

Camelot Entertainment Group, Inc.
Form SB-2
February 02, 2007

As filed with the Securities and Exchange Commission on February 2, 2007
Registration No. 333-_____

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

FORM SB-2

REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933

CAMELOT ENTERTAINMENT GROUP INC.
(Name of Small Business Issuer in its Charter)

Delaware	7812	52-2195605
State or Jurisdiction of Incorporation or Organization	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification No.)

**2020 Main Street, Suite 990
Irvine, CA 92614
(949) 777-1090**

(Address and Telephone Number of Principal Executive Offices and Principal Place of Business)

**Robert P. Atwell, Chief Executive Officer
2020 Main Street, Suite 990
Irvine, CA 92614
(949) 777-1090**

(Name, Address and Telephone Number of Agent for Service)

Copies of Communications to:

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Approximate date of proposed sale to the public: As soon as practicable after this Registration Statement becomes effective.

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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 of 1933, please check the following box and list the Securities Act Registration Statement number of the earlier effective registration statement for the same offering. o

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act of 1933, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act of 1933, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

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

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Number of Units/Shares to be Registered	Proposed Maximum Offering Price Per Unit	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Common Stock, par value \$.001 per share ⁽¹⁾	28,094,877 ⁽²⁾	\$0.042	\$1,348,554	\$144.30
Total	28,094,877		\$1,348,554	\$144.30

⁽¹⁾ Represents 28,094,877 shares of common stock issuable in connection with the conversion of promissory notes in accordance with the Securities Purchase Agreement dated December 27, 2006 between us and AJW Partners, LLC, AJW Offshore, Ltd., AJW Qualified Partners, LLC and New Millennium Capital Partners II, LLC. The price of \$0.042 per share is being estimated solely for the purpose of computing the registration fee pursuant to Rule 457(c) of the Securities Act and is based on the estimated conversion price of the Callable Secured Convertible Notes (\$0.07 was the closing price on the date the transaction closed, December 29, 2006, less a 40% discount).

⁽²⁾ The number of shares being registered for the conversion of the Callable Secured Convertible Notes is 28,094,877 representing approximately 30% of our 93,649,589 common shares issued and outstanding.

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 or until the registration statement shall become effective on such date as the commission, acting pursuant to Section 8(a), may determine.

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Preliminary Prospectus subject to completion dated February 2, 2007

PROSPECTUS

28,094,877 SHARES OF COMMON STOCK

This prospectus relates to the resale of up to 28,094,877 shares of our common stock issuable to AJW Partners, LLC, AJW Offshore, Ltd., AJW Qualified Partners, LLC and New Millennium Capital Partners II, LLC (collectively, the "Selling Stockholders") in connection with the conversion of notes. The Selling Stockholders may sell their common stock from time to time at prevailing market prices.

Our common stock is currently quoted on the OTC Bulletin Board ("OTCBB") under the symbol "CMEG". On February 1, 2007, the closing price of our shares was \$0.11.

The securities offered in this prospectus involve a high degree of risk and are subject to the "penny stock" rules. You should carefully consider the factors described under the heading "Risk Factors" beginning on page 2.

Neither the Securities and Exchange Commission (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.

The date of this prospectus is February ____, 2007.

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SUMMARY INFORMATION

This summary highlights information contained elsewhere in this prospectus. You should read the entire prospectus carefully, including, the section entitled "Risk Factors", and our Consolidated Financial Statements and the related Notes included in this prospectus before deciding to invest in our common stock. Except as otherwise required by the context, all references in this prospectus to "we", "us", "our", "CMEG", or "Company" refer to the consolidated operations of Camelot Entertainment Group Inc., a Delaware corporation, and its wholly owned subsidiaries.

Our Business

We are a vertically-integrated entertainment company focused on creating, producing and distributing quality content across various media channels including feature film, television, radio, the Internet, and various forms of digital media for use in the home or on mobile devices. We were incorporated in Delaware on October 12, 1999 as Dstage.com, Inc. On April 15, 2004, we changed our name to Camelot Entertainment Group, Inc. and changed our business model from pursuing a new approach to venture formation (the Dstage.com Model) to the "Camelot Studio Model" (or "CSM"), which provides for the development, production, marketing and distribution of motion pictures. The CSM attempts to combine the efficiencies realized by studios of the early 1900's, with the artistic focus and diversity of today's independent productions. Using this approach, we believe the risk-reward relationship facing the typical film project can be dramatically shifted. For example, whereas a typical film pushes artists and directors to rush development and production in hopes of conserving cash, the CSM extends the pre-production cycle substantially to reduce costs while simultaneously increasing quality. Similarly, whereas a low-budget picture is severely limited by the types of postproduction technology used, due to budget constraints, we intend to invest directly in top of the line technology, spreading the costs over a targeted minimum of 12 original motion pictures each year. The goal of the CSM is to develop the ability to consistently produce films with the look, feel and artistic content of multi-million dollar pictures, for a fraction of the cost.

Our historical operations, as Dstage.com, Inc., consisted primarily of attempting to provide support, organization and restructuring services to other development stage companies. Due to the complete and drastic change in our business focus to producing, distributing and marketing original motion pictures, we believe that period-to-period comparisons of our operating results are not necessarily meaningful and should not be relied on as an indication of future performance. However, it is still important that you read the audited financial statements, the unaudited interim financials and the related notes included elsewhere in this prospectus in addition to thoroughly reading our current plan of operations.

Our common stock is currently quoted on the OTCBB under the symbol "CMEG".

Our Contact Information

Our principal executive offices are located at 2020 Main Street, Suite 990, Irvine, CA 92614. We can be reached by calling (949) 777-1090, faxing (949) 777-109 or emailing info@camelotfilms.com. We invite you to visit our website at www.camelotfilms.com for information about our company, products and services.

Going Concern

As reflected in Note 1 to the Financial Statements which accompany this prospectus, our consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and liabilities and commitments in the normal course of business. In the near term, we expect operating costs to continue to exceed funds generated from operations. As a result, we expect to continue to incur operating losses and we may not have

sufficient funds to grow our business in the future. We can give no assurance that we will achieve profitability or be capable of sustaining profitable operations. As a result, operations in the near future are expected to continue to use working capital.

To successfully grow the individual segments of the business, we must decrease our cash burn rate, improve our cash position and the revenue base of each segment, and succeed in our ability to raise additional capital through a combination of primarily public or private equity offering or strategic alliances. We also depend on certain contractors and our executives, and the loss of any of those contractors or executives, may harm our business.

The Offering

Common Stock Offered by Selling Stockholders:	Up to 28,094,877 shares which represents approximately 30% of our 93,649,589 common shares issued and outstanding.
Common Stock to be Outstanding After the Offering:	Up to 121,744,466 shares.
Use of Proceeds:	We will not receive any proceeds from the sale of the common stock.
OTCBB Symbol:	CMEG

RISK FACTORS

An investment in our shares involves a high degree of risk. Before making an investment decision, you should carefully consider all of the risks described in this prospectus. Each of the following risks could materially adversely affect our business, financial condition and results of operations, which could cause the price of our shares to decline significantly and you may lose all or a part of your investment. Our forward-looking statements in this prospectus are subject to the following risks and uncertainties. Our actual results could differ materially from those anticipated by our forward-looking statements as a result of the risk factors below. See "Forward-Looking Statements."

Risks Associated with Our Operations

We are subject to various risks that may materially harm our business, financial condition and results of operations. You should carefully consider the risks and uncertainties described below and the other information in this filing before deciding to purchase our common stock. If any of these risks or uncertainties actually occurs, our business, financial condition or operating results could be materially harmed. In that case, the trading price of our common stock could decline.

We have a limited operating history as a motion picture company in which to evaluate our business.

We were incorporated in Delaware on October 12, 1999 as Dstage.com, Inc., a business development organization. On April 15, 2004, we changed our name to Camelot Entertainment Group, Inc. and our business model to motion picture production, distribution and marketing. We have been unable to fully implement this new business model because of financing constraints. To date, we have no revenue and a limited operating history as a motion picture company upon which an evaluation of our future success or failure can be made. Current and future Company assets, including scripts and other properties that may be obtained in the future, may not be suitable for development to the projected forecast for 2007-2008 unless additional financing is secured. No assurances of any nature can be made to investors that the Company will be profitable or that it will remain in business. There can be no assurances that our management will be successful in managing the Company as a motion picture production, distribution and marketing company.

We have incurred significant and continuing losses and may not be able to generate revenues to sustain our operations.

We have experienced significant operating losses since our inception on October 12, 1999. We have incurred net losses of approximately \$591,740 and \$730,295 for the nine months ended September 30, 2006 and 2005, respectively, and have an accumulated deficit of \$12,416,599 at September 30, 2006, all of which related to our

previous activities as a business development organization, Dstage.com, and none of which relate to our current activities as a motion picture production, marketing and distribution entity.

We will continue to have a high level of operating expenses and will be required to make significant up-front expenditures in connection with the commencement of income-generating activities (including, but not limited to, salaries of executive, marketing and other personnel). We expect to incur additional losses until such time as we are able to fully implement our new business model and generate sufficient revenues to finance our operations and the costs of expansion. There can be no assurance that the Company will be able to generate such revenues and operate profitably.

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We will require additional funds to achieve our current business strategy and our inability to obtain additional financing could cause us to cease our business operations.

Even with the proceeds generated from this offering and through prior funding, including loans from Company executives, we will need to raise additional funds through public or private debt or sale of equity to achieve our new business strategy. Such financing may not be available when needed. Even if such financing is available, it may be on terms that are materially adverse to your interests with respect to dilution of book value, dividend preferences, liquidation preferences, or other terms.

Our ability to grow our company through acquisitions, business combinations and joint ventures, to maintain and expand our development, production and distribution of motion pictures and to fund our operating expenses will depend upon our ability to obtain funds through equity financing, debt financing (including credit facilities) or the sale or syndication of some or all of our interests in certain projects or other assets. Our new business plan requires a substantial investment of capital. At present, we need to generate approximately one million dollars (\$1,000,000) annually either through revenue generation or some form of financing to implement our business model. This amount may be adjusted at the time we begin fully implementing our business plan. As a result, there can be no guarantee that we will be able to generate this level of revenue and/or funding, and as a result our ability to remain in business could be adversely affected if we are not successful in developing revenues and/or funding. The production, acquisition and distribution of motion pictures require a significant amount of capital. A significant amount of time may elapse between our expenditure of funds and the receipt of commercial revenues from our motion pictures, if any. This time lapse requires us to fund a significant portion of our capital requirements from private parties, institutions, and other sources. Although we intend to reduce the risks of our production exposure through strict financial guidelines and financial contributions from broadcasters, sub-distributors, tax shelters, government and industry programs and studios, we cannot assure you that we will be able to implement successfully these arrangements or that we will not be subject to substantial financial risks relating to the production, acquisition, completion and release of future motion pictures. If we increase our production slate or our production budgets, we may be required to increase overhead, make larger up-front payments to talent and consequently bear greater financial risks. Any of the foregoing could have a material adverse effect on our business, results of operations or financial condition.

If we are unable to obtain financing on reasonable terms, we could be forced to delay, scale back or eliminate certain product and service development programs. In addition, such inability to obtain financing on reasonable terms could have a material negative effect on our business, operating results, or financial condition to such extent that we are forced to restructure, file for bankruptcy, sell assets or cease operations, any of which could put your investment dollars at significant risk.

We have been the subject of a going concern opinion for the fiscal years ended December 31, 2005 and 2004 from our independent auditors, which means that we may not be able to continue operations unless we can become profitable or obtain additional funding.

Our independent auditors have added an explanatory paragraph to their audit opinions issued in connection with our financial statements for the fiscal years ended December 31, 2005 and 2004, which states that the financial statements raise substantial doubt as to our ability to continue as a going concern. Our ability to make operations profitable or obtain additional funding will determine our ability to continue as a going concern. Our financial statements do not include any adjustments that might result from the outcome of this uncertainty. We will have to raise additional funds to meet our current obligations and to cover operating expenses through the year ending December 31, 2007. If we are not successful in raising additional capital we may not be able to continue as a going concern.

We are subject to a working capital deficit, which means that our current assets at September 30, 2006 were not sufficient to satisfy our current liabilities.

As of September 30, 2006, we had a working capital deficit of \$760,536, which means that our current liabilities of \$779,306 exceeded our current assets of \$18,770 by that amount on September 30, 2006. Current assets are assets that are expected to be converted to cash within one year and, therefore, may be used to pay current liabilities as they become due. Our working capital deficit means that our current assets on September 30, 2006 were not sufficient to satisfy all of our current liabilities on that date. We will have to raise additional capital or debt to fund the deficit or cease operations.

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If we are unable to retain the services of our executive officers, Robert P. Atwell, George Jackson, and Michael Ellis, or if we are unable to successfully recruit qualified managerial personnel and employees with experience in business and the motion picture industry, we may not be able to continue our operations.

Our success depends to a significant extent upon the continued service of our executive officers, Robert P. Atwell, President and Chief Executive Officer, George Jackson, Secretary and Chief Financial Officer, and Michael Ellis, Chief Operating Officer. Loss of the services of any of our executive officers could have a material adverse effect on our growth, revenues, and prospective business. We do not maintain key-man insurance on the lives of our executive officers.

In addition, in order to successfully implement and manage our business plan, we will be dependent upon, among other things, successfully recruiting highly skilled creative and production personnel, including producers, executives, cinematographers, editors, costume designers, set designers, sound technicians, lighting technicians, actors, sales and marketing experts, and legal and accounting experts. Although we expect to find qualified candidates to fill these positions, competition is intense and they may be unwilling to work for us under acceptable terms. This could delay production or reduce the quality of our film projects, which would impair our ability to successfully implement our business model.

Also, many of these positions could require us to hire members of unions or guilds. As a result, our ability to terminate unsatisfactory or non-performing workers could be adversely affected by existing union or guild contracts and regulations. This could cause delays in production of our film projects and significantly increase costs.

There can be no assurance that we will be able to find, attract and retain existing employees or that we will be able to find, attract and retain qualified personnel on acceptable terms.

Mr. Atwell, our President, Chief Executive Officer and Chairman owns a controlling interest in our voting stock and investors will not have any voice in our management.

Mr. Atwell, our President, Chief Executive Officer and Chairman, is the beneficial owner of 63.47% of our issued and outstanding common shares and 51.00% of each of our Class A Convertible Preferred Stock ("Class A") and Class B Convertible Preferred Stock ("Class B"). Each share of Class A entitles the holder to 50 votes and each share of Class B entitles the holder to 1,000 votes. In the aggregate, Mr. Atwell is entitled to cast 5,414,440,485 or 99.37% of the votes in any vote by our stockholders. Thus, Mr. Atwell, will have the ability to control substantially all matters submitted to our stockholders for approval, including:

- § election of our board of directors;
- § removal of any of our directors;
- § amendment of our certificate of incorporation or bylaws; and
- § adoption of measures that could delay or prevent a change in control or impede a merger, takeover or other business combination involving us.

As a result of his ownership and position as a director and executive officer, he is able to influence all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions. In addition, sales of significant amounts of shares held by our directors and executive officers, or the prospect of these sales, could adversely affect the market price of our common stock. Management's stock ownership may discourage a potential acquirer from making a tender offer or otherwise attempting to obtain control of us, which in turn could reduce our stock price or prevent our stockholders from realizing a premium over our stock price.

It is likely that additional shares of our stock will be issued in the normal course of our business development, which will result in a dilutive affect on our existing stockholders.

We will issue additional stock as required to raise additional working capital in order to secure intellectual properties, undertake company acquisitions, recruit and retain an effective management team, compensate our officers and directors, engage industry consultants and for other business development activities.

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If we fail to adequately manage our growth, we may not be successful in growing our business and becoming profitable.

We expect our business and number of employees to grow over the next year. We expect that our growth will place significant stress on our operation, management, employee base and ability to meet capital requirements sufficient to support our growth over the next 12 months. Any failure to address the needs of our growing business successfully could have a negative impact on our chance of success.

If we acquire or invest in other businesses, we will face certain risks inherent in such transactions.

We may acquire, make investments in, or enter into strategic alliances or joint ventures with, companies engaged in businesses that are similar or complementary to ours. If we make such acquisitions or investments or enter into strategic alliances, we will face certain risks inherent in such transactions. For example, we could face difficulties in managing and integrating newly acquired operations. Additionally, such transactions would divert management resources and may result in the loss of artists or songwriters from our rosters. We cannot assure you that if we make any future acquisitions, investments, strategic alliances or joint ventures that they will be completed in a timely manner, that they will be structured or financed in a way that will enhance our creditworthiness or that they will meet our strategic objectives or otherwise be successful. Failure to effectively manage any of these transactions could result in material increases in costs or reductions in expected revenues, or both.

“Penny Stock” rules may make buying or selling our common stock difficult.

Trading in our securities is subject to the “penny stock” rules. The SEC has adopted regulations that generally define a penny stock to be any equity security that has a market price of less than \$5.00 per share, subject to certain exceptions. These rules require that any broker-dealer who recommends our securities to persons other than prior customers and accredited investors, must, prior to the sale, make a special written suitability determination for the purchaser and receive the purchaser’s written agreement to execute the transaction. Unless an exception is available, the regulations require the delivery, prior to any transaction involving a penny stock, of a disclosure schedule explaining the penny stock market and the risks associated with trading in the penny stock market. In addition, broker-dealers must disclose commissions payable to both the broker-dealer and the registered representative and current quotations for the securities they offer. The additional burdens imposed upon broker-dealers by such requirements may discourage broker-dealers from effecting transactions in our securities, which could severely limit the market price and liquidity of our securities. Broker-dealers who sell penny stocks to certain types of investors are required to comply with the Commission’s regulations concerning the transfer of penny stocks. These regulations require broker-dealers to:

- § Make a suitability determination prior to selling a penny stock to the purchaser;
- § Receive the purchaser’s written consent to the transaction; and
- § Provide certain written disclosures to the purchaser.

Risks Associated with the Motion Picture Production and Distribution Industry

Because the movie industry is intensely competitive and we lack the name recognition and resources of our competitors, we may never generate any revenues or become profitable.

The motion picture industry is highly competitive. We believe that a motion picture’s theatrical success is dependent upon general public acceptance, marketing technology, advertising and the quality of the production. We intend to produce motion pictures that normally should compete with numerous independent and foreign productions as well as productions produced and distributed by a number of major domestic companies, many of which are units of

conglomerate corporations with assets and resources substantially greater than ours. Some of the production and distribution companies that we will compete with are The Weinstein Company, Jerry Bruckheimer Films, Miramax Films, Lions Gate Entertainment Corp., Sony Pictures Entertainment, Inc., New Line Cinema, a subsidiary of Time Warner, Universal Studios, 20th Century Fox Film Corporation, a subsidiary of News Corp., Buena Vista Motion Pictures Group, a collection of affiliated motion picture studios all subsidiaries of The Walt Disney Company, Paramount Pictures Corporation, a subsidiary of Viacom, and Troma Entertainment, Inc. All of these competitors are significantly larger than us, have a long-standing business relationship with customers, vendors and financial institutions, and have established staying power in the industry over the past twenty years.

Our management believes that in recent years there has been an increase in competition in virtually all facets of the motion picture industry. With increased alternative distribution channels for many types of entertainment, the motion picture business competes more intensely than previously with all other types of entertainment activities as well as television. While increased use of pay per view television, pay television channels, and home video products are potentially beneficial, there is no guarantee that we will be able to successfully penetrate these markets. Failure to penetrate these potential distribution channels would have a material adverse impact on our results of operations.

Since our success depends on the commercial success of our motion pictures, which is unpredictable and highly speculative, we may never generate any revenue or become profitable.

The success of a single motion picture project is fraught with an unusually high degree of uncertainty and risk.. A studio or independent producer's ability to finance a project, execute a successful distribution strategy, obtain favorable press and compete with an unknown quantity of competing releases are just some of the factors that impact the commercial success or failure of a film project. Our strategy involves producing a minimum of 12 motion pictures per year. While the intent is to reduce production risk through this strategy, our plan has the potential to compound risks germane to the industry.

Each film we produce and distribute should appeal to a given segment of society to achieve acceptance. Although our intent to target niche markets that should require less than broad market acceptance to achieve commercial success, there can be no assurance that this strategy will succeed.

Motion picture production and distribution is highly speculative and inherently risky. There can be no assurance of the economic success of any motion picture since the revenues derived from the production and distribution of a motion picture (which do not necessarily bear a direct correlation to the production or distribution costs incurred) depend primarily upon its acceptance by the public, which cannot be predicted. The commercial success of a motion picture also depends upon the acceptance of competing films released into the marketplace at or near the same time, the availability of alternative forms of entertainment and leisure time activities, general economic conditions and other tangible and intangible factors, all of which can change and cannot be predicted with certainty. Further, the theatrical success of a motion picture is generally a key factor in generating revenues from other distribution channels. There is a substantial risk that some or all of our motion pictures will not be commercially successful, resulting in costs not being recouped or anticipated profits not being realized.

Theaters are more likely to exhibit feature films with substantial studio marketing budgets. Even if we are able to complete the films and obtain distribution, it is unclear how much should be spent on marketing to promote each film by our distributors.

All of these factors cannot be predicted with certainty. In addition, motion picture attendance is seasonal, with the greatest attendance typically occurring during the summer and holidays. The release of a film during a period of relatively low theater attendance is likely to affect the film's box office receipts adversely.

Relatively few motion pictures return a profit to investors. There can be no assurance that a motion picture will recoup its production costs. There is a very high degree of risk that any motion picture we may produce will not return all or any portion of our investment.

We may not be able to complete a specific motion picture, which could cost us substantial amounts and potentially adversely affect our other planned productions.

The probability of successfully completing a motion picture project is also laden with an unusually high degree of uncertainty and risks. Movie producers are often involved in several projects at the same time and an active film director is often presented with opportunities to direct many movies. In addition, independent contractors needed to produce the film often have commitments to more than one movie project. Because we may decide to replace key members of our production team if they are unable to perform their duties within our schedule, the availability of qualified personnel to replace key members may not be adequate and as a result our ability to continue and complete a specific production may be put in jeopardy. As a result, we might have to close down a production. That event would have an adverse affect on our planned operations.

If we do not complete the film on schedule or within budget, our ability to generate revenue may be diminished, delayed or even evaporate. Our success depends on our ability to complete the film on schedule and within budget. If a specific film is not completed, we may lose all of the funds paid into a particular project with no way to recoup that investment.

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We intend to distribute our films in foreign countries which may be unpredictable and may have unstable and different governments and/or laws than the U.S.

We plan to license motion picture and television programming in foreign countries to sub-distributors. If we are at all successful in this regard, a portion of our revenues should be derived from foreign sources. Because of this, our business is subject to certain risks inherent in international trade, many of which are beyond our control. Such risks include, but are not limited to, changes in laws and policies affecting trade, investment and taxes (including laws and policies relating to the repatriation of funds and to withholding taxes), differing degrees of protection for intellectual property, the instability of foreign economies and governments and in some cases an adverse acceptance to a film may occur, resulting in a demand to renegotiate the license agreement's terms and conditions. In addition, fluctuations in foreign exchange rates may affect our results of operations.

Piracy of the original motion pictures that we plan to produce may reduce our revenues and potential earnings.

According to industry sources, piracy losses in the motion picture industry have increased substantially, from an estimated \$2.2 billion in 1997 to an estimated \$3.5 billion in 2002. In certain regions such as Asia, the Eastern bloc countries and South America, motion picture piracy has been a major issue for some time. With the proliferation of DVD format around the globe, along with other digital recording and playback devices, losses from piracy have spread more rapidly in North America and Europe. Piracy of original motion pictures we produce and distribute may adversely impact the gross receipts received from the exploitation of these films, which could have a material adverse effect on our business, results of operations or financial condition.

Our operating results will fluctuate.

Like all motion picture production companies, our revenues and results of operations could be significantly dependent upon the timing of releases and the commercial success of the motion pictures we distribute, none of which can be predicted with certainty. Accordingly, our revenues and results of operations may fluctuate significantly from period to period, and the results of any one period may not be indicative of the results for any future periods.

In accordance with generally accepted accounting principles and industry practice, we intend to amortize film costs using the individual-film-forecast method under which such costs are amortized for each film in the ratio that revenue earned in the current period for such title bears to management's estimate of the total revenues to be realized from all media and markets for such title. To comply with this accounting principle, our management plans to regularly review, and revise when necessary, our total revenue estimates on a title-by-title basis, which may result in a change in the rate of amortization and/or a write-down of the film asset to net realizable value. Results of operations in future years should be dependent upon our amortization of film costs and may be significantly affected by periodic adjustments in amortization rates. The likelihood of the Company's reporting of losses is increased because the industry's accounting method requires the immediate recognition of the entire loss in instances where it is expected that a motion picture should not recover the Company's investment.

Similarly, should any of our films be profitable in a given period, we should have to recognize that profit over the entire revenue stream expected to be generated by the individual film.

Our film production budgets may increase and film production spending may exceed such budgets.

Our future film budgets may increase due to factors including, but not limited to, (1) escalation in compensation rates of people required to work on our projects, (2) number of personnel required to work on our projects, (3) equipment needs, (4) the enhancement of existing or the development of new proprietary technology and (5) the addition of facilities to accommodate the growth of a studio. Due to production exigencies, which are often difficult to predict, it is not uncommon for film production spending to exceed film production budgets, and our projects may not be

completed within the budgeted amounts. In addition, when production of each film is completed, we may incur significant carrying costs associated with transitioning personnel on creative and development teams from one project to another. These carrying costs increase overall production budgets and could have a material adverse effect on our results of operations and financial condition.

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Our anticipated successive releases of films could place a significant strain on our limited resources.

We anticipate establishing parallel creative teams so that we can develop more than one film at a time. These teams are expected to work on future projects, as we move towards producing 12 films per year. Due to the anticipated strain on our personnel from the effort required for the release of an upcoming film and the time required for creative development of future films, it is possible that we would be unable to release twelve new films in the first year and in subsequent years. We may be required to expand our employee base, increase capital expenditures and procure additional resources and facilities in order to accomplish the scheduled releases of our films. This growth and expansion may place a significant strain on our resources. We cannot provide any assurances that any future film will be released as targeted or that this strain on resources will not have a material adverse effect on our business, financial condition or results of operations. As we move towards achieving 12 films a year, there will likely be additional demands placed on the availability of key people. A lack of availability of key people may adversely impact the success and timing of our future films.

We may implement a variety of new and upgraded operational and financial systems, procedures and controls, including improvement and maintenance of our accounting system, other internal management systems and backup systems. Our growth and these diversification activities, along with the corresponding increase in the number of our employees and our rapidly increasing costs, may result in increased responsibility for our management team. We may need to improve our operational, financial and management information systems, to hire, train, motivate and manage our employees, and to provide adequate facilities and other resources for them. We cannot provide any assurance we will be successful in accomplishing all of these activities on a timely and cost-effective basis. Any failure to accomplish one or more of these activities on a timely and cost-effective basis would have a material adverse effect on our business, financial condition and results of operations.

The decisions regarding the timing of theatrical releases and related products, the marketing and distribution strategy, and the extent of promotional support are important factors in determining the success of our motion pictures and related products. We may enter into agreements with third-parties to assist us in the marketing and distribution of our films, and we may require the marketers and distributors to consult with us with respect to all major marketing and distribution decisions. Said agreements may or may not include: (1) the manner in which distributors may distribute our films and related products; (2) the number of theaters to which our films are distributed; (3) the specific timing of release of our films and related products; or (4) the specific amount or quality of marketing and promotional support of the films and related products as well as the associated promotional and marketing budgets.

We are smaller and less diversified than all of our competitors.

Although we plan to be an independent distributor and producer, we expect to constantly compete with major U.S. and international studios. Most of the major U.S. studios are part of large diversified corporate groups with a variety of other operations, including television networks and cable channels that can provide both means of distributing their products and stable sources of earnings that may allow them better to offset fluctuations in the financial performance of their motion picture and television operations. In addition, the major studios have more resources with which to compete for ideas, storylines and scripts created by third parties as well as for actors, directors and other personnel required for production. The resources of the major studios may also give them an advantage in acquiring other businesses or assets, including film libraries, that we might also be interested in acquiring. The foregoing could have a material adverse effect on our business, results of operations and financial condition.