTAL REGULATION

The environmental legislation and policies which the Company believes are applicable to SET in the United States primarily include TSCA, RCRA, and the Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA"), as amended by the Superfund Amendments and Reauthorization Act of 1986 ("SARA"), and may include, on a case by case basis, the Clean Air Act of 1970, as amended (the "Clean Air Act"). These laws regulate the management and disposal of toxic and hazardous substances, provide for the protection of land and groundwater resources, and control the discharge of pollutants into the air. Many of these laws have international counterparts, particularly in Europe and elsewhere in North America.

TSCA regulates the manufacture, distribution, and sale of chemical substances, and requires testing of new chemicals and new uses of known chemicals that may present an unreasonable risk of injury to health or the environment. The EPA, through TSCA, has adopted comprehensive regulations for PCB's and other halogenated substances, as part of a vast regulatory program covering thousands of chemicals.

RCRA was enacted in 1976 with the primary objective to protect human health and the environment and to conserve valuable material and energy resources. The most important aspect of RCRA is its establishment of "cradle-to-grave" management and tracking of hazardous waste, from generator to transporter, to treatment, storage, and disposal.

CERCLA and subsequent amendments under SARA (often referred to collectively as Superfund) impose strict, retroactive liability upon persons who generated, transported, or arranged for the transportation of hazardous substances or owned or operated the vessels or facilities at which such substances were disposed. CERCLA provides for the investigation and remediation of hazardous substance sites and mandates that any hazardous substances remaining on-site must meet certain regulatory requirements, with a preference for innovative technology. These program regulations may create an incentive to utilize environmental-friendly technologies such as SET, which destroy targeted wastes without creating additional residual waste product. Moreover, to the extent hazardous substances are effectively destroyed, potential liability can be eliminated or significantly reduced.

The Clean Air Act empowered the EPA to establish and enforce ambient air quality standards and limitations on emissions of air pollutants from specific facilities. In 1987, the EPA began to enforce stricter standards for incineration emissions. With more stringent regulations on waste reduction technologies, the Company believes that SET could obtain a desired market share since, in most cases, it produces little or no air emissions.

CERCLA imposes strict joint and several liability upon owners or operators of facilities when a release or threatened release of a hazardous substance has occurred, upon parties who generated hazardous substances that were released at such facilities and upon parties who arranged for the transportation of hazardous substances to and from such facilities. The Company's plans to own and operate SET at on-site installations expose the Company to potential liability under CERCLA for releases of hazardous substances at those sites. In the event that off-site treatment, storage or disposal facilities utilized by the Company for final disposition of residues from SET are targeted for investigation and clean-up under CERCLA, the Company could incur liability as a generator of such materials or by virtue of having arranged for their transportation and disposal.

In light of such potential liability, the Company has designed the SET technology to minimize the potential for release of hazardous substances into the environment. In addition, the Company has developed plans to manage the

risk of CERCLA liability, including training of operators, use of operational controls and structuring of its relationships with the entities responsible for the handling of waste materials and by-products. The Company also maintains insurance with respect to environmental claims, although there can be no assurance that such insurance will be adequate.

The Clean Air Act Amendments of 1990 impose strict requirements upon owners and operators of facilities that discharge pollutants into the environment. These amendments may require that certain air emission control technology be installed on the SET systems in the event that there is any discharge of non-recovered gases into the environment. Such additional air emission controls can be costly and require an air permit to construct and operate.

The Company obtained a Nationwide Permit issued by the EPA under the Alternative Destruction Technology Program that allowed it to use SET on-site to treat PCB-contaminated soils and metallic surfaces, although the permit is currently expired. The Nationwide Permit contains numerous conditions for maintaining the Nationwide Permit and there can be no assurance that the Company will be able to comply with such conditions to maintain and/or secure renewal of the Nationwide Permit. In addition, if environmental legislation or regulations are amended, or are interpreted or enforced differently, the Company may be required to meet stricter standards of

operation and/or obtain additional operating permits or approvals. Failure to obtain such permits or otherwise comply with such regulatory requirements could have a material adverse effect on the Company and its operations. Various revisions to the equipment and process parameters are being made to the existing permit. The Company believes that the revised permit will be issued pending the final site selection for the full or part-time operation of any SET system for the treatment of PCB wastes. The revised permit will require the Company to fund closure costs associated with the implementation of any SET system for the treatment of PCB wastes. The closure costs are calculated on a site-by-site basis and are funded accordingly by the Company.

EMPLOYEES

As of December 31, 2006, the Company (including its direct subsidiaries) had a total of 29 full-time and 4 part-time employees, of which approximately 27 are engineers, scientists, environmental technicians and other professionals. None of such employees are covered by collective bargaining agreements and the Company's relations with its employees are believed to be good.

All 27 persons on the technical staff are extensively trained in proper procedures for handling waste materials and environmental media. Advanced Sciences technical staff have more than 500 years of combined experience performing environmental and waste sampling tasks. Ten of our personnel hold DOE security clearances.

All Advanced Sciences sampling personnel maintain currency in the following minimum training requirements:

- OSHA 40-hour Hazardous Waste Operations and Emergency Response (HAZWOPER)
- OSHA 8-hr Annual HAZWOPER Refresher
- OSHA HAZWOPER Supervisor
- Hazard Communication (HAZCOM)/Hazardous Materials Information System (HMIS) training
- Radiation Worker II
- First Aid/CPR
- Annual Medical Monitoring
- Respirator Fit Testing
- General Safety
- Hazardous Energy Control (Lockout/Tagout)
- Work Control Process
- Excavation/Penetration Permit
- Construction Equipment Inspection & Maintenance Program
- Hotwork (welding safety)
- Confined Space Program
- Asbestos and Other Fibrous Materials
- Chronic Berylium Disease Prevention

- IATA Dangerous Good Awareness Certificate
- Workplace Substance Abuse Prevention Program participation

OTHER INFORMATION

See Item 8, Financial Statements and Supplementary Data, of this Annual Report on Form 10-K for information regarding revenue from customers, a measure of profit or loss and total assets for each of the Company's segments for the last 3 fiscal years.

The Company currently requires additional cash to sustain existing operations and to meet current obligations and ongoing capital requirements. The reports of our independent registered public accounting firms on our fiscal 2004, 2005 and 2006 consolidated financial statements contain a "going concern" qualification in which they express substantial doubt about our ability to continue in business.

ITEM 1A. RISK FACTORS

Investing in our securities involves a material degree of risk. Before making an investment decision, you should carefully consider the risk factors set forth below as well as other information we include or incorporate by reference in this annual report and the additional information in the other reports we file with the U.S. Securities and Exchange Commission ("SEC").

Credit and Business Risks

The documents governing our indebtedness restrict our ability and the ability of our subsidiaries to engage in some business transactions.

We have entered into a loan arrangement with the Shaar Fund, Ltd. that is collateralized by essentially all the assets of the Company that are not related to the receivable line of credit facility with Commerce Funding Corporation (the "New Shaar Note"). The New Shaar Note is used to fund working capital and general corporate requirements. As of December 31, 2006 and 2005, the outstanding balance was approximately $6.5 million and $5.4 million respectively. The agreements governing the Shaar Loan restrict our ability and the ability of our subsidiaries to, among other things, engage in the following actions:

- declare or pay dividends on and redeem or repurchase capital stock;
- transfer assets or make loans between us and some of our subsidiaries;
- make material changes in the nature or conduct of our business;
- merge or consolidate with, acquire substantially all of the stock or assets of any other companies; and
- transfer or sell assets.

Our failure to comply with obligations under the New Shaar Note could result in an event of default. A default, if not cured or waived, could permit acceleration of our indebtedness. We cannot be certain that we will be able to remedy any default. If our indebtedness is accelerated, we cannot be certain that we will have funds available to pay the accelerated indebtedness or that we will have the ability to refinance the accelerated indebtedness on terms favorable to us or at all.

We have liquidity problems and are uncertain of our continued access to loans.

Our current monthly operating expenses exceed cash revenues by approximately $110 thousand. Currently, this cash shortfall is being covered by loans from The Shaar Fund, Ltd., but The Shaar Fund, Ltd. may discontinue these loans at any time and for any reason. If that happened, we would not be able to meet our current obligations and would be unable to continue operations unless alternative funding was obtained.

In addition, we owe approximately $654 thousand in loans that are currently due or are payable on demand. Although the lenders on these loans have not yet called the loans, the Company does not currently have the ability to pay these loans absent additional financing.

If we are able to obtain financing to cover these obligations, it probably would involve additional dilution to shareholders or additional financial risk to the Company.

Our ability to operate as a going concern is in doubt

The reports of our independent registered public accounting firms on our fiscal 2006, 2005 and 2004 consolidated financial statements contains a "going concern" qualification in which they express substantial doubt about our ability to continue in business.

As shown in the consolidated financial statements for the years ended December 31, 2006, 2005, and 2004, the Company incurred losses before deemed dividends and dividends to preferred stockholders of approximately $1.8 million, $2.7 million and $2.4 million, respectively. The Company has also experienced net cash outflows from operating activities of approximately $596 thousand, $1.3 million and $1.5 million for the years ended December 31, 2006, 2005 and 2004, respectively. At December 31, 2006 and 2005 the Company had working capital deficit of approximately $5.7 million and $4.6 million, respectively.

Our losses have resulted from a combination of:

- costs associated with expansion of our environmental management services business;
- significant costs associated with our commercialization activities;
- financing and interest expenses;
- inadequate revenues due to significant delays in our obtaining material project contracts from potential governmental and private-sector customers; and
- general and administrative expenses.

Until we are able to obtain additional significant environmental services contracts, or one or more large projects for our SET technology, we will continue to experience losses.

Our business strategy depends on business collaborations.

In the environmental services and hazardous waste treatment markets, the Company may not be able to enter into favorable business collaborations and might thus be required to bid upon projects for its own account. If such bids were successful, the Company would be required to make significant expenditures on personnel and capital equipment which would require significant financing.

Even if the Company is successful in achieving favorable business collaborations, the implementation of such arrangements and the expansion of the Company's business may require the commitment of significant capital resources toward the hiring of technical and operational support personnel, the development of a waste treatment facility for SET, and the building of equipment for on-site remediation of contaminated elements. In the event the Company is presented with one or more significant environmental services contracts, reclamation or clean-up projects, individually or in conjunction with collaborative working partners, it may require additional

capital to take advantage of such opportunities. There can be no assurance that such financing will be available or, if available, that it will be on favorable terms.

Our previously reported losses could increase due to our inability to accurately estimate the overall risks, revenue, or costs on a contract.

We generally enter into three principal types of contracts with our clients: firm fixed-price, fixed-unit-rate, and time-and-materials award. Under our firm fixed-price and fixed-unit-rate contracts, we receive a fixed price regardless of the actual costs we incur and, consequently, we are exposed to a number of risks. These risks include underestimation of costs, problems with new technologies, unforeseen costs or difficulties, delays beyond our control and economic and other changes that may occur during the contract period. Under our time-and-materials contracts, we are paid for labor and costs incurred at negotiated contractual rates. Profitability on these contracts is driven by the extent of utilization of our billable personnel and cost control.

Accounting for a contract requires judgment relative to assessing the contract□s estimated risks, revenue, and costs, and on making judgments on other technical issues. Due to the size and nature of several of our contracts, the estimation of overall risks, revenue and costs at completion is complicated and subject to many variables. Changes in underlying assumptions, circumstances, or estimates may also adversely affect future period financial performance.

We may continue to encounter difficulties in pursuing our growth objectives.

Although the Department of Energy has indicated that a number of new contracts will be awarded in 2007 and 2008, governmental awards are frequently delayed. Additionally, we cannot predict whether we will be successful in obtaining new federal services business awards. In some instances, we may choose to bid as the lead of a prime contractor team. In the past, we have operated mainly as a subcontractor or in a minority position on the prime contractor team. We expect to be bidding against organizations that have substantially greater resources and experience in being the leading prime contractor or sub-contractor for these kinds of projects.

In light of these uncertainties for new business awards in our commercial and federal services business units, our growth plan anticipates pursuing new opportunities for providing services with respect to sampling and data management, low-level radioactive waste treatment at DOE sites in the United States. In many of these potential opportunities, we may not have experience comparable to our current and past experience in our federal and commercial businesses. Thus, we may be subject to a range of risks in obtaining and performing these types of businesses, the adequacy and experience of management, and the adequacy of operational resources and technical capabilities needed to perform these mandates successfully. We cannot predict whether we will be successful in obtaining or performing any new business initiatives in these new business areas.

Government Contracting Risks

The U.S. government can audit and disallow claims for compensation under our government contracts, and can terminate those contracts without cause.

Our government contracts, which are primarily with the DOE and DOD, are, and are expected to continue to be, a significant part of our business. Allowable costs under cost reimbursement government contracts are subject to audit by the U.S. government. To the extent that these audits result in determinations that costs claimed as reimbursable are not allowable costs or were not allocated in accordance with Federal government regulations, we could be required to reimburse the U.S. government for amounts previously received. In addition, if we were to lose and not replace our revenues generated by one or more of the U.S. government contracts, our businesses, financial condition, results of operations, and cash flows could be adversely affected.

We derived approximately 100% of our consolidated revenues in 2006 and 2005 from contracts funded by the DOE. The work that we performed for customers that represented greater than 10% of the Company□s segment revenues were with a prime contractor, Bechtel Jacobs Engineering. These contracts with Bechtel Jacobs were not, and are not, cost reimbursement contracts and therefore are not subject to the reimbursable cost audits.

We have a number of contracts and subcontracts with agencies of the U.S. government, principally for environmental services and data management, that extend beyond one year and for which additional government funding has not yet been appropriated. We cannot be certain that the U.S. government will appropriate such funds.

All contracts with agencies of the U.S. government are subject to unilateral termination at the option of the customer. In the event of a termination, we would not receive projected revenues or profits associated with the terminated portion of those contracts; however, all costs incurred prior to termination are recoverable in accordance with Federal Acquisition Regulations.

In addition, government contracts are subject to specific procurement regulations, contract provisions, and a variety of other socioeconomic requirements relating to the formation, administration, performance, and accounting of these contracts. Many of these contracts include express or implied certifications of compliance with applicable laws and contract provisions. As a result of our government contracting, claims for civil or criminal fraud may be brought by the government for violations of these regulations, requirements, or statutes. We may also be subject to qui tam litigation brought by private individuals on behalf of the government under the Federal Civil False Claims Act, which could include claims for up to treble damages. Further, if we fail to comply with any of these regulations, requirements, or statutes, our existing government contracts could be terminated, we could be suspended from government contracting or subcontracting, including federally funded projects at the state level, and our ability to participate in foreign projects funded by the United States could be adversely affected. If one or more of our government contracts are terminated for any reason, or if we are suspended from government work, we could suffer a significant reduction in expected revenues.

Most of our government contracts are awarded through a regulated competitive bidding process. The inability to complete existing government contracts or win new government contracts over an extended period could harm our operations and adversely affect our future revenues.

Most of our government contracts are awarded through a regulated competitive bidding process. Some government contracts are awarded to multiple competitors, which increases overall competition and pricing pressure and may require us to make sustained post-award efforts to realize revenues under these government contracts. In addition, government clients can generally terminate or modify their contracts at their convenience. Moreover, even if we are qualified to work on a new government contract, we might not be awarded the contract because of existing government policies designed to protect small businesses and underrepresented minority contractors. The inability to complete existing government contracts or win new government contracts over an extended period could harm our operations and adversely affect our future revenues.

If our partners fail to perform their contractual obligations on a project, we could be exposed to legal liability, loss of reputation and profit reduction or loss on the project.

We perform projects jointly with outside partners, entering into subcontracts, joint ventures, and other contractual arrangements so that we can jointly bid and perform on particular projects. Success on these joint projects depends in large part on whether our partners fulfill their contractual obligations satisfactorily. If any of our partners fail to satisfactorily perform their contractual obligations as a result of financial or other difficulties, we may be required to make additional investments and provide additional services in order to make up for our partner□s shortfall. If we are unable to adequately address our partner□s performance issues, then our client could terminate the joint project, exposing us to legal liability, loss of reputation, and reduced profit or loss on the project.

Our future success will likely depend, in part, on the success of our existing collaborative relationships. Collaborative arrangements involve risks that the participating parties may disagree on business decisions and strategies resulting in potential delays, additional costs, and risks of litigation. Our inability to successfully maintain existing collaborative relationships or enter into new collaborative arrangements could have a material adverse effect on our results of operations.

Regulatory Risks

Our services expose us to significant risks of liability and our insurance policies may not provide adequate coverage.

When we perform our hazardous waste treatment services, our personnel and equipment may be exposed to radioactive and hazardous materials and conditions. Although we are committed to a policy of operating safely and prudently, we may be subject to liability claims by employees, customers, and third parties as a result of such exposures. In addition, we may be subject to fines, penalties, or other liabilities arising under environmental or safety laws. To date, we have been able to obtain liability insurance for the operation of our business. However, there can be no assurance that our existing liability insurance is adequate or that it will be able to be maintained or that all possible claims that may be asserted against us will be covered by insurance. A partially or completely uninsured claim, if successful and of sufficient magnitude, could have a material adverse effect on our results of operations and financial condition.

We operate in a highly regulated industry requiring our customers and us to have and comply with federal, state, and local government permits and approvals.

We and our customers operate in a highly regulated environment. Facilities utilizing our hazardous waste treatment technology are required to have federal, state, and local government permits and approvals. Any of these permits or approvals may be subject to denial, revocation, or modification under various circumstances. Failure to obtain or comply with the conditions of permits or approvals or with environmental and safety laws may adversely affect our operations and may subject us to penalties and other sanctions.

In addition to regulatory requirements, environmental laws impose joint and several liabilities for the cleanup of contamination upon the current and former owners and operators of contaminated property and on any party who arranges for the disposal or treatment of hazardous substances at a facility that is or becomes contaminated. Such liability is imposed without regard to fault and regardless of knowledge or compliance with environmental requirements. There can be no assurance that we will not face such liability in the future.

In addition, if new environmental legislation or regulations are enacted or existing legislation or regulations are amended or are interpreted or enforced differently, we or our customers may be required to obtain additional operating permits or approvals. Changes in environmental requirements also may require us to change or improve our waste management technologies and services and incur additional expenses. There can be no assurance that we will be able to meet all of the applicable regulatory requirements.

Changes in existing environmental laws, regulations, and programs could reduce demand for our environmental services, which could cause our revenues to decline.

A significant amount of our engineering services and hazardous waste treatment business is generated either directly or indirectly as a result of existing Federal and state laws, regulations, and programs related to pollution and environmental protection. federal, state, and local environmental legislation and regulations require substantial expenditures and impose liabilities for noncompliance. Accordingly, a relaxation or repeal of these laws and regulations, or changes in governmental policies regarding the funding, implementation, or enforcement of these programs, could result in a decline in demand for environmental services that may have a material adverse effect on our revenue.

Competition Risks

We face increasing competition in the provision of environmental services and waste treatment technologies.

The environmental services and hazardous waste treatment industry is characterized by several large companies and numerous small companies. Any of these companies may possess or develop technologies superior to our technologies. In addition, we compete with companies offering environmental services and hazardous waste treatment technologies alternatives. In our services business, our competitors range from major national and regional environmental service and consulting firms with large environmental services staffs to small local firms. To the extent that our competitors offer more cost-effective management technology alternatives or offer

comparable services at lower prices, our ability to compete effectively could be adversely affected.

Our success depends on attracting and retaining qualified personnel in a competitive environment.

We are dependent upon our ability to attract and retain highly qualified managerial and business development personnel, skilled technical specialists, and experts in a wide range of scientific, engineering, and health and safety fields. Competition for key personnel is intense. We cannot be certain that we will retain our key managerial, business development, and technical personnel or that we will attract or assimilate key personnel in the future. Failure to retain or attract such personnel could materially adversely affect our businesses, financial position, results of operations, and cash flows.

We are also highly dependent upon the technical expertise and management experience of our senior management. The loss of the services of any of these individuals could have a material adverse effect on our results of operations and financial condition. Senior management is not subject to employment agreements. There are no "key man" life insurance policies on any members of senior management or any other personnel.

Other Risks

Certain anti-takeover provisions and potential adverse effect on market price of securities from issuance of preferred stock may limit the ability of security holders to dispose of their shares if the anti-takeover provisions were enacted.

The Company's certificate of incorporation, as amended (the "Certificate of Incorporation"), and by-laws (the "By-laws") contain certain provisions that could have the effect of delaying or preventing a change of control of the Company, which could limit the ability of security holders to dispose of their shares in such transactions. The Certificate of Incorporation authorizes the Board of Directors to issue one or more series of preferred stock without stockholder approval. Such preferred stock could have voting and conversion rights that adversely affect the voting power of the holders of convertible preferred stock or common stock, or could result in one or more classes of outstanding securities that would have dividend, liquidation or other rights superior to those of the convertible preferred stock or common stock. Issuance of such preferred stock may have an adverse effect on the then prevailing market price of the convertible preferred stock or common stock. Additionally, the Company is subject to the anti-takeover provisions of Section 203 of the Delaware general corporate law ("DGCL"), which prohibits the Company from engaging in a "business combination" with an "interested stockholder" for a period of three years after the date of the transaction in which the person became an interested stockholder, unless the business combination is approved in a prescribed manner. Section 203 of the DGCL could have the effect of delaying or preventing a change of control of the Company.

Our charter contains authorized, unissued preferred stock that may inhibit a change of control of our company under circumstances that could give shareholders an opportunity to realize a premium over prevailing market prices of our securities.

Our Certificate of Incorporation and By-Laws contain provisions that could make it more difficult for a third party to acquire the company under circumstances that could give stockholders an opportunity to realize a premium over then-prevailing market prices of our securities. Our Certificate of Incorporation authorizes our Board of Directors to issue preferred stock without stockholder approval and upon terms as it may determine. The rights of holders of our common stock are subject to, and may be adversely affected by, the rights of future holders of preferred stock. In addition, our by-laws require stockholders to provide advance notice to nominate candidates for election as directors and to submit proposals for consideration at stockholder meetings. Section 203 of the Delaware General Corporation Law makes it more difficult for an "interested stockholder" (generally a 15% stockholder) to effect various business combinations with a corporation for a three-year period after the stockholder becomes an "interested stockholder." In general, these provisions may discourage a third party from attempting to acquire our company and, therefore, may inhibit a change of control of our company

The value of our common stock could continue to be volatile.

Our common stock has experienced substantial price volatility. In addition, the stock market has experienced extreme price and volume fluctuations that have affected the market price of many companies and that have often been unrelated to the operating performance of these companies. The overall market and the price of our common stock may continue to fluctuate greatly. The trading price of our common sto