TELKONET INC
Form S-1
August 28, 2003

As filed with the Securities and Exchange Commission on August 28, 2003
Registration No. 333-

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM S-1
REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

TELKONET, INC.
(Exact Name of Registrant as Specified in Its Charter)

UTAH	87-0627421
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

902-A COMMERCE ROAD, ANNAPOLIS, MARYLAND 21401
(410) 897-5900
(Address, Including Zip Code, and Telephone Number, Including Area Code, of Principal Executive Offices)

STEPHEN L. SADLE
CHIEF OPERATING OFFICER
902-A COMMERCE ROAD
ANNAPOLIS, MARYLAND 21401
(Name and Address of Agent for Service)

(410) 897-5900
(Telephone Number, Including Area Code, of Agent for Service)

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copy to:
WILLIAM J. CONTI, ESQ.
BAKER & HOSTETLER LLP
1050 CONNECTICUT AVENUE, NW
SUITE 1100
WASHINGTON, D.C. 20036
202-861-1726
202-861-1783 (FAX)

APPROXIMATE DATE OF COMMENCEMENT OF PROPOSED SALE TO THE PUBLIC: ______________.

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

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

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

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

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

CALCULATION OF REGISTRATION FEE

Title of Securities To Be Registered	Amount To Be Registered	Proposed Maximum Offering Price Per Share	Proposed Maximum Aggregate Offering Price
Common Stock, $0.001 par value	17,353,367	$ 2.77(1)	$ 48,068,826(1)

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

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

PROSPECTUS

TELKONET, INC.

17,353,367 Shares

Common Stock

This prospectus covers 17,353,367 shares of our common stock that may be offered and sold from time to time by the selling stockholders. We will not receive any proceeds from the sale of the shares of our common stock pursuant to this prospectus. We will bear the costs relating to the registration of the shares of our common stock, which we estimate to be approximately $________.

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

Our common stock is traded on the NASDAQ OTC Bulletin Board under the symbol "TLKO.OB." On August 22, 2003, the last reported sale price of our common stock was $2.70.

Investing in shares of our common stock involves risks, including the risk that Telkonet will not be able to continue as a going concern. See "RISK FACTORS" beginning on page 7 of this prospectus.

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

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

The date of this prospectus is August 28, 2003.

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PROSPECTUS SUMMARY

This summary highlights information described more fully elsewhere in this prospectus and may not contain all of the information that may be important to you. You should read this entire prospectus carefully, including the consolidated financial statements and related notes and other financial data included in this prospectus, before making an investment decision. You should also carefully consider the information set forth under "RISK FACTORS" beginning on p. 7.

As used in this prospectus, the terms "we," "us," "our," "our company," and "Telkonet" mean Telkonet, Inc. and our subsidiaries, unless the context otherwise requires.

THE COMPANY

We were formed in 1999 to develop products for use in the powerline communications (PLC) industry. PLC products use existing electrical wiring in commercial buildings and residences to carry high speed data communications signals, including the Internet. Since our formation, we have worked on the development and marketing of our patent-pending PLC technology.

Our PLC technology, the "PlugPlusInternet" product suite, consists of two separate components, the PlugPlusInternet Gateway and the PlugPlusInternet Modem. The PlugPlusInternet Gateway is a modular, self-contained unit that accepts data from an existing network on one port and distributes it via a second port. The Gateway integrates a communications processor that runs a series of proprietary applications under Linux. The signal generated by the Gateway can be directly coupled into low voltage wiring via the power cord of the Gateway. The signal may also be routed to a remote injection point via an inexpensive coaxial cable. This allows the PlugPlusInternet product suite to couple into the medium voltage and multi-phase environments found in commercial buildings. A suite of software applications running on the Gateway can perform communications functions or system management functions. The Gateway is designed to network with dozens of PlugPlusInternet Modems. The PlugPlusInternet Modem is a small, self-contained unit with a standard 110V plug on one side and an Ethernet RJ-45 connector on the other.

The PlugPlusInternet product suite delivers data at speeds in excess of 7 Mega bits per second (Mbps), with burst speeds of 12.6 Mbps. The PlugPlusInternet product suite is installed by connecting an incoming broadband signal (DSL, TL, satellite or cable modem) into the Gateway and connecting the Gateway to a building's electrical panel. Once installed, the Gateway distributes the high-speed Internet signal throughout the entire existing network of electrical wires within the building. The user may access a high-speed Internet signal by plugging the PlugPlusInternet Modem into any electrical outlet and plugging a computer Ethernet connection into the Modem. Multiple personal computers equipped with a PlugPlusInternet Modem can communicate with one another and can share a single broadband resource via the PlugPlusInternet Gateway. Moving the location of a personal computer, server, or printer is accomplished by moving the PlugPlusInternet Modem to another electrical outlet without additional wiring. Our target markets for sales of the PlugPlusInternet product suite include office buildings, hotels, schools, shopping malls, commercial buildings, multi-dwelling units, government facilities, and any other commercial facilities that have a need for Internet access and network connectivity.

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

Telkonet is a Utah corporation with its principal executive offices at 902-A Commerce Road, Annapolis, Maryland 21401. Our telephone number is (410) 897-5900.

THE OFFERING

This prospectus covers up to 17,353,367 shares of our common stock to be sold by the selling stockholders identified in this prospectus. The selling stockholders, or their pledgees, donees, transferees or other successors in interest may, from time to time, sell all or a portion of the shares covered by this prospectus at fixed prices that may be changed, at market prices prevailing

at the time of sale, at prices related to such market prices or at negotiated prices. The selling stockholders may also sell shares of our common stock covered by this prospectus directly to purchasers or may use brokers, dealers, underwriters or agents to sell shares upon terms and conditions that will be described in the applicable prospectus supplement.

From time to time the selling stockholders may be engaged in short sales, short sales against the box, puts and calls and other hedging transactions in our securities to the extent permitted by applicable law and exchange regulations, and may sell and deliver the shares in connection with such transactions or in settlement of securities loans. These transactions may be entered into with broker-dealers or other financial institutions. In addition, from time to time, a selling stockholder may pledge its shares pursuant to the margin provisions of its customer agreements with its broker-dealer. Upon delivery of the shares or a default by a selling stockholder, the broker-dealer or financial institution may offer and sell the pledged shares from time to time. For a more complete description of the offering see "PLAN OF DISTRIBUTION" on p. 47.

USE OF PROCEEDS

All net proceeds from the sale of our common stock by the selling stockholders will go to the selling stockholders and we will not receive any proceeds from the sale of the common stock by the selling stockholders. The proceeds Telkonet receives from the exercise of warrants, the underlying shares of our common stock of which are included in this prospectus, will be used to expand sales and marketing efforts, support strategic partnership programs, build required infrastructure and fund working capital requirements.

SUMMARY FINANCIAL DATA
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

We derived the following historical financial information from the unaudited consolidated financial statements of Telkonet for the six months ended June 30, 2003 and 2002 and the consolidated financial statements of Telkonet for the year ended December 31, 2002, 2001 and 2000 which have been audited by

Russell Bedford Stefanou Mirchandani LLP. Russell Bedford Stefanou Mirchandani LLP's report on our financial statements contained explanatory paragraphs expressing substantial doubt about our ability to continue as a going concern. The unaudited financial data as of and for the six months ended June 30, 2003 and 2002 include adjustments, all of which are normal recurring adjustments, which our management considers necessary for the fair presentation of our results for these unaudited periods. The results of operations for the six months ended June 30, 2003 are not necessarily indicative of the results that may be expected for the full year. Certain reclassifications have been made to conform this data to the current presentation.

(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

(Amounts in thousands, except per share data)	FOR THE SIX MONTHS ENDED JUNE 30, 2003	FOR THE SIX MONTHS ENDED JUNE 30, 2002 (AS RESTATED)	F 2002
STATEMENT OF OPERATIONS DATA:			
Product revenue	$ --	$ --	$ --
Service Revenue	--	--	--
Total net revenue	--	--	--
Cost of products sold	--	--	--
Cost of services sold	--	--	--
Gross profit	--	--	--
Selling, general and administrative expenses	2,063	655	2,875
Management fees	--	--	--
Research and development expenses	598	602	280
Asset impairment charge	--	--	--
Interest income	--	--	--
Interest expense	799	218	626
Interest expense-others	--	--	--
Other income	--	--	(3)
Provision for income taxes	--	--	--
Minority interest share of losses (income)	--	--	--
Net (loss) income	$ (3,460)	$ (1,475)	$ (3,778)
Net (loss) income per common share-basic and diluted	$ (0.22)	$ (0.09)	$ (0.22)
Weighted average common shares outstanding-basic	15,775	17,245	17,120
Weighted average common shares outstanding-diluted			

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(Amounts in thousands)	JUNE 30,	

	2003	2002
BALANCE SHEET DATA:		
Cash and cash equivalents	$ 4,581	$ 19
Property and equipment, net	107	38
Goodwill and other intangibles, net	--	--
Total assets	5,430	295
Long-term debt and notes payable	6,453	863
Total debt	7,752	1,822
Minority interest	--	--
Total stockholders' equity	(2,322)	(1,527)

(Amounts in thousands)	FOR THE SIX MONTHS ENDED JUNE 30,		
	2003	2002 (AS RESTATED)	
OTHER FINANCIAL DATA:			
Depreciation and amortization	$ 82	$ 71	$
Net cash provided by (used in) operating activities	(2,420)	(842)	
Net cash provided by (used in) investing activities	(29)	(19)	
Net cash provided by financing activities	7,011	982	
Capital expenditures	29	19	

Effective January 1, 2002, we adopted Statement of Financial Accounting Standard No. 142, "Goodwill and Other Intangible Assets" (SFAS No. 142). SFAS No. 142 requires that goodwill and certain intangibles no longer be amortized but instead tested for impairment at least annually.

The following table presents the impact of SFAS No. 142 on our summary financial data as indicated:

(Amounts in thousands, except per share data)	FOR THE YEARS ENDED DECEMBER 31,	
	2001 (AS RESTATED)	2000
Net (loss) income:		
Net (loss) income as reported	$ (1,717)	$ (930
Goodwill amortization	--	--
Equity method investment amortization	--	--
Adjusted net (loss) income	$ (1,717)	$ (930

Basic and diluted (loss) income per share:

Net (loss) income per share, basic and diluted, as reported	$ (0.08)	$ (0.04
Goodwill amortization	--	--
Equity method investment amortization	--	--
Adjusted (loss) income per share, basic and diluted	$ (0.08)	$ (0.04

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RISK FACTORS

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

TELKONET'S INDEPENDENT ACCOUNTANTS HAVE EXPRESSED SUBSTANTIAL DOUBTS ABOUT TELKONET'S ABILITY TO CONTINUE AS A GOING CONCERN.

The report of Telkonet's independent accountants contains an explanatory paragraph expressing substantial doubts about Telkonet's ability to continue as a going concern due to the fact that Telkonet has incurred losses since inception. There can be no assurance that Telkonet will ever achieve significant revenues or profitable operations.

TELKONET IS EMERGING FROM ITS DEVELOPMENT STAGE AND HAS NO OPERATING HISTORY ON WHICH TO BASE AN EVALUATION OF ITS CURRENT BUSINESS AND FUTURE PROSPECTS.

Telkonet is emerging from its development stage. As a result, it has no operating history upon which to base an evaluation of its current business and future prospects. The first PlugPlusInternet product was introduced in July 2001. We have not generated substantial revenues. Moreover, we do not currently have any contracts in place that will provide any significant revenue. Because of our lack of an operating history, management has limited insight into trends that may emerge and could materially adversely affect our business. Prospective investors should consider the risks and difficulties our company may encounter in its new and rapidly evolving market, especially given our lack of operating history. These risks include our ability to:

- market the PlugPlusInternet product suite;
- build a customer base;
- generate revenues;
- compete favorably in a highly competitive market;
- access sufficient capital to support growth;
- recruit and retain qualified employees;
- introduce new products and services; and
- build technology and support systems.

WE HAVE A HISTORY OF OPERATING LOSSES AND AN ACCUMULATED DEFICIT AND WE EXPECT TO CONTINUE TO INCUR LOSSES FOR THE FORESEEABLE FUTURE.

Since inception through June 30, 2003, we have incurred cumulative losses of $9,918,391 and have never generated enough funds through our operations to support our business. As of June 30, 2003, we have had no sales of the PlugPlusInternet product suite. We expect to continue to incur substantial operating losses at least through 2003. Our losses to date have resulted principally from:

- research and development costs relating to the development of our PlugPlusInternet product suite;
- costs and expenses associated with manufacturing, distribution and marketing of our products;
- general and administrative costs relating to our operations; and

- interest expense related to our Series A and Series B Debentures and our Senior Notes.

We are currently unprofitable and may never become profitable. Since inception, we have funded our research and development activities primarily from private placements of equity and debt securities, a bank loan and short term loans from certain of our executive officers. As a result of our substantial research and development expenditures and limited product revenues, we have incurred substantial net losses. Our ability to achieve profitability will depend primarily on our ability to successfully commercialize the PlugPlusInternet product suite.

THE TERMS OF OUR SENIOR NOTES SUBJECT US TO THE RISK OF FORECLOSURE ON SUBSTANTIALLY ALL OF OUR ASSETS.

During the second quarter of 2003, we completed an offering of $5,000,000 of Senior Notes. The Senior Notes each accrue interest at 8.0% per annum and mature three years from the date of purchase. Accrued but unpaid interest on the Senior Notes is payable quarterly on January 1, April 1, July 1 and October 1 of each year during the Senior Note term. The Senior Notes are secured by a first priority security interest in all of the intellectual property assets of Telkonet. If an event of default occurs under the Senior Notes, including, but not limited to, the failure by Telkonet to make any required payment to the noteholders when such payment is due, the noteholders may exercise their right to foreclose on all or a portion of our assets used as collateral for the payment of these obligations. Any such default and resulting foreclosure could have a material adverse effect on our financial condition.

The Senior Notes mature three years from the date of issuance, at which time the entire outstanding principal balance of each Senior Note becomes due and payable. We may not have sufficient funds to repay the outstanding balance on the Senior Notes upon their maturity. Accordingly, we may be required to obtain the funds necessary to repay the noteholders through the issuance of additional equity or debt securities or the sale of assets. There can be no assurance that, if needed, we can issue equity or debt securities or sell assets under terms that are acceptable to us or at all. If we are unable to obtain funds to repay this indebtedness, we may be forced to dispose of assets or take other actions on disadvantageous terms, which could result in losses to Telkonet and have a material adverse effect on our financial condition.

POTENTIAL FLUCTUATIONS IN OPERATING RESULTS COULD HAVE A NEGATIVE EFFECT ON THE PRICE OF OUR COMMON STOCK.

Our operating results may fluctuate significantly in the future as a result of a variety of factors, most of which are outside our control, including:

- the level of use of the Internet;
- the demand for high-tech goods;
- the amount and timing of capital expenditures and other costs relating to the expansion of our operations;
- price competition or pricing changes in the industry;
- technical difficulties or system downtime;

- economic conditions specific to the internet and communications industry; and
- general economic conditions.

Our quarterly results may also be significantly impacted by the impact of the accounting treatment of acquisitions, financing transactions or other matters. Such accounting treatment could have a material impact on the results for any quarter and have a negative impact on the price of our common stock.

THERE IS PRESENTLY A LIMITED TRADING MARKET FOR SHARES OF OUR COMMON STOCK.

Our common stock is traded on the OTC Bulletin Board. Stocks that trade on the OTC Bulletin Board tend to be less liquid and trade with larger spreads between the bid and ask price than stocks on larger exchanges or automated quotation systems. Information with respect to OTC Bulletin Board quotations reflects inter-dealer prices without retail markup, markdown or commission and may not represent actual transactions, and quotations on the OTC Bulletin Board are sporadic. This means that shares of our common stock are less liquid than shares of companies traded on larger exchanges or automated quotation systems and, as a result, holders of our common stock may have some difficulty selling their shares in the open market.

In addition, our stock is subject to what are known as the "penny stock" rules. The "penny stock" rules place additional requirements on broker-dealers who sell or make a market in such securities. Consequently, the ability or willingness of broker-dealers to sell or make a market in our common stock could be impacted and your ability to resell your shares, and the price at which you could sell your shares, could be adversely affected.

OUR DIRECTORS AND EXECUTIVE OFFICERS OWN A SUBSTANTIAL PERCENTAGE OF OUR ISSUED AND OUTSTANDING COMMON STOCK. THEIR OWNERSHIP COULD ALLOW THEM TO EXERCISE SIGNIFICANT CONTROL OVER CORPORATE DECISIONS.

As of June 30, 2003, our officers and directors owned 49.2% of our common stock. This means that our officers and directors, as a group, exercise significant control over matters upon which our stockholders may vote, including the selection of the Board of Directors, mergers, acquisitions and other significant corporate transactions.

FURTHER ISSUANCES OF EQUITY SECURITIES MAY BE DILUTIVE TO CURRENT STOCKHOLDERS.

During the third quarter of 2001, we commenced an offering of up to $1,689,100 principal amount of Series A Debentures. In connection with the placement of the Series A Debentures, we also issued non-detachable warrants granting holders the right to acquire 1,689,100 shares of our common stock at $1.00 per share. The Series A Debentures are convertible into, and the warrants are exerciseable for, the shares of our common stock that are included in the registration statement of which this prospectus forms a part. As of the date of this prospectus, 3,378,200 shares of our common stock have been issued in connection with the conversion of the Series A Debentures.

During the fourth quarter of 2002, we commenced an offering of up to $2,500,000 principal amount of Series B Debentures. In connection with the placement of the Series B Debentures, we also issued non-detachable warrants granting holders the right to acquire 2,500,000 shares of our common stock at $1.00 per share. The Series B Debentures are convertible into, and the warrants are exerciseable for, the shares of our common stock that are included in the registration statement of which this prospectus forms a part. As of the date of this prospectus, 4,545,455 shares of our common stock have been issued in connection with the conversion of the Series B Debentures.

During the second quarter of 2003, we commenced an offering of up to $5,000,000 principal amount of Senior Notes. The Senior Notes each accrue interest at 8.0% per annum, mature three years from the date of purchase and are secured by a first priority security interest in all of the intellectual property assets of Telkonet. In connection with the placement of the Senior Notes, we also issued non-detachable warrants granting holders the right to acquire 6,250,000 shares of our common stock at $1.00 per share. The warrants issued in connection with the Senior Note offering are exerciseable for the shares of our common stock that are the subject of the registration statement of which this prospectus forms a part.

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

THE EXERCISE OF OPTIONS AND WARRANTS OUTSTANDING AND AVAILABLE FOR ISSUANCE MAY ADVERSELY AFFECT THE MARKET PRICE OF OUR COMMON STOCK.

As of June 30, 2003, we had outstanding options to purchase a total of 10,336,667 shares of common stock at exercise prices ranging from $1.00 to $3.43 per share, with a weighted average exercise price of $1.08. As of June 30, 2003, we had warrants outstanding to purchase a total of 12,123,260 shares of common stock at exercise prices ranging from $0.50 to $2.97 per share, with a weighted average exercise price of $0.96. In addition, as of June 30, 2003, we had 4,663,333 additional shares of common stock which may be issued in the future under the Telkonet, Inc. Stock Incentive Plan. The exercise of outstanding options and warrants and the sale in the public market of the shares purchased upon such exercise will be dilutive to existing stockholders and could adversely affect the market price of our common stock.

THE POWERLINE COMMUNICATIONS INDUSTRY IS INTENSELY COMPETITIVE AND RAPIDLY EVOLVING.

We operate in a highly competitive, quickly changing environment, and our future success depends on our ability to develop and introduce new products and product enhancements that achieve broad market acceptance in commercial and governmental sectors. Our future success will depend, in large part, upon our ability to identify demand trends in the commercial and governmental sectors and quickly develop, manufacture and sell products that satisfy these demands in a cost effective manner. We will also need to respond effectively to new product announcements by our competitors by quickly introducing competitive products.

Delays in product development and introduction could result in:

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

GOVERNMENT REGULATION OF OUR PRODUCTS COULD IMPAIR OUR ABILITY TO SELL SUCH PRODUCTS IN CERTAIN MARKETS.

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

PRODUCTS SOLD BY OUR COMPETITORS COULD BECOME MORE POPULAR THAN OUR PRODUCTS OR RENDER OUR PRODUCTS OBSOLETE.

The market for powerline communications products is highly competitive. Although we are presently the only company marketing PLC products to the commercial segment, Linksys Group, Inc. (recently acquired by Cisco Systems) and Netgear, Inc. offer similar PLC solutions for the residential market. There can be no assurance that Linksys Group, Netgear or any other company will not develop PLC products that compete with our products in the future. These potential competitors have longer operating histories, greater name recognition and substantially greater financial, technical, sales, marketing and other resources. These potential competitors may, among other things, undertake more extensive marketing campaigns, adopt more aggressive pricing policies, obtain more favorable pricing from suppliers and manufacturers and exert more influence on the sales channel than we can. As a result, we may not be able to compete successfully with these potential competitors and these potential competitors may develop or market technologies and products that are more widely accepted than those being developed by us or that would render our products obsolete or noncompetitive. We anticipate that potential competitors will also intensify their efforts to penetrate our target markets. These potential competitors may have more advanced technology, more extensive distribution channels, stronger brand names, bigger promotional budgets and larger customer bases than we do. These companies could devote more capital resources to develop, manufacture and market competing products than we could. If any of these companies are successful in competing against us, our sales could decline, our margins could be negatively impacted, and we could lose market share, any of which could seriously harm our business and results of operations.

THE FAILURE OF THE INTERNET TO CONTINUE AS AN ACCEPTED MEDIUM FOR BUSINESS COMMERCE COULD HAVE A NEGATIVE IMPACT ON OUR RESULTS OF OPERATIONS.

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

adoption of new standards and protocols to handle increased levels of Internet activity or increased governmental regulation could slow or stop the growth of the Internet as a viable medium for business commerce. Moreover, critical issues concerning the commercial use of the Internet (including security, reliability, accessibility and quality of service) remain unresolved and may adversely affect the growth of Internet use or the attractiveness of its use for business commerce. The failure of the necessary infrastructure to further develop in a timely manner or the failure of the Internet to continue to develop rapidly as a valid medium for business would have a negative impact on our results of operations.

FAILURE OF OUR SERVICES AND PRODUCTS TO BE SUCCESSFUL IN THE MARKETPLACE COULD HAVE A NEGATIVE EFFECT ON OUR RESULTS OF OPERATIONS.

Since we are just emerging from our development stage, we do not know with any certainty whether our services and/or products will be accepted within the business marketplace. If our services and/or products prove to be unsuccessful within the marketplace, or if we fail to attain market acceptance, it could have a negative effect on our results of operations.

WE MAY NOT BE ABLE TO OBTAIN PATENTS, WHICH COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR BUSINESS.

Our ability to compete effectively in the powerline technology industry will depend on our success in acquiring suitable patent protection. We currently have several patents pending. We intend to file additional patent applications that we deem to be economically beneficial. If we are not successful in obtaining patents, we will have limited protection against those who might copy our technology. As a result, the failure to obtain patents could negatively impact our business and results of operations.

INFRINGEMENT BY THIRD PARTIES ON OUR PROPRIETARY TECHNOLOGY AND DEVELOPMENT OF SUBSTANTIALLY EQUIVALENT PROPRIETARY TECHNOLOGY BY OUR COMPETITORS COULD NEGATIVELY IMPACT OUR BUSINESS.

Our success depends partly on our ability to maintain patent and trade secret protection, to obtain future patents and licenses, and to operate without infringing on the proprietary rights of third parties. There can be no assurance that the measures we have taken to protect our intellectual property, including those integrated to our PlugPlusInternet product suite, will prevent misappropriation or circumvention. In addition, there can be no assurance that any patent application, when filed, will result in an issued patent, or that our existing patents, or any patents that may be issued in the future, will provide us with significant protection against competitors. Moreover, there can be no assurance that any patents issued to, or licensed by, us will not be infringed upon or circumvented by others. Infringement by third parties on our proprietary technology could negatively impact our business. Moreover, litigation to establish the validity of patents, to assert infringement claims against others, and to defend against patent infringement claims can be expensive and time-consuming, even if the outcome is in our favor. We also rely to a lesser extent on unpatented proprietary technology, and no assurance can be given that others will not independently develop substantially equivalent proprietary information, techniques or processes or that we can meaningfully protect our rights to such unpatented proprietary technology. Development of substantially equivalent technology by our competitors could negatively impact our business.

WE DEPEND ON A SMALL TEAM OF SENIOR MANAGEMENT, AND WE MAY HAVE DIFFICULTY ATTRACTING AND RETAINING ADDITIONAL PERSONNEL.

Our future success will depend in large part upon the continued services and performance of senior management and other key personnel. If we lose the services of any member of our senior management team, our overall operations could be materially and adversely affected. In addition, our future success will depend on our ability to identify, attract, hire, train, retain and motivate other highly skilled technical, managerial, marketing, purchasing and customer service personnel when they are needed. Competition for these individuals is intense. We cannot ensure that we will be able to successfully attract, integrate or retain sufficiently qualified personnel when the need arises. Any failure to attract and retain the necessary technical, managerial, marketing, purchasing and customer service personnel could have a negative effect on our financial condition and results of operations.

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FORWARD-LOOKING STATEMENTS

This prospectus and any prospectus supplement may contain "forward-looking statements" which represent our expectations or beliefs, including, but not limited to, statements concerning industry performance and our results, operations, performance, financial condition, plans, growth and strategies, which include, without limitation, statements preceded or followed by or that include the words "may," "will," "expect," "anticipate," "intend," "could," "estimate," or "continue" or the negative or other variations thereof or comparable terminology. Any statements contained in this prospectus, any prospectus supplement or the information incorporated by reference that are not statements of historical fact may be deemed to be forward-looking statements within the meaning of Section 27(A) of the Securities Act of 1933 and Section 21(F) of the Securities Exchange Act of 1934. For such statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. These statements by their nature involve substantial risks and uncertainties, some of which are beyond our control, and actual results may differ materially depending on a variety of important factors, many of which are also beyond our control. You should not place undue reliance on these forward-looking statements, which speak only as of the date of this prospectus. We do not undertake any obligation to update or release any revisions to these forward-looking statements to reflect events or circumstances after the date of this prospectus or to reflect the occurrence of unanticipated events, except to the extent such updates and/or revisions are required to prevent these forward-looking statements from being materially false or misleading.

THE COMPANY

We were formed in 1999 to develop products for use in the powerline communications (PLC) industry. PLC products use existing electrical wiring in commercial buildings and residences to carry high speed data communications signals, including the Internet. Since our formation, we have worked on the development and marketing of our patent-pending PLC technology.

Our PLC technology, the "PlugPlusInternet" product suite, consists of two separate components, the PlugPlusInternet Gateway and the PlugPlusInternet Modem. The PlugPlusInternet Gateway is a modular, self-contained unit that accepts data from an existing network on one port and distributes it via a second port. The Gateway integrates a communications processor that runs a series of proprietary applications under Linux. The signal generated by the Gateway can be directly coupled into low voltage wiring via the power cord of the Gateway. The signal may also be routed to a remote injection point via an inexpensive coaxial cable. This allows the PlugPlusInternet product suite to couple into the medium voltage and multi-phase environments found in commercial buildings. A suite of software applications running on the Gateway can perform communications functions or system management functions. The Gateway is designed to network with dozens of PlugPlusInternet Modems. The PlugPlusInternet Modem is a small, self-contained unit with a standard 110V plug on one side and an Ethernet RJ-45 connector on the other.

The PlugPlusInternet product suite delivers data at speeds in excess of 7 Mega bits per second (Mbps), with burst speeds of 12.6 Mbps. The PlugPlusInternet product suite is installed by connecting an incoming broadband signal (DSL, TL, satellite or cable modem) into the Gateway and connecting the Gateway to a building's electrical panel. Once installed, the Gateway distributes the high-speed Internet signal throughout the entire existing network of electrical wires within the building. The user may access a high-speed Internet signal by plugging the PlugPlusInternet Modem into any electrical outlet and plugging a computer Ethernet connection into the Modem. Multiple personal computers equipped with a PlugPlusInternet Modem can communicate with one another and can share a single broadband resource via the PlugPlusInternet Gateway. Moving the location of a personal computer, server, or printer is accomplished by moving the PlugPlusInternet Modem to another electrical outlet without additional wiring. Our target markets for sales of the PlugPlusInternet product suite include office buildings, hotels, schools, shopping malls, commercial buildings, multi-dwelling units, government facilities, and any other commercial facilities that have a need for Internet access and network connectivity.

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

In July 2001, we announced the completion of our initial product development phase of the PlugPlusInternet product suite and, in August 2001, we announced that successful system tests of the PlugPlusInternet product suite had been performed.

In January 2002, we shifted our management emphasis from research and development to sales and marketing of the PlugPlusInternet product suite.

In November 2002, we successfully installed a PlugPlusInternet system at the historic Partridge Inn in Augusta, Georgia. The installation provided high-speed Internet connectivity to guest rooms, meeting rooms and a lobby kiosk. In December 2002, we conducted a product field trial at the Marriott Residence Inn-Landfall in Wilmington, NC. As part of this trial, we implemented a hotel-wide PlugPlusInternet system that provided connectivity to the hotel's 90 guest rooms, meeting rooms, common areas and a lobby kiosk.

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

In March 2003, we entered into a Strategic Alliance Agreement with Choice Hotels International (NYSE: CHH), one of the largest hotel franchise companies in the world with more than 3,500 hotels, inns, all-suite hotels and resorts open and under development in 46 countries under the Comfort Inn, Comfort Suites, Quality, Clarion, Sleep Inn, Rodeway Inn, EconoLodge and MainStay Suites brand names. The agreement has an initial term of two years, pursuant to which we will become a Choice Hotels-endorsed vendor offering the PlugPlusInternet product suite to Choice Hotels' U.S. franchisees. Choice Hotel franchisees that participate in our "Early Adopter Program" will receive a discount on installation and maintenance of the PlugPlusInternet product suite.

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

Telkonet is a Utah corporation with its principal executive offices at 902-A Commerce Road, Annapolis, Maryland 21401. Our telephone number is (410) 897-5900.

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COMPETITION

The market for powerline communications is highly competitive. Although we are presently the only company marketing PLC products to the commercial segment, Linksys Group, Inc. (recently acquired by Cisco Systems) and Netgear, Inc. offer similar PLC solutions for the residential market. There can be no assurance that Linksys Group, Netgear or any other company will not develop PLC products that compete with our products in the future. These potential competitors have longer operating histories, greater name recognition and substantially greater financial, technical, sales, marketing and other resources. These potential competitors may, among other things, undertake more extensive marketing campaigns, adopt more aggressive pricing policies, obtain more favorable pricing from suppliers and manufacturers and exert more influence on the sales channel than we can. As a result, we may not be able to compete successfully with these potential competitors and these potential competitors may develop or market technologies and products that are more widely accepted than those being developed by us or that would render our products obsolete or noncompetitive.

We anticipate that potential competitors will also intensify their efforts to penetrate our target markets. These potential competitors may have more advanced technologies, more extensive distribution channels, stronger brand names, bigger promotional budgets and larger customer bases than we do. These companies could devote more capital resources to develop, manufacture and market competing products than we could.

RAW MATERIALS

We have not experienced any significant or unusual problems in the purchase of raw materials or commodities. While we are dependent, in certain situations, on a limited number of vendors to provide certain raw materials and components, we have not experienced significant problems or issues procuring any essential materials, parts or components. We obtain the majority of our raw materials from the following suppliers: Arrow Electronics, Inc., Avnet Electronics Marketing, Digi-Key Corporation, Intellon Corporation and Superior Manufacturing Services.

PATENTS AND TRADEMARKS

We have various patents pending which we consider in the aggregate to constitute a valuable asset. These pending patents cover various technologies incorporated to our PlugPlusInternet product suite, including components enabling the use of electric utility power lines as a telephonic communications carrier network. We believe several of our pending patents offer us a significant competitive advantage. We are not presently a party to any license agreements.

MANUFACTURING AND INSTALLATION METHODS

Telkonet sources its own raw material components and utilizes contract manufacturers for assembly and testing of its products. Our finished product is distributed directly from Telkonet to the customer. On July 23, 2003, Telkonet executed an agreement with CompuCom Systems, Inc. pursuant to which CompuCom has agreed to provide installation and customer support services for the PlugPlusInternet product suite. Telkonet is not presently a party to any third party distribution agreement.

RESEARCH AND DEVELOPMENT

During the six months ended June 30, 2003 and for the year ended December 31, 2002, we spent $597,550 and $280,450, respectively, on research and development activities relating to the development of new products or improvements of existing products. We spent $120,828 in 2001 (as restated) and $119,000 in 2000 on research and development activities.

MAJOR CUSTOMERS

Telkonet has just emerged from its development stage and, as of the date of this prospectus, has not had significant sales of its products or services.

ENVIRONMENTAL MATTERS

We do not anticipate any material effect on our capital expenditures, earnings or competitive position due to compliance with government regulations involving environmental matters.

SEASONALITY

We do not consider our business to be seasonal.

EMPLOYEES

As of June 30, 2003, we had 17 full time employees. The hiring of additional key staff is planned in the areas of business development, sales and marketing, engineering and support. We believe our relations with our employees are good.

GOVERNMENT REGULATION

We are subject to regulation in the United States by the Federal Communications Commission (FCC). We are also may be subject to regulation by government entities in other countries.

UNITED STATES REGULATION

FCC rules permit the operation of unlicensed digital devices that radiate radio frequency emissions if the manufacturer complies with certain equipment authorization procedures, technical requirements, marketing restrictions and product labeling requirements. Differing technical requirements apply to "Class A" devices intended for use in commercial settings and more stringent standards apply to "Class B" devices intended for residential use. An independent, FCC-certified testing lab has verified that our PlugPlusInternet Gateways comply with the FCC technical requirements for Class A and Class B digital devices. No further testing of these devices is required and the devices may be manufactured and marketed for commercial and residential use. Additional devices designed by us for commercial and residential use will be subject to the FCC rules for unlicensed digital devices. Moreover, if in the future, the FCC changes its technical requirements for unlicensed digital devices, further testing and/or modifications of devices may be necessary.

REGULATION ABROAD

Our products will be subject to compliance with applicable regulatory requirements in those foreign countries where our products are sold.

PROPERTY

We currently lease approximately 3,000 square feet office space at 902A Commerce Drive, Annapolis, Maryland 21401, where we maintain our principal business office.

We consider this property to be suitable and adequate for its present purposes, well maintained and in good operating condition.

LEGAL PROCEEDINGS

In March 2003, Jenson Services, Inc. and James P. Doolin filed an action against Telkonet in the Third Judicial District Court in and for Salt Lake County, State of Utah. The action sets forth various counts all based on allegations that Telkonet, through its agents, promised to undertake a registration of certain shares of Telkonet common stock owned by plaintiffs. The action seeks damages from Telkonet in unspecified amounts. Telkonet believes that plaintiffs' claims are without merit and that Telkonet has meritorious defenses to such claims. Telkonet intends to vigorously defend itself against the plaintiffs' claims in their entirety.

MARKET PRICE OF AND DIVIDENDS ON OUR COMMON STOCK AND RELATED STOCKHOLDER MATTERS

Our common stock is quoted on the OTC Bulletin Board (OTCBB) under the symbol "TLKO.OB." The following table shows the high and low sales prices for our common stock as quoted on the OTCBB for the periods indicated. On August 22, 2003, the last reported sale price of our common stock was $2.70. As of August

22, 2003, there were 24,011,065 shares of our common stock issued and outstanding.

	HIGH	LOW
YEAR ENDED DECEMBER 31, 2003		
First Quarter	$ 1.33	$ 1.18
Second Quarter	$ 2.67	$ 2.43
YEAR ENDED DECEMBER 31, 2002		
First Quarter	$ 0.87	$ 0.87
Second Quarter	$ 1.53	$ 1.40
Third Quarter	$ 1.08	$ 0.98
Fourth Quarter	$ 0.62	$ 0.56
YEAR ENDED DECEMBER 31, 2001		
First Quarter	$ 1.98	$ 1.98
Second Quarter	$ 1.06	$ 1.00
Third Quarter	$ 0.84	$ 0.83
Fourth Quarter	$ 0.95	$ 0.95
YEAR ENDED DECEMBER 31, 2000		
Third Quarter	$ 1.74	$ 1.29
Fourth Quarter	$ 4.08	$ 3.54

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

CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

During our two most recent fiscal years and the subsequent interim periods, no independent accountant that was previously engaged as the principal accountant to audit our financial statements resigned, indicated that it declined to stand for re-election or was dismissed by us.

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QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are presently engaging in marketing our products in Canada and contemplate future sales in various regions of the world. In connection with these foreign marketing and sales activities, we may export to and import from other countries. Our operations may, therefore, be subject to volatility because of currency fluctuations, inflation and changes in political and economic conditions in these countries. Sales and expenses may be denominated in local currencies and may be affected as currency fluctuations affect our product prices and operating costs or those of our competitors.

We presently do not use any derivative financial instruments to hedge our exposure to adverse fluctuations in interest rates, foreign exchange rates, fluctuations in commodity prices or other market risks, nor do we invest in speculative financial instruments.

Due to the nature of our borrowings, we have concluded that there is no material market risk exposure and, therefore, no quantitative tabular disclosures are required.

EXECUTIVE OFFICERS AND DIRECTORS

GENERAL

The following table furnishes the information concerning Telkonet's executive officers and directors as of June 30, 2003:

Name	Age	Title
Ronald W. Pickett	55	President & Director
Stephen Sadle	56	Chief Operating Officer & Director
E. Barry Smith	52	Chief Financial Officer
James Landry	49	Vice President, Engineering
Robert P. Crabb	55	Secretary
Warren V. Musser	76	Chairman of the Board
A. Hugo DeCesaris	44	Director
David W. Grimes	65	Director

RONALD W. PICKETT, President and Director, fostered the development of Telkonet since 1999 as Telkonet's principal investor and co-founder. He also was the founder, and for twenty years served as Chairman of the Board of Directors and President, of Medical Advisory Systems, Inc., which is now named Digital Angel Corporation (AMEX: "DOC"). A graduate of Gordon College, Mr. Pickett has engaged in various entrepreneurial activities for 35 years.

STEPHEN L. SADLE, Director and Chief Operating Officer, is a co-founder of Telkonet. From 1970 to 1986 Mr. Sadle was president of a successful infrastructure construction and development company in the Washington, D.C. metro area. From 1986 to 1999, he was Vice President of Business Development and Sales for The Driggs Corporation, a major heavy and infrastructure firm interfacing with both government and the private sectors. From 1999 to 2000, Mr. Sadle was Vice President and General Sales Manager of Internos, a provider of web-based vertical intranet applications, and developed operating extranets in the transportation and construction industries.

E. BARRY SMITH, Chief Financial Officer, is a CPA and senior financial executive with diversified experience in both public and private companies. Mr. Smith's background includes big-four public accounting experience with the firm of Deloitte & Touche, Senior Financial Partner with over 15 years executive management experience with Safeguard Scientifics, Inc. and their partner companies including: ThinAirApps, Inc. (Wireless Application Provider-sold to Palm, Inc.) and Tangram Enterprise Solutions (Software/Hardware for PC/LAN Mainframe Connectivity and Enterprise Software Management). Mr. Smith's experience also includes, Vice President of Finance & Administration for US Golf Management (Public/Private Golf Course & Restaurant Management), Vice President of Finance for International Communications Research (Market Research & Database Services) and Treasurer for The Chilton Company (Publishing).

JAMES LANDRY, Vice President, Engineering, has over 18 years experience in developing communications hardware for the enterprise/carrier market with 3Com, US Robotics, Penril Datacomm and Data General. While at 3Com/US Robotics, he was singularly responsible for the development of the xDSL product line as well as a number of modems and interface cards. At Penril, he served as the product development leader for the Series 1544 multiplexer/channel bank and at Data General he was technical leader of system integration for ISDN WAN. Mr. Landry brings a wealth of practical design leadership and a solid history of delivering products to the marketplace. He holds four United States patents.

ROBERT P. CRABB, Secretary, has over 35 years of sales, marketing and corporate management experience, including a career in sales and management with the Metropolitan Life Insurance Company. His entrepreneurial expertise also includes public company administration, financial consulting and commercial/residential real estate development. Mr. Crabb oversees Telkonet's public company administration and corporate governance, is a former Director of Telkonet and has been involved with Telkonet since 1999.

WARREN V. MUSSER, Chairman of the Board of Directors, has had extensive experience with public companies during his distinguished and successful career as an entrepreneur. A partial list of his accomplishments includes: Chairman Emeritus, Safeguard Scientifics, Inc. (formerly Safeguard Industries, Inc.), Chairman of the Board and Chief Executive Officer, Safeguard Scientifics, Inc., Founder, Chairman of the Board and President, Lancaster Corporation (became Safeguard Industries, Inc.), Founder & President, Musser and Company, Inc. (Investment Banking Firm). In addition, Mr. Musser is a Director of CompuCom Systems, Inc. and Internet Capital Group, Inc., Vice Chairman of Nutri/System, Inc. and Eastern Technology Council and Chairman of Economics, PA. He also serves as the Vice President/Development, Cradle of Liberty Council of the Boy Scouts of America.

A. HUGO DECESARIS, Director, has over 25 years experience in the homebuilding industry with Washington Homes, Inc., where he served as Vice President and a member of the Board of Directors. In January of 2001, Washington Homes, Inc. became a wholly-owned subsidiary of K. Hovnanian Enterprises, Inc. and is now one of the top ten homebuilders in the nation. Mr. DeCesaris is currently the Regional Vice President for the Maryland Division of Washington Homes, Inc., President and owner of Southern Maryland's largest Marina and a member of the Board of Directors of MNCBIA Volume Builders Council.

DAVID W. GRIMES, Director, is a co-founder of Telkonet. From 1963 to 1982, Mr. Grimes was a senior executive with NASA, heading the $200 million per year Delta Program. He also was founder, and from 1982 to 1989 served as Chief Executive Officer, of Transpace Carriers Inc., a venture to commercialize the Delta launch vehicle. From 1989 to 1992, he was the Engineering Division

Director at EER Inc., with supervisory responsibility for more than 100 engineers and technicians on electrical mechanical and thermal tasks for Goddard Space Flight Center. From 1992 to 1999, Mr. Grimes served as Chief Engineer for Final Analysis, Inc. and led the design and development of the Low Earth Orbit constellation of 38 satellites for use in global store and forward communications. Mr. Grimes is a recognized expert in space and ground communications systems.

EXECUTIVE COMPENSATION

SUMMARY COMPENSATION TABLE

The following table sets forth information concerning the annual and long-term compensation for services in all capacities to Telkonet for the fiscal year ended December 31, 2002 for each of the three highest paid persons who are officers or directors of Telkonet.

NAME AND	BASE	OTHER ANNUAL

PRINCIPAL POSITION	YEAR	SALARY($)	BONUS ($)	COMPENSATION($
	2000	$ 76,747	$ 0	$ 0
Peter Larson (1)	2001	$ 160,484	$ 0	$ 0
Chief Executive Officer	2002	$ 4,000	$ 0	$ 0
	2000	$ 0	$ 0	$ 0
J. Gregory Fowler (2)	2001	$ 0	$ 0	$ 0
Chief Executive Officer	2002	$ 114,000	$ 0	$ 0
	2000	$ 0	$ 0	$ 0
David S. Yaney (3)	2001	$ 0	$ 0	$ 0
Chief Technology Officer	2002	$ 73,000	$ 0	$ 0
	2000	$ 0	$ 0	$ 0
James Landry	2001	$ 29,000	$ 0	$ 0
Vice President, Engineering	2002	$ 116,000	$ 0	$ 0
	2000	$ 78,270	$ 0	$ 0
Stephen L. Sadle	2001	$ 160,484	$ 0	$ 0
Chief Operating Officer	2002	$ 130,000	$ 0	$ 0

(1) Mr. Larson resigned as Chief Executive Officer of Telkonet on January 12, 2002.

(2) On January 30, 2002, Mr. Fowler was appointed Chief Executive Officer of Telkonet. Mr. Fowler resigned as Chief Executive Officer of Telkonet on December 12, 2002.

(3) Dr. Yaney was appointed Chief Technology Officer of Telkonet on February 15, 2002. Dr. Yaney resigned as Chief Technology Officer of Telkonet on September 3, 2002.

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OPTION/SAR GRANTS

The following table sets forth information concerning stock options granted in the fiscal year ended December 31, 2002, to the persons listed on the Summary Compensation Table.

NAME	NUMBER OF SECURITIES UNDERLYING OPTIONS/SARS GRANTED	PERCENT OF TOTAL OPTIONS/SARS GRANTED TO EMPLOYEE IN FISCAL YEAR	EXERCISE OF BASE PRICE ($/SH)
Peter Larson	0	0	$ 0
J. Gregory Fowler	650,000 (1)	22.9%	$ 1.00
David S. Yaney	400,000	14.1%	$ 1.00
James Landry	100,000	3.5%	$ 1.00

Stephen L. Sadle	1,000,000	35.5%	$ 1.00

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(1) This includes 450,000 shares of our common stock subject to purchase pursuant to options that were forfeited by Mr. Fowler upon his resignation on December 12, 2002.

AGGREGATED OPTION/SAR EXERCISES

The following table summarizes information relating to stock option exercises during the year ended December 31, 2002 by those persons listed on the Summary Compensation Table.

AGGREGATE OPTION EXERCISES IN 2002 AND
OPTION VALUES AS OF DECEMBER 31, 2002

NAME	SHARES ACQUIRED ON EXERCISE	VALUE REALIZED	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS AT DECEMBER 31, 2002		VALUE OF U DECE
			EXERCISABLE	UNEXERCISABLE	EXERCISA
Peter Larson	0	$ 0	0	0	$ 0
J. Gregory Fowler	0	$ 0	200,000	0	$ 0
David S. Yaney	0	$ 0	50,000	0	$ 0
James Landry	0	$ 0	78,845	0	$ 0
Stephen L. Sadle	1,000,000(2)	$ 8,330	0	0	$ 0

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(1) Based on a stock price of $0.55, which was the average of the high asked and low bid prices reported on December 31, 2002.

(2) Mr. Sadle sold 166,600 shares in a private sale in 2002 and returned the remaining 833,400 shares to the Company as part of a recapitalization. See, "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS" on page 25 of this prospectus.

DIRECTORS' COMPENSATION

Telkonet reimburses directors for costs and expenses in connection with their attendance and participation at Board of Directors meetings and for other travel expenses incurred on Telkonet's behalf. Telkonet has the authority to compensate each non-management director $250.00 for each meeting of the Board of Directors. As of the date of this prospectus, no such payments have been made.

In January 2003, options to purchase the following number of shares were granted to the following non-employee directors of Telkonet under the Stock Incentive Plan: David Grimes (900,000 shares) and Warren Musser (2,000,000 shares). These options entitle the holder to purchase shares of Telkonet common stock at $1.00 per share and vest ratably over twelve quarters beginning January 1, 2003. These options are not "incentive stock options" within the meaning of Section 422 of the Internal Revenue Code of 1986. Approval of the grant of these options will be submitted to Telkonet's stockholders at the 2003 annual meeting of stockholders.

EMPLOYMENT AGREEMENTS

Peter Larson, former Chief Executive Officer, was employed pursuant to an employment agreement for a three-year term that commenced June 19, 2000 and provided for an annual salary of $130,000 and bonuses and benefits based upon Telkonet's internal policies. Mr. Larson resigned from his employment on January 12, 2002.

Mr. Sadle, Chief Operating Officer, is employed pursuant to an employment agreement for a three-year term that commenced June 19, 2000 and provides for an annual salary of $130,000 and bonuses and benefits based upon Telkonet's internal policies. On April 24, 2002, Mr. Sadle's employment agreement was amended to, among other things, extend the term through December 31, 2004. On January 18, 2003, Telkonet and Mr. Sadle executed a new employment agreement, the terms of which superceded the terms of the April 24, 2002 amended employment agreement. The January 18, 2003 employment agreement has a term of three years and provides for an annual salary of $130,000 and bonuses and benefits based upon Telkonet's internal policies.

Mr. Fowler, former Chief Executive Officer, was employed pursuant to an employment agreement for a three-year term that commenced January 30, 2002 and provided for an annual salary of $130,000 and bonuses and benefits based upon Telkonet's internal policies. Mr. Fowler resigned effective December 12, 2002.

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David S. Yaney, former Chief Technology Officer, was employed pursuant to an employment agreement for a three-year term that commenced February 15, 2002 and provided for an annual salary of $130,000 and bonuses and benefits based upon Telkonet's internal policies. Dr. Yaney resigned effective September 3, 2002.

Mr. Landry, Vice President--Engineering, has been employed since September 24, 2001 with an annual salary of $160,000 with bonuses and benefits based upon Telkonet's internal policies.

Mr. Crabb, corporate secretary, is employed pursuant to an employment agreement for a three year term that commenced January 18, 2003 and provides for an annual salary of $120,000 and bonuses and benefits based upon Telkonet's internal policies.

Mr. Pickett, President, is employed pursuant to an employment agreement for an unspecified term that commenced January 30, 2003 and provides for an annual salary $100,000, 3,000 shares of our common stock per month for each month of his employment and bonuses and benefits based upon Telkonet's internal policies.

Mr. Smith, Chief Financial Officer, is employed pursuant to an employment agreement for a one-year term that commenced February 17, 2003 and provides for an annual salary of $130,000 and bonuses and benefits based upon Telkonet's internal policies.

Mr. Lubert, former Chief Executive Officer, was employed pursuant to an employment agreement for a two-year term that commenced January 1, 2003 and provided for an annual salary of $130,000 and bonuses and benefits based upon

Telkonet's internal policies. Mr. Lubert resigned effective June 16, 2003, however, Telkonet has agreed to pay Mr. Lubert's salary through December 17, 2004.

In addition, under the Stock Incentive Plan, stock options are periodically granted to employees at the discretion of the Board of Directors. Executives of Telkonet are eligible to receive stock option grants, based upon individual performance and the performance of Telkonet as a whole.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

Telkonet presently does not have any committees of the Board of Directors. However, on August 12, 2003 the Board of Directors voted unanimously to expand our Board of Directors to seven. The Board of Directors is presently considering candidates for appointment to these vacant board seats. We intend that these new directors will be "independent" as such term is defined by Rule 4200(a)(14) of the Rules of the National Association of Securities Dealers. Once appointed, each independent director will serve until the next annual meeting of our stockholders and his successor is duly elected and qualified.

SECURITY OWNERSHIP OF MANAGEMENT
AND CERTAIN BENEFICIAL OWNERS

The following table sets forth, as of August 22, 2003, the number of shares of Telkonet's common stock beneficially owned by each director and executive officer of Telkonet, by all directors and executive officers as a group, and by each person known by Telkonet to own beneficially more than 5.0% of the outstanding common stock.

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BENEFICIAL OWNER (1)	SHARES BENEFICIALLY OWNED	PERCENT OF CL
Howard Lubert 435 Devon Park Drive Building 500 Wayne, PA 19087	83,333 (2)	
E. Barry Smith 435 Devon Park Drive Building 500 Wayne, PA 19087	87,501 (3)	
Stephen Sadle, 902-A Commerce Road Annapolis, MD 21401	3,946,600 (4)	1
James Landry 902-A Commerce Road Annapolis, MD 21401	176,763 (5)	
Robert P. Crabb 902-A Commerce Road Annapolis, MD 21401	641,331 (6)	
Warren V. Musser 435 Devon Park Drive Building 500		

Wayne, PA 19087	500,001 (7)	
Ronald W. Pickett 902-A Commerce Road Annapolis, MD 21401	2,679,964 (8)	11
David Grimes 902-A Commerce Road Annapolis, MD 21401	1,523,000 (9)	
L. Peter Larson 902-A Commerce Road Annapolis, MD 21401	2,505,285 (10)	1
Hugo DeCesaris 902-A Commerce Road Annapolis, MD 21401	1,375,000 (11)	5
Jenson and Associates, 5525 South 900 East Suite 110 Salt Lake City, Utah 84117	1,980,000	8
All directors and executive officers as a group	13,518,778	49

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(1) Unless otherwise indicated, each person has sole power to vote and dispose, or direct the disposition of, all shares of common stock beneficially owned, subject to applicable community property and similar laws.

(2) Includes immediately exercisable options to purchase 83,333 shares of Telkonet common stock at $1.00 per share.

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(3) Includes immediately exercisable options to purchase 58,334 shares of Telkonet common stock at $1.00 per share.

(4) Includes immediately exercisable options to purchase 225,000 shares of Telkonet common stock at $1.00 per share.

(5) Includes immediately exercisable options to purchase 176,763 shares of Telkonet common stock at $1.00 per share.

(6) Includes immediately exercisable options to purchase 125,000 shares of Telkonet common stock at $1.00 per share. Also includes 279,793 shares of Telkonet common stock and immediately exercisable options to purchase 236,538 shares of Telkonet common stock at $1.00 per share owned by Susquehanna Development Company, LLC of which Mr. Crabb is the managing member.

(7) Includes immediately exercisable options to purchase 500,001 shares of Telkonet common stock at $1.00 per share.

(8) Includes 21,000 shares of our common stock subject to issuance pursuant to Mr. Pickett's employment agreement.

(9) Includes immediately exercisable options to purchase 225,000 shares of Telkonet common stock at $1.00 per share.

(10) Includes immediately exercisable options to purchase 1,000,000 shares of Telkonet common stock at $1.00 per share.

(11) Includes an immediately exercisable warrant to purchase 815,000 shares of Telkonet common stock at $0.50 per share.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

STOCK REPURCHASES

On January 12, 2002, the Board of Directors approved a plan authorizing the repurchase of certain shares of, and options to purchase, Telkonet common stock owned by Messrs. Grimes, Larson and Sadle. Each of Messrs. Grimes, Larson and Sadle, at the time of the stock repurchase, owned in excess of five percent of the issued and outstanding shares of Telkonet common stock and were directors and executive officers of Telkonet.

As part of the stock repurchase, Mr. Grimes surrendered 3,721,918 shares of Telkonet common stock and options to purchase 160,000 shares of Telkonet common stock owned by him. In consideration of the surrender of these shares and options, Telkonet retained Mr. Grimes as a consultant for a period of three years and issued to Mr. Grimes fully vested options to purchase 1,000,000 shares of Telkonet common stock at fair market value on the date of exercise, but not less than $1.00 per share. In addition, Mr. Grimes agreed that certain shares of Telkonet common stock owned by him would be subject to a 36-month lock-up agreement under which 50,000 shares would be released on each of December 1, 2002 and December 1, 2003 and the remaining shares would be released on January 1, 2005. On April 24, 2002, the terms of Mr. Grimes' lock-up agreement were amended to permit the immediate release of 139,280 shares of Telkonet common stock, the release of 50,000 shares of Telkonet common stock on December 1, 2002, the release of 50,000 shares of Telkonet common stock on December 1, 2003 and the release of the remaining Telkonet common stock on January 1, 2005. The revised lock-up agreement also provided for the release of common stock in proportion to the number of options to purchase Telkonet common stock exercised by Mr. Grimes from time to time during the term of the lock-up agreement. As of December 31, 2002, Mr. Grimes had exercised all of the options issued to Mr. Grimes in the repurchase. Consequently, all of the shares subject to Mr. Grimes' revised lock-up agreement were released as of December 31, 2002.

Mr. Larson surrendered 705,000 shares of Telkonet common stock and options to purchase 200,000 shares of Telkonet common stock owned by him. In consideration of the surrender of these shares and options, Telkonet retained Mr. Larson as a consultant for a period of three years and issued to Mr. Larson fully vested options to purchase 1,000,000 shares of Telkonet common stock at fair market value on the date of exercise, but not less than $1.00 per share. In addition, Mr. Larson agreed that certain shares of Telkonet common stock owned

by him would be subject to a 36-month lock-up agreement under which 50,000 shares would be released on each of December 1, 2002 and December 1, 2003 and the remaining shares would be released on January 1, 2005. On April 24, 2002, the terms of Mr. Larson's lock-up agreement were amended to permit the immediate release of 139,280 shares of Telkonet common stock, the release of 50,000 shares of Telkonet common stock on December 1, 2002, the release of 50,000 shares of Telkonet common stock on December 1, 2003 and the release of the remaining Telkonet common stock on January 1, 2005. The revised lock-up agreement also provides for the release of common stock in proportion to the number of options to purchase Telkonet common stock exercised by Mr. Larson from time to time during the term of the lock-up agreement.

Mr. Sadle surrendered 2,147,694 shares of Telkonet common stock and options to purchase 200,000 shares of Telkonet common stock owned by him. In consideration of the surrender of these shares and options, the Board of Directors granted Mr. Sadle options to purchase 1,000,000 shares of Telkonet common stock at fair market value on the date of exercise, but not less than $1.00 per share. In addition, Mr. Sadle agreed that certain shares of Telkonet common stock owned by him would be subject to a 36-month lock-up agreement under which 50,000 shares would be released on each of December 1, 2002 and December 1, 2003 and the remaining shares would be released on January 1, 2005. On April 24, 2002, the terms of Mr. Sadle's lock-up agreement were amended to permit the immediate release of 139,280 shares of Telkonet common stock, the release of 50,000 shares of Telkonet common stock on December 1, 2002, the release of 50,000 shares of Telkonet common stock on December 1, 2003 and the release of the remaining Telkonet common stock on January 1, 2005. The revised lock-up agreement also provides for the release of common stock in proportion to the number of options to purchase Telkonet common stock exercised by Mr. Sadle from time to time during the term of the lock-up agreement. As of December 31, 2002, Mr. Sadle had exercised all of the options issued to Mr. Sadle in the repurchase. Consequently, all of the shares subject to Mr. Sadle's revised lock-up agreement were released as of December 31, 2002.

Mr. Sadle's employment agreement was also amended to include a provision by which Mr. Sadle would be required to forfeit shares of Telkonet common stock owned by him, up to an aggregate of 1,500,000 shares of common stock, in the event he voluntarily terminated his employment prior to the end of its 36-month term. Pursuant to the amended employment agreement, Mr. Sadle was required to forfeit 40,000 shares for each month following the month in which he resigned until the expiration of the amended employment agreement. The amended employment agreement also extended the term of Mr. Sadle's employment until December 31, 2004. On January 30, 2003, the Board of Directors approved an amendment to Mr. Sadle's employment agreement that permits the release of the 1,500,000 shares of common stock subject to forfeiture upon Mr. Sadle's resignation in proportion to the number of options to purchase Telkonet common stock exercised by Mr. Sadle from time to time during the term of the employment agreement. As of December 31, 2002, Mr. Sadle had exercised all of the options issued to Mr. Sadle in the repurchase. Consequently, all of the shares subject to forfeiture pursuant to Mr. Sadle's revised employment agreement were released from such forfeiture restriction as of January 30, 2003.

PERSONAL GUARANTY BY A DIRECTOR OF TELKONET

On March 9, 2001, we issued A. Hugo DeCesaris, a Telkonet director and stockholder owning in excess of 5.0% of Telkonet's issued and outstanding common stock, a warrant to purchase 1,000,000 shares of our common stock at $0.50 per share as consideration for his personal guaranty of Telkonet's $250,000 line of credit with First Mariner Bank.

LOANS BY OFFICERS AND SIGNIFICANT STOCKHOLDERS

In 2001 and 2002, Ronald W. Pickett and Stephen Sadle, each of whom is a director and officer of Telkonet and owns in excess of 5.0% of the issued outstanding Telkonet common stock, loaned $200,000 and $4,830, respectively, to Telkonet for working capital purposes. At the time of such loans, no formal repayment terms or arrangements were agreed to by the parties. On December 30, 2002, the aggregate remaining principal balance owed by Telkonet to Mr. Pickett was forgiven in exchange for Telkonet Series B Debentures. On January 31, 2003, the aggregate principal balance owed by Telkonet to Mr. Sadle was repaid in full, without interest.

On June 1, 2001, Hugo DeCesaris, a director of Telkonet and a stockholder owning in excess of 5.0% of Telkonet's issued and outstanding common stock, loaned $7,500 to Telkonet for working capital purposes. At the time of such loan, no formal repayment terms or arrangements were agreed to by the parties. As of December 31, 2002, the aggregate remaining principal balance owed by Telkonet to Mr. DeCesaris was $7,500.

PURCHASE OF CONVERTIBLE DEBENTURES

During the third quarter of 2001, Telkonet commenced an offering of up to $1,689,100 principal amount of Series A Debentures. The Series A Debentures each accrue interest at 8.0% per annum and mature three years from the date of purchase. Each Series A Debenture is convertible at any time following the six month anniversary of the date of issuance of such Series A Debenture into shares of Telkonet common stock at a conversion price equal to $0.50 per share for each $10,000 principal amount plus interest of the Series A Debenture converted. In connection with the placement of the Series A Debentures, Telkonet issued non-detachable warrants granting holders the right to acquire 1,689,100 share of our common stock at $1.00 per share.

During the fourth quarter of 2002, Telkonet commenced an offering of up to $2,500,000 principal amount of Series B Debentures. The Series B Debentures each accrue interest at 8.0% per annum and mature three years from the date of purchase. Each Series B Debenture is convertible at any time following the six month anniversary of the date of issuance of such Series B Debenture into shares of Telkonet common stock at a conversion price equal to $0.55 per share for each $10,000 principal amount plus interest of the Series B Debenture converted. In connection with the placement of the Series B Debentures, Telkonet issued non-detachable warrants granting holders the right to acquire 2,500,000 shares of our common stock at $1.00 per share.

As of March 26, 2003, Telkonet sold Series A and Series B Debentures having an aggregate principal value of $4,189,100, of which $824,000 was attributable to sales to the following Telkonet directors, officers and 5.0% shareholders, and members of their immediate family:

NAME	PURCHASE PRICE
Stephen L. Sadle	$ 65,000
David Grimes	$ 65,000
Hugo DeCesaris	$ 42,000 (1)
Ronald W. Pickett	$ 200,000
E. Barry Smith	$ 20,000
Howard E. Lubert	$ 100,000
Robert P. Crabb	$ 7,000
Warren V. Musser	$ 325,000 (2)

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(1) Includes Series A Debentures having an aggregate principal value of $20,000 and Series B Debentures having an aggregate principal value of $22,000 purchased by a members of Mr. DeCesaris' immediate family.

(2) Includes Series B Debentures having an aggregate principal value of $25,000 purchased by Mr. Musser's wife, and Series B Debentures having an aggregate principal value of $200,000 purchased by The Musser Foundation, of which Mr. Musser is the founder.

ARRANGEMENT WITH A DIRECTOR AND EXECUTIVE OFFICER

On January 29, 2002, we granted Susquehanna Development, LLC options to purchase 300,000 shares of our common stock at $1.00 per share as consideration for certain business services provided by Susquehanna Development. Robert P. Crabb, our corporate secretary, is the managing member of Susquehanna Development.

In January, 2003, we entered into an oral agreement with Warren V. Musser, Chairman of our Board of Directors, pursuant to which we agreed to pay Mr. Musser a commission equal to 8.0% of the aggregate value of Series B Debentures purchased by persons referred to Telkonet by Mr. Musser. Pursuant to this agreement, Mr. Musser received $8,000.

In January, 2003, we entered into an oral agreement with Howard Lubert, Telkonet's former Chief Executive Officer, pursuant to which we agreed to pay Mr. Lubert a commission equal to 8.0% of the aggregate value of Series B Debentures purchased by persons referred to Telkonet by Mr. Lubert. Pursuant to this agreement, Mr. Lubert received $12,000.

USE OF PROCEEDS

All net proceeds from the sale of our common stock will go to the selling stockholders selling common stock under this prospectus. We will not receive any proceeds from the sale of the common stock sold by the selling stockholders. The proceeds Telkonet receives from the exercise of warrants, the underlying shares of our common stock of which are included in this prospectus, will be used to expand sales and marketing efforts, support strategic partnership programs, build required infrastructure and fund working capital requirements.

SELLING STOCKHOLDERS

During the third quarter of 2001, we commenced an offering of up to $1,689,100 principal amount of Series A Debentures. The Series A Debentures each accrue interest at 8.0% per annum and mature three years from the date of purchase. Each Series A Debenture is convertible at any time following the six month anniversary of the date of issuance of such Series A Debenture into shares of Telkonet common stock at a conversion price equal to $0.50 per share for each $10,000 principal amount plus interest of the Series A Debenture converted. In connection with the placement of the Series A Debentures, Telkonet issued non-detachable warrants granting holders the right to acquire 1,689,100 share of our common stock at $1.00 per share. As of May 23, 2002, the Series A Debenture offering was fully subscribed.

During the fourth quarter of 2002, we commenced an offering of up to $2,500,000 principal amount of Series B Debentures. The Series B Debentures each accrue interest at 8.0% per annum and mature three years from the date of purchase. Each Series B Debenture is convertible at any time following the six month anniversary of the date of issuance of such Series B Debenture into shares of our common stock at a conversion price equal to $0.55 per share for each $10,000 principal amount plus interest of the Series B Debenture converted. In connection with the placement of the Series B Debentures, we also issued non-detachable warrants granting holders the right to acquire 2,500,000 shares of our common stock at $1.00 per share. As of February 14, 2003, the Series B Debenture offering was fully subscribed.

During the second quarter of 2003, we commenced an offering of up to $5,000,000 principal amount of Senior Notes. The Senior Notes each accrue interest at 8.0% per annum, mature three years from the date of purchase and are secured by a first priority security interest in all of the intellectual property assets of Telkonet. In connection with the placement of the Senior Notes, we also issued non-detachable warrants granting holders the right to acquire 6,250,000 shares of our common stock at $1.00 per share. As of June 26, 2003, the Senior Note offering was fully subscribed.

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The shares of our common stock covered by this prospectus include shares of common stock acquired by the selling stockholders pursuant to the conversion of the Series A and Series B Debentures (including outstanding principal and accrued interest) and shares of our common stock that have been issued or will be issued upon the exercise of warrants to purchase shares of our common stock issued in the Series A and Series B Debenture offerings and the Senior Note offering. The following table provides certain information regarding the selling stockholders' beneficial ownership of our common stock prior to and after the offering. Beneficial ownership is determined under the SEC's rules, and generally includes voting or investment power with respect to securities.

SELLING STOCKHOLDER	NUMBER OF SHARES OWNED PRIOR TO THE OFFERING	NUMBER OF SHARES BEING OFFERED FOR SALE	NUMBE SHARES AFTER OFFER
Cynthia S. Abshire	37,455	37,455	0
Robert Abshire	16,027	16,027	0
Michael G. and Maria Accattato	90,539	90,539	0
F. Scott and Barbara Addis	57,455	57,455	0
Steven Agnoff	68,013	68,013	0
Burgess M. Allen, Jr.	43,914	43,914	0
Henry Alperin	303,138	303,138	0
Mark D. Anderson	10,055	10,055	0
George Anthony	28,763	28,763	0
Fred C. Applegate Trust	250,000	250,000	0
Ozcan Ardan	16,194	16,194	0
Wendel B. Ardrey	28,735	28,735	0
Kerry Armbruster	144,227	144,227	0
Tonya Armstrong	11,569	11,569	0
Nancy P. Arnold	48,583	48,583	0
Sonan L. Ashley	234,264	234,264	0
Attkisson, Carter, and Akers, Incorporated	677,788	677,788	0

Augusta Cardiology Clinic	182,958	182,958	0
John W. Baker	125,000	125,000	0
Burton Barmore	12,389	12,389	0
Bryan W. Baughman	22,672	22,672	0
Matthew K. Beckstead	211,476	211,476	0
Rod K. Beckstead	53,105	53,105	0
Berkin Business S.A.	125,000	125,000	0
Valerie Biskey	155,368	155,368	0
Horace Blalock	174,673	174,673	0
A. Boardman Oil Company	28,743	28,743	0
J. Dickey Boardman, Jr.	7,185	7,185	0

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SELLING STOCKHOLDER	NUMBER OF SHARES OWNED PRIOR TO THE OFFERING	NUMBER OF SHARES BEING OFFERED FOR SALE	NUMBE SHARES AFTER OFFER
Robert L. Bower	63,966	63,966	0
Barbara Sue Bramlett	32,389	32,389	0
Jackie Brooks	222,891	222,891	0
Barry S. Bryant	70,337	70,337	0
Carolyn H. Byrd	125,000	125,000	0
Patsy D. Clayton	14,381	14,381	0
Lynn Claytor	125,000	125,000	0
Robert Clemmens	14,397	14,397	0
Bryan Coats	14,371	14,371	0
Kathy Coleman	70,994	70,994	0
I.R. Collier	19,233	19,233	0
Edward A. Corley	189,778	189,778	0
William D. Corley	128,902	128,902	0
James Cosper	972	972	0
Robert P. and Kriss Crabb	20,109 (2)	20,109	0
John R. Cralle	61,232	61,232	0

Tony and Johanna Currin	37,231	37,231	0
John Daily	15,817	15,817	0
Charles Daniel	178,180	178,180	0
Anthony DeCesaris, Jr.	63,350 (3)	63,350	0
Joseph A. and Donna M. DeCesaris	44,778 (4)	44,778	0
Amy Dickson	10,055	10,055	0
Milton O. Dickson, Sr.	10,055	10,055	0
Tommy Duncan	239,910	239,910	0
Barry Dunn	169,108	169,108	0
William A. Dunn, Jr.	211,887	211,887	0
J. Martin Echols	355,475	355,475	0
Robert Edmond	109,138	109,138	0
Verda C. Elrod	10,077	10,077	0
EPM AG	125,000	125,000	0
EPM Holdings AG	125,000	125,000	0
Paul Facchina, Jr.	15,837	15,837	0
D. Greer Falls	15,885	15,885	0
Dorth G. Falls	28,850	28,850	0
Frank A. Farnesi	31,250	31,250	0

SELLING STOCKHOLDER	NUMBER OF SHARES OWNED PRIOR TO THE OFFERING	NUMBER OF SHARES BEING OFFERED FOR SALE	NUMBE SHARES AFTER OFFER
Edward J. Farrell	312,500	312,500	0
Robert J. Ferrara	125,930	125,930	0
First Mirage, Inc.	125,000	125,000	0
First Montauk Securities Corp.	50,000	50,000	0
Patsy A. Fisher	45,029	45,029	0
H.E. and Paula Fowler	64,357 (5)	64,357	0
Joseph A. and Cecelia A. Fowler	64,357 (6)	64,357	0

J. Gregory and Sherry L. Fowler	31,976 (7)	31,976	0
Kurt Friemann	125,000	125,000	0
Donna Michelle Godwin Trust	15,817	15,817	0
David W. and Suzanne Grimes	207,109 (8)	207,109	0
Donnie W. Guy	70,246	70,246	0
Thomas M. Hall	315,298	315,298	0
Richard A. Hansen	312,500	312,500	0
Franklin D. Hart, Jr.	96,521	96,521	0
The Hart Organization Corp.	62,500	62,500	0
James A. Hendrickson	302,410	302,410	0
Robert F. Heishman	60,450	60,450	0
High Capital Funding, LLC	187,500	187,500	0
James H. Hillis, Jr.	57,487	57,487	0
Hitschler Enterprises, LLC	500,000	500,000	0
Kevin J. Hoban	38,959	38,959	0
Judith Hollington	45,817	45,817	0
Larry Hollington	64,444	64,444	0
A. Louis Hook, Jr.	32,389	32,389	0
Kenneth S. Hudson	103,449	103,449	0
Dale L. Hutchins	5,000	5,000	0
Ronald Jacobson	14,491	14,491	0
Faye S. Jennings	28,727	28,727	0
Joseph L. and Karen L. Johnson, III	32,231	32,231	0
David E. Jones	4,329	4,329	0
Glen E. Jones	25,000	25,000	0
J. Pope and Gail W. Jones	18,467	18,467	0
John Pope Jones	7,478	7,478	0
David Jordon	316,093	316,093	0

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	NUMBER OF SHARES OWNED PRIOR TO THE	NUMBER OF SHARES BEING	NUMBE SHARES AFTER

SELLING STOCKHOLDER	OFFERING	OFFERED FOR SALE	OFFER
Richard L. Keller	16,194	16,194	0
James R. Kelley	60,872	60,872	0
Nancy Kines	64,778	64,778	0
Michael Kingoff	5,000	5,000	0
Richard Knight, Sr.	14,405	14,405	0
Richard L. Kunkle	21,572	21,572	0
Langtry Trust Group	125,000	125,000	0
P. David and Jennifer Leinwand	5,000	5,000	0
Joanne Leonard	8,277	8,277	0
Tom Leonard	73,097	73,097	0
James T. Lewis	161,945	161,945	0
Ronald and Brenda Boyette Lindquist	29,154	29,154	0
Dianne H. Lollis	15,800	15,800	0
Hoyt G. Louder	250,000	250,000	0
Howard and Barbara Lubert	287,357 (9)	287,357	0
Earl Marshall	57,671	57,671	0
Phillip R. Mason	229,208	229,208	0
Joseph H. May	22,893	22,893	0
Alice McCoy	34,200	34,200	0
J. Lavern McCullough	48,583	48,583	0
Cynthia L. McDonald	171,319	171,319	0
Daniel McGinnis	62,500	62,500	0
M. Dixon McKay	339,098	339,098	0
Charles McPherson	15,837	15,837	0
Meadow Ventures	103,939	103,939	0
Eugenia Medlock	197,713	197,713	0
Claire Merica	15,817	15,817	0
Jan O. and Janice M. Miller	15,846	15,846	0
Lawrence W. and Crystal D. Moeller	32,178	32,178	0
Robert A and Cathleen Parlett Moeller	38,614	38,614	0

Maria Molinsky	31,250	31,250	0
Louis Mulherin, Jr.	254,436	254,436	0
Julian I. Murphy	28,743	28,743	0
Hilary Musser	71,819 (10)	71,819	0
Peter Musser, Jr.	824,555 (11)	824,555	0

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SELLING STOCKHOLDER	NUMBER OF SHARES OWNED PRIOR TO THE OFFERING	NUMBER OF SHARES BEING OFFERED FOR SALE	NUMBE SHARES AFTER OFFER
The Musser Foundation	60,004 (12)	60,004	0
Eric Newquist	15,817	15,817	0
Patrick L. O'Donnell	24,479	24,479	0
John G. and Nancy Lee Page	71,105	71,105	0
John Parlett, Jr.	28,727 (13)	28,727	0
W. Timothy Parlett	5,000 (14)	5,000	0
William Parlett	28,731 (15)	28,731	0
Pasquale Patrizio	12,500	12,500	0
Walter M. and Susan R. Patterson, III	28,763	28,763	0
Selena Peregoy	15,817	15,817	0
Brian K. Phelan	287,915	287,915	0
Jana S. Pine	110,085	110,085	0
Ted A. Poore	34,774	34,774	0
Randall Redmond	14,395	14,395	0
Kenneth J. Remington	48,583	48,583	0
Gerry Rhodes	28,791	28,791	0
Caroline T. Richardson	241,164	241,164	0
Furman Terry Richardson	8,621	8,621	0
Pamela K. Richardson	2,866	2,866	0
Michael C. and Pamela Rogers	60,529	60,529	0
Collin and Susan P. Royster	57,514	57,514	0

Stephen L. and Barbara J. Sadle	207,109 (16)	207,109	0
Dawn Saggus	48,583	48,583	0
Clayton Reed Shop	41,938	41,938	0
Kenneth D. Simpson	126,945	126,945	0
Kimberly Sligh	97,076	97,076	0
E. Barry and Donna Smith	1,107 (17)	1,107	0
William A. Smith	64,778	64,778	0
Scott Stolz	15,846	15,846	0
H. Swain	86,947	86,947	0
James J. and Diane J. Swiggard	1,091	1,091	0
Ronald K. Taylor	40,000	40,000	0
Thomas D. Thompson	84,011	84,011	0
John W. Thurmound, III	28,727	28,727	0
John and Robin Tinney	10,000	10,000	0

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SELLING STOCKHOLDER	NUMBER OF SHARES OWNED PRIOR TO THE OFFERING	NUMBER OF SHARES BEING	NUMBE SHARES AFTER