

## **Insider Trading Compliance Manual**

In order to take an active role in the prevention of insider trading violations by its officers, directors, employees, consultants, attorneys, advisors and other related individuals, we have adopted the policies and procedures described in this Memorandum.

### **I. Adoption of Insider Trading Policy**

Effective March 6, 2007, as revised on January 27, 2011, we have adopted the Insider Trading Policy attached hereto as Exhibit A (the "Policy"), which prohibits trading based on material, nonpublic information regarding us ("Inside Information"). The Policy covers all officers and members of our board of directors (the "directors"), all our other employees and its subsidiaries, all secretaries and assistants supporting our directors and consultants or our contractors or their subsidiaries who have or may have access to Inside Information and members of the immediate family or household of any such person, or any affiliate (as such term is defined under the Securities Act of 1933, as amended) of any such person or our Company. The Policy (and/or a summary thereof) is to be delivered to all our employees, consultants and related individuals who are within the categories of covered persons upon the commencement of their relationships, and is to be circulated to all covered personnel at least annually.

### **II. Designation of Certain Persons**

**A. Section 16 Individuals.** All our directors and executive officers are subject to the reporting and liability provisions of Section 16 of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and the rules and regulations promulgated thereunder ("Section 16 Individuals"). Attached hereto as Exhibit B is a separate memorandum which discusses the relevant terms of Section 16.

**B. Other Persons Subject to our Policy.** In addition, certain employees, consultants, and advisors as described in Section I above, or certain of their respective affiliates, have, or are likely to have, from time to time access to Inside Information and together with the Section 16 Individuals, are subject to our Policy, including the pre-clearance requirement described in Section IV. A. below.

### **III. Appointment of Compliance Officer**

We have appointed Michael F. Adams as the Company's Insider Trading Compliance Officer (the "Compliance Officer").

#### **IV. Duties of Compliance Officer**

The Compliance Officer has been designated by the Board to handle any and all matters relating to our Insider Trading Compliance Program. Certain of those duties may be delegated to outside counsel and consultants with special expertise in securities issues and relevant law. The duties of the Compliance Officer shall include the following:

- A.** Pre-clearing all transactions involving our securities by the Section 16 Individuals and those individuals having regular access to Inside Information, defined for these purposes to include our employees and our subsidiaries, all secretaries and assistants supporting such directors, officers and employees, and consultants or contractors or our subsidiaries who have or may have access to Inside Information and members of the immediate family or household of any such person, in order to determine compliance with the Policy, insider trading laws, Section 16 of the Exchange Act and Rule 144 promulgated under the Securities Act of 1933, as amended. Attached hereto as Exhibit C is a Pre-Clearance Checklist to assist the Compliance Officer's performance of this duty.
- B.** Assisting in the preparation and filing of Section 16 reports (Forms 3, 4 and 5) for all Section 16 Individuals.
- C.** Serving as our designated recipient copies of reports filed with the Securities and Exchange Commission by Section 16 Individuals under Section 16 of the Exchange Act.
- D.** Performing periodic reviews of available materials, which may include Forms 3, 4 and 5, Form 144, officers and director's questionnaires, and reports received from our stock administrator and transfer agent, to determine trading activity by officers, directors and others who have, or may have, access to Inside Information.
- E.** Circulating the Policy (and/or a summary thereof) to all covered employees, including Section 16 Individuals, on an annual basis, and providing the Policy and other appropriate materials to new officers, directors and others who have, or may have, access to Inside Information.
- F.** Assisting the Board of Directors in implementation of the Policy and Sections I and II of this memorandum.
- G.** Coordinating with our counsel regarding all securities compliance matters.
- H.** Retaining copies of all appropriate securities reports, and maintaining records of his activities as Compliance Officer.
- I.** Oversee the implementation of trading suspensions applicable to directors, officers, or some or all employees that may be ordered by the Board or CEO.

## **Exhibit A**

### **Application of Policy**

This Policy applies to all transactions in our securities, including common stock, options and warrants to purchase common stock and any other securities the Company may issue from time to time, such as preferred stock, warrants and convertible debentures, as well as to derivative securities relating to our stock, whether or not issued by us, such as exchange-traded options. It applies to all our officers and directors, all our other employees and our subsidiaries, all secretaries and assistants supporting such directors, officers and employees, and our consultants or contractors or our subsidiaries who have or may have access to Material Nonpublic Information (as defined below) regarding us and members of the immediate family or household of any such person, or any affiliate (as such term is defined under the Securities Act of 1933, as amended) of any such person or of us. This group of people is sometimes referred to in this Policy as "Insiders." This Policy also applies to any person who receives Material Nonpublic Information from any Insider.

Any person who possesses Material Nonpublic Information regarding us is an Insider for so long as such information is not publicly known.

### **Definition of Material Nonpublic Information**

It is not possible to define all categories of material information. However, information should be regarded as material if there is a reasonable likelihood that it would be considered important to an investor in making an investment decision regarding the purchase or sale of our securities. Nonpublic information is information that has not been previously disclosed to the general public and is otherwise not available to the general public.

While it may be difficult to determine whether particular information is material, there are various categories of information that are particularly sensitive and, as a general rule, should always be considered material. In addition, material information may be positive or negative. Examples of such information may include:

- Financial results
- Projections of future earnings or losses
- Major contract awards, cancellations or write-offs
- Joint ventures with third parties
- Research milestones
- News of a pending or proposed merger or acquisition
- News of the disposition of material assets
- Impending bankruptcy or financial liquidity problems
- Gain or loss of a substantial customer or supplier
- Results of trials
- New product announcements of a significant nature
- Significant pricing changes
- Stock splits
- New equity or debt offerings
- Significant litigation exposure due to actual or threatened litigation

- Changes in senior management
- Capital investment plans
- Changes in dividend policy

### **Certain Exceptions**

For purposes of this Policy, we consider that the exercise of stock options for cash under our stock option plan (but not the sale of any such shares) is exempt from this Policy, since the other party to the transaction is us itself and the price does not vary with the market but is fixed by the terms of the option agreement or the plan.

### **Statement of Policy**

#### **General Policy**

It is our policy to prohibit the unauthorized disclosure of any nonpublic information acquired in the workplace and the misuse of Material Nonpublic Information in securities trading.

#### **Specific Policies**

**1. Trading on Material Nonpublic Information.** With certain exceptions, no officer or director, no employee or its subsidiaries and no consultant or contractor or any of our subsidiaries and no members of the immediate family or household of any such person, shall engage in any transaction involving a purchase or sale of our securities, including any offer to purchase or offer to sell, during any period commencing with the date that he or she possesses Material Nonpublic Information concerning us, and ending at the close of business on the second Trading Day following the date of public disclosure of that information, or at such time as such nonpublic information is no longer material. However, see Section 2 under "Permitted Trading Period" below for a full discussion of trading pursuant to a pre-established plan or by delegation.

As used herein, the term "Trading Day" shall mean a day on which national stock exchanges and the NASDAQ National Market are open for trading.

**2. Tipping.** No Insider shall disclose ("tip") Material Nonpublic Information to any other person (including family members) where such information may be used by such person to his or her profit by trading in our securities to which such information relates, nor shall such Insider or related person make recommendations or express opinions on the basis of Material Nonpublic Information as to trading in our securities.

Regulation FD (Fair Disclosure) is an issuer disclosure rule implemented by the SEC that addresses selective disclosure. The regulation provides that when we, or persons acting on our behalf, discloses material nonpublic information to certain enumerated persons (in general, securities market professionals and holders of our securities who may well trade on the basis of the information), it must make public disclosure of that information. The timing of the required public disclosure depends on whether the selective disclosure was intentional or unintentional; for an intentional selective disclosure, we must make public disclosures simultaneously; for a non-intentional disclosure we must make public disclosure promptly. Under the regulation, the required

public disclosure may be made by filing or furnishing a Form 8-KSB, or by another method or combination of methods that is reasonably designed to effect broad, non-exclusionary distribution of the information to the public.

It is our policy that all communications with the press be handled through Michael F. Adams, President and CEO or Mr. Adams' duly appointed designee (telephone (978) 657-0075).

**3. Confidentiality of Nonpublic Information.** Nonpublic information relating to us is our property and the unauthorized disclosure of such information is forbidden.

**4. Duty to Report Inappropriate and Irregular Conduct.** All employees, and particularly managers and/or supervisors, have a responsibility for maintaining financial integrity within our company, consistent with generally accepted accounting principles and both federal and state securities laws. Any employee who becomes aware of any incidents involving financial or accounting manipulation or irregularities, whether by witnessing the incident or being told of it, must report it to their immediate supervisor and to our Audit Committee. In certain instances, employees are allowed to participate in federal or state proceedings. For a more complete understanding of this issue, employees should consult their employee manual and/or seek the advice of counsel. The Compliance Officer can provide you with contact information for our outside general corporate and securities counsel.

### **Potential Criminal and Civil Liability and/or Disciplinary Action**

**1. Liability for Insider Trading.** Insiders may be subject to penalties of up to \$1,000,000 and up to ten (10) years in jail for engaging in transactions in our securities at a time when they possess Material Nonpublic Information regarding our Company. In addition, the SEC has the authority to seek a civil monetary penalty of up to three times the amount of profit gained or loss avoided by illegal insider trading. "Profit gained" or "loss avoided" generally means the difference between the purchase or sale price of our stock and its value as measured by the trading price of the stock a reasonable period after public dissemination of the nonpublic information.

**2. Liability for Tipping.** Insiders may also be liable for improper transactions by any person (commonly referred to as a "tippee") to whom they have disclosed Material Nonpublic Information regarding our Company or to whom they have made recommendations or expressed opinions on the basis of such information as to trading in our securities. The Securities and Exchange Commission (the "SEC") has imposed large penalties even when the disclosing person did not profit from the trading. The SEC, the stock exchanges and the National Association of Securities Dealers, Inc. use sophisticated electronic surveillance techniques to monitor and uncover insider trading.

**3. Possible Disciplinary Actions.** Individuals subject to the Policy who violate this Policy shall also be subject to disciplinary action by us, which may include suspension, forfeiture of perquisites, ineligibility for future participation in our equity incentive plans and/or termination of employment.

## Permitted Trading Period

### 1. Black-Out Period and Trading Window.

To ensure compliance with this Policy and applicable federal and state securities laws, we require that all officers; directors; employees with the title of general manager, controller or more senior; and members of the immediate family or household of any such person refrain from conducting transactions involving the purchase or sale of our securities, other than during the period in any fiscal quarter (including the year end) commencing forty eight hours following the date and time of public disclosure of the financial results for the prior fiscal quarter or year with respect to the Form 10-K and Form 10-Q, as applicable, and ending on the fifteenth calendar day of the third month of the fiscal quarter (including the year end) (the "Trading Window"). If such public disclosure occurs on a Trading Day before the markets close, then such date of disclosure shall be considered the first Trading Day following such public disclosure.

The safest period for trading in our securities, assuming the absence of Material Nonpublic Information, is generally the first ten Trading Days of the Trading Window. The last month of each fiscal quarter and the period of time from the end of such quarter until the public disclosure of quarterly results are particularly sensitive periods of time for transactions in our securities from the perspective of compliance with applicable securities laws. This is because officers, directors and certain other employees, as any quarter progresses, are increasingly likely to possess Material Nonpublic Information about the expected financial results for the quarter. The purpose of the Trading Window is to avoid any unlawful or improper transactions.

It should be noted that even during the Trading Window any person possessing Material Nonpublic Information concerning our Company should not engage in any transactions in our securities until such information has been known publicly for at least two Trading Days. We have adopted the policy of delaying trading for "commencing forty eight hours following the date and time of public disclosure" because the securities laws require that the public be informed effectively of previously undisclosed material information before Insiders trade in our stock. Public disclosure may occur through a widely disseminated press release or through filings, such as Forms 10-K, 10-Q and 8-K, with the SEC. Furthermore, in order for the public to be effectively informed, the public must be given time to evaluate the information disclosed by our Company. Although the amount of time necessary for the public to evaluate the information may vary depending on the complexity of the information, generally two Trading Days is a sufficient period of time.

Although we may from time to time require during a Trading Window that directors, officers, selected employees and others suspend trading because of developments known to us and not yet disclosed to the public, each person is individually responsible at all times for compliance with the prohibitions against insider trading. Trading in our securities during the Trading Window should not be considered a "safe harbor," and all directors, officers and other persons should use good judgment at all times.

From time to time, our Company, at the direction of the CEO or the Board, may also require that directors, officers, selected or all employees and others suspend trading because of developments known to us and not yet disclosed to the public. In such event, such persons are advised not to engage in any transaction involving the purchase or

sale of our securities during such period and should not disclose to others the fact of such suspension of trading. Such suspension shall last for the duration of the period set by the Board or the CEO, as applicable which shall be the earlier of: (i) two Trading Days after such developments have been disseminated to the public or (ii) such time as the Board or the CEO, as applicable, have determined that the developments are no longer material.

Notwithstanding these general rules, Insiders may trade outside of the Trading Window provided that such trades are made pursuant to a pre-established plan or by delegation; these alternatives are discussed in the next section.

## **2. Trading According to a Pre-established Plan or by Delegation.**

Trading which is not "on the basis of" material non-public information may not give rise to insider trading liability. The United States Securities and Exchange Commission has adopted Rule 10b5-1 under which insider trading liability can be avoided if Insiders follow very specific procedures. In general, such procedures involve trading according to pre-established instructions (a "Pre-established Trade").

### **Pre-established Trades must:**

**a)** Be documented by a contract, written plan, or formal instruction which provides that the trade take place in the future. For example, an Insider can contract to sell his or her shares on a specific date, or simply delegate such decisions to an investment manager, 401(k) plan administrator or similar third party. This documentation must be provided to our Insider Trading Compliance Officer.

**b)** Include in its documentation the specific amount, price and timing of the trade, or the formula for determining the amount, price and timing. For example, the Insider can buy or sell shares in a specific amount and on a specific date each month, or according to a pre-established percentage (of the Insider's salary, for example) each time that the share price falls or rises to pre-established levels. In the case where trading decisions have been delegated, the specific amount, price and timing need not be provided.

**c)** Be implemented at a time when the Insider does not possess Material Nonpublic Information. As a practical matter, this means that the Insider should set up Pre-established Trades, or delegate trading discretion, only during a "Trading Window" (discussed in Section 1, above). However, in doing so, the Insider should take into account the considerations described in Section 1 above, including, without limitation, the fact that use of the Trading Window may not provide a "safe harbor" for the Insider. And,

**d)** Remain beyond the scope of the Insider's influence after implementation. In general, the Insider must allow the Pre-established Trade to be executed without changes to the accompanying instructions, and the Insider cannot later execute a hedge transaction that modifies the effect of the Pre-established Trade. An Insider wishing to change the amount, price or timing of a Pre-established Trade, or terminate a Pre-established Trade, can do so only during a "Trading Window" (discussed in Section 1, above). If the Insider has delegated decision-making authority to a third party, the Insider cannot

subsequently influence the third party in any way and such third party must not possess material non-public information at the time of any of the trades.

Prior to implementing a pre-established plan for trading, all officers and directors must receive the approval for such plan from our Insider Trading Compliance Officer. No pre-established plan or any amendment thereto may become effective until 30 calendar days after the execution date of any such plan or amendment.

### **3. Pre-Clearance of Trades**

Even during a Trading Window, all Insiders must comply with our "pre-clearance" process prior to trading in our securities, implementing a pre-established plan for trading, or delegating decision-making authority over the Insider's trades. To do so, each officer and director must contact our Insider Trading Compliance Officer prior to initiating any of these actions. However, once a pre-established plan or delegation of trading authority is approved by the Compliance Officer the Insiders shall not be required to pre-clear trades executed pursuant to the plan or delegated authority. We also require compliance with the pre-clearance process from all other employees, consultants and contractors, other than and in addition to officers and directors.

### **4. Individual Responsibility**

As Insiders, every person subject to this Policy has the individual responsibility to comply with this Policy against insider trading, regardless of whether we have recommended a Trading Window to that Insider or any other Insiders of our company. The guidelines set forth in this Policy are guidelines only, and appropriate judgment should be exercised in connection with any trade in our securities.

An Insider may, from time to time, have to forego a proposed transaction in our securities even if he or she planned to make the transaction before learning of the Material Nonpublic Information and even though the Insider believes he or she may suffer an economic loss or forego anticipated profit by waiting.

### **Applicability of Policy to Inside Information Regarding Other Companies**

This Policy and the guidelines described herein also apply to Material Nonpublic Information relating to other companies, including our customers, vendors or suppliers ("business partners"), when that information is obtained in the course of employment with, or other services performed on behalf of us. Civil and criminal penalties, as well as termination of employment, may result from trading on inside information regarding our business partners. All employees should treat Material Nonpublic Information about our business partners with the same care as is required with respect to information relating directly to our company.

Prohibition Against Buying and Selling Company Common Stock Within a Six-Month Period  
Directors, Officers and 10% Shareholders

Purchases and sales (or sales and purchases) of Company common stock occurring within any six-month period in which a mathematical profit is realized result in illegal

"short-swing profits." The prohibition against short-swing profits is found in Section 16 of the Exchange Act. Section 16 was drafted as a rather arbitrary prohibition against profitable "insider trading" in a company's securities within any six-month period regardless of the presence or absence of material nonpublic information that may affect the market price of those securities. Each executive officer, director and 10% shareholder of our company is subject to the prohibition against short-swing profits under Section 16. Such persons are required to file Forms 3, 4 and 5 reports reporting his or her initial ownership of our common stock and any subsequent changes in such ownership. The Sarbanes-Oxley Act of 2002 requires officers and directors ("insiders") who must report transactions on Form 4 to do so by the end of the second business day following the transaction date. Please note that the prohibition against short-swing profits and the reporting requirements apply to trades made pursuant to a pre-established plan or delegation of trading authority.

Profit realized, for the purposes of Section 16, is calculated generally to provide maximum recovery by us. The measure of damages is the profit computed from any purchase and sale or any sale and purchase within the short-swing (i.e., six-month) period, without regard to any setoffs for losses, any first-in or first-out rules, or the identity of the shares of common stock. This approach sometimes has been called the "lowest price in, highest price out" rule.

#### Inquiries

Please direct your questions as to any of the matters discussed in this Policy to our Insider Trading Compliance Officer.

#### Exhibit B

#### Section 16 Memorandum

**To:** All Officer, Directors and 10% Shareholders ("Section 16 Individuals")

**Re:** Overview of Section 16 Under the Exchange Act of 1934, as Amended

#### A. Introduction.

This Memorandum provides an overview of Section 16 of the Exchange Act of 1934, as amended (the "Exchange Act"), and the related rules promulgated by the Securities and Exchange Commission (the "SEC"). Although each executive officer, director and 10% shareholder (commonly called an "Insider") of AdvanSource Biomaterials Corporation is personally responsible for complying with the provision of Section 16, failure to comply strictly with its reporting provision will result in obligations on the part of our Company to publicly disclose such failure. Moreover, Congress has granted to the SEC authority to seek monetary court-imposed fines on Insiders who fail to timely comply with their reporting obligations.

Section 16(a) of the Exchange Act provides that insiders of a corporation with a class of securities registered under Section 12 of the Exchange Act (i) must file an initial report of their beneficial ownership of equity securities of the corporation (including derivative securities such as options, warrants and stock appreciation rights) as of the later of the date on which the corporation becomes subject to Section 12 of the Exchange Act or ten

days after the date they attain insider status, and (ii) must report subsequent changes in their beneficial ownership of equity and derivative securities of the corporation. Section 16(b) provides that insiders are liable to the corporation for any profits made on six-month short-swing transactions in the corporation's securities. Section 16(c) prohibits insiders from engaging in both traditional short sales of the corporation's securities and certain other transactions that are economically or functionally equivalent to a short sale.

## **B. Reporting Requirements Under Section 16(a).**

**1. General.** An Insider must disclose his or her holdings at the time he or she attains insider status and must disclose all subsequent changes in such holdings during the time the individual is an Insider (and, in certain circumstances, for up to six months after the individual ceases to be an Insider). Disclosure is made on one of three forms: the Initial Statement of Beneficial Ownership of Securities on Form 3; the Statement of Changes in Beneficial Ownership of Securities on Form 4; and the Annual Statement of Changes in Beneficial Ownership of Securities on Form 5.

### **2. Method of Filing.**

(a) SEC. The Sarbanes-Oxley Act mandates that all Form 4s must be filed electronically through EDGAR.

(b) Company. In addition, the rules under Section 16 require that a copy of the applicable Form be sent to our person designated by us to receive such reports at the same time that copies are sent to the SEC. If no person such has been designated, reports are to be sent to the Corporate Secretary at our principal executive offices. If the designated person at our company does not receive a copy of the Form within three days of its due date, we cannot presume that the filing with the SEC was timely made, which may result in the need to make disclosure of the late filing in our proxy statement.

(c) Filing Date. In the event that a due date falls on a weekend or SEC holiday, the Form will be deemed timely filed if it is received (or receipt is guaranteed) by the next business day after such weekend or holiday.

(d) Securities to be Reported. A person who is subject to Section 16 must only report as beneficially owned those securities in which he or she has a pecuniary interest. See the discussion of "beneficial ownership" below at Section D.

**3. Initial Report of Ownership - Form 3.** Under Section 16(a), Insiders are required to make an initial report on Form 3 to the SEC of their holdings of all equity securities of the corporation (whether or not such equity securities are registered under the Exchange Act). This would include all traditional types of securities, such as Common Stock, Preferred Stock and Junior Stock, as well as all types of derivative securities, such as warrants to purchase stock, options to purchase stock, puts and calls. Even Insiders who do not beneficially own any equity securities of our company must file a report on Form 3 to that effect.

(a) Initial Filing Deadline. The initial statement of ownership for persons who become officers, directors or 10% shareholders of our company must be filed within ten days

after the date on which they become an officer, director or 10% shareholder, and should reflect ownership as of the date they became such an Insider.

(b) One-Time Filing. An Insider is required to file an initial statement of beneficial ownership on Form 3 only once, unless such person ceases to be an Insider and later becomes an Insider again. Thus, an additional statement on such Form is not required when either (1) the Insider attains a second "Insider" position (such as the election of the President to the Board of Directors), or (2) an additional class of equity securities of our Company is registered under Section 12.

**4. Changes in Ownership - Form 4.** An Insider should use Form 4 to report (i) all transactions that are not exempt from Section 16(b), (ii) all exercises and conversions of derivative securities (e.g. stock options) regardless of whether they are exempt and (iii) vesting of options. Directors, officers and 10% shareholders of U.S. public companies will be required to file their Form 4 reports under Section 16 of the Exchange Act by the second business day after execution of a transaction.

(a) Prior Transactions. Our Insiders need not report transactions that occurred prior to the date they first became an officer, director or 10% shareholder, and those transactions may not become a basis for short-swing profit liability such Section 16(b). However, a director or officer who becomes subject to Section 16 solely as a result of the issuer first registering a class of its equity securities pursuant to Section 12 of the Exchange Act is subject to the reporting and liability provisions of Section 16 with respect to any transactions conducted in the six months prior to the first transaction requiring a filing on Form 4 after such registration.

(b) Termination of Insider Status. If a person ceases to be an officer or director, he or she continues to be subject to the reporting and liability provision of Section 16 for up to six months following termination of such status. As a result, he or she must file a Form 4 with respect to any non-exempt change in beneficial ownership which occurs within six months after any change in ownership which occurred before he or she ceased to be an officer or director. Such an individual must also file a Form 5 after his or her termination to report exempt and previously unreported transactions for that portion of the issuer's fiscal year during which he or she was an officer or director, as well as to report exempt and previously unreported transactions occurring within six months of the last transaction conducted while the person was an officer or director subject to Section 16.

A 10% shareholder whose beneficial ownership (under the Section 13(d) voting or investment control test) drops below 10% need not report any subsequent transactions on Form 4 after reporting less than 10% but must file a Form 5 with respect to any exempt or previously unreported transactions that occurred during the portion of the fiscal year that such person was a 10% shareholder.

Both Form 4 and Form 5 have an exit box that should be checked when the Insider after reporting less than 10% files his or her final Form 4 or Form 5 if a final filing is required.

(c) What Constitutes a Change in Beneficial Ownership. Generally, an Insider is deemed to have acquired (disposed of) beneficial ownership of a security at the time he or she makes a firm commitment to acquire (dispose of) the security. (Please see Section D below for a complete definition of "Beneficial Ownership.") If it is necessary that certain

conditions outside the Insider's control be satisfied prior to the consummation of the purchase or sale and if it is uncertain whether such conditions will be satisfied, the Insider will not be deemed to have acquired beneficial ownership or to have divested himself or herself until such time as the conditions prescribed are satisfied and the undertaking to purchase or sell becomes a firm commitment.

An Insider is deemed to have acquired ownership of a derivative security (whether issued by us or a third party) upon grant or acquisition, regardless of when it becomes exercisable. Similarly, an Insider is deemed to have disposed of ownership of a derivative security upon its sale, cancellation or expiration. See Sections B.6 and C below.

(d) Report Each Change of Ownership. Except for certain exempt transactions that may be reported on a Form 5, every change of ownership must be reported on Form 4.

**5. Special Transactional Reporting Requirements.** Changes in beneficial ownership that constitute exempt transactions under Section 16(a) or Section 16(b), other than the exercise of an option, need not be reported currently on Form 4. Such transactions fall into two categories: (i) those which must be reported in the annual filing on Form 5, and (ii) those which need not be reported at all. The following are some examples of transactions in these categories.

**(i) Annual Filing on Form 5**

(a) Small Acquisitions. Reporting an acquisition of an equity security not exceeding \$10,000 in market value, or of the right to acquire such securities, may be deferred until the annual filing on Form 5, so long as (A) total acquisitions of the same class of security (including securities underlying derivative securities) within the preceding six months do not exceed \$10,000 in market value, and (B) the person making the acquisition does not within six months thereafter make any disposition that is not exempt from Section 16(b) of the Exchange Act. Once either of the conditions described in (A) and (B) is not met, the small acquisition must be reported on Form 4 within ten days after the end of the calendar month in which the condition(s) fail.

(b) Gifts and Inheritance. Acquisitions and dispositions of our securities pursuant to bona fide gifts or by will or the laws of descent and distribution are exempt from the liability provisions of Section 16(b). Insiders need not report such acquisitions or dispositions until the Form 5 for the fiscal year in which such transaction occurs.

(c) Option Grants Under Rule 16b-3. The grant of an option to an Insider pursuant to Rule 16b-3 is exempt from liability and is reportable on Form 5. See Section C below.

**(ii) No Reporting Required.**

(a) Stock Splits and Stock Dividends. Insiders need not report the acquisition or disposition of stock via stock splits or stock dividends that are provided pro rata to all security holders, and such acquisitions and dispositions are exempt from the liability provision of Section 16(b). It is advisable for Insiders to use the extra space provided on Form 4 or Form 5 to explain any change in their holdings resulting from such events.

(b) Pro Rata Rights. Acquisitions of shareholder rights granted pro rata to all holders of a class of registered equity securities (including so-called "poison pill" shareholder rights) are exempt from the reporting and liability provisions of Section 16.

**6. Year-End Filing - Form 5.** An Insider must file a Form 5 within 45 days after the end of the issuer's fiscal year (May 14) unless all holdings and transactions that are required to be reported on Form 5 (including exempt transactions) have already been reported as of the date the Form 5 is due.

If not previously reported, the following transactions must be reported on Form 5: (a) any transaction during the last fiscal year that was exempt from the operation of the short-swing profit recovery rules under Section 16(b) (such as grants of options under Rule 16b-3); and (b) any holdings or transactions that should have been reported during our last fiscal year (two fiscal years for the first Form 5 filed) on a Form 3 or Form 4, but were not reported. The Form 5 filing requirements apply to each person who was an Insider during any portion of the applicable fiscal year.

**7. Reporting Obligations Regarding Certain Transactions in Derivative Securities.** In general, the acquisition or disposition of any option, warrant, put or call, whether or not transferable or then exercisable, is a reportable purchase or sale of the underlying security to which such derivative security relates, and requires the filing of a Form 4.

(a) Grant of Option or Warrant. If a derivative security is granted pursuant to Rule 16b-3, the otherwise reportable purchase is exempt and need not be reported until the annual filing on Form 5. If an Insider receives a derivative security other than pursuant to Rule 16b-3, the acquisition is deemed to be a purchase for Section 16 purposes and must be currently reported on Form 4.

(b) Exercise or Conversion of Option, Warrant or Other Right. The exercise of any option, warrant or other right to purchase securities must be currently reported on Form 4.

(c) Pledges. The right of a pledgee or borrower of securities to sell the pledged or borrowed securities is not a derivative security or "option" for purposes of Section 16, and the acquisition or disposition of such a right does not require the filing of a Form 4. Moreover, the SEC Staff has taken the position that bona fide pledges or loans of securities do not represent changes in beneficial ownership and need not be reported by the pledgor or lender. However, the sale of the pledged or borrower securities by the pledgee or borrower must be reported by the pledgor or lender and may result in Section 16(b) liability for the pledgor or lender.

(d) Rights Without a Fixed Price. Rights that do not have a fixed exercise or conversion price, such as a right to purchase stock at a future date at a specified percentage of its market value on the date of purchase, are not derivative securities and need not be reported, unless such rights have a floor or ceiling to the exercise or conversion price.

### **C. Securities Acquired Pursuant to Rule 16b-3.**

1. General. Rule 16b-3 generally provides exemptions from Section 16(b) for discretionary transactions by Insiders (e.g., not at the volition of the Insider). Rule 16b-3

provides that a grant or award of equity securities is exempt from Section 16 if any of the following conditions are met:

- (1) the transaction is approved in advance by the board of directors or a committee of the board composed solely of two or more non-employee directors;
- (2) the transaction is approved in advance by the shareholders, or subsequently ratified by the shareholders by the date of the next annual meeting of shareholders; or
- (3) the securities so acquired are held by the officer or director for six months following the date of such acquisition.

2. Transactions Must Comply with Rule 16b-3. Individual transactions must meet certain general requirements in order to qualify for beneficial treatment under Rule 16b-3.

#### **D. Determining Beneficial Ownership.**

The issue of beneficial ownership arises in two contexts under Section 16:

**1. Determining Who is a 10% Holder.** Beneficial ownership in the Section 16 context is determined by reference to Rule 13d-3, which provides that a person is the beneficial owner of securities if that person has or shares voting or disposition power with respect to such securities, or can acquire such power within 60 days through the exercise or conversion of derivative securities.

**2. Determining Beneficial Ownership for Reporting and Short-Swing Profit Liability.** For all Section 16 purposes other than determining who is a 10% holder, beneficial ownership means a direct or indirect pecuniary interest in the subject securities through any contract, arrangement, understanding, relationship or otherwise. "Pecuniary interest" means the opportunity, directly or indirectly, to profit or share in any profit derived from a transaction in the subject securities. Discussed below are several of the situations that may give rise to an indirect pecuniary interest.

(a) **Family Holdings.** An Insider is deemed to have an indirect pecuniary interest in securities held by members of the Insider's immediate family sharing the same household. Immediate family includes grandparents, parents (and step-parents), spouses, siblings, children (and step-children) and grandchildren, as well as parents-in-law, siblings-in-law, children-in-law and all adoptive relationships. An Insider may disclaim beneficial ownership of shares held by members of his or her immediate family, but the burden of proof will be on the Insider to uphold the lack of a pecuniary interest.

(b) **Partnership Holdings.** Beneficial ownership of a partnership's securities is attributed to the general partner of a limited partnership in proportion of such person's partnership interest. Such interest is measured by the greater of the general partner's share of partnership profits or of the general partner's capital account (including any limited partnership interest held by the general partner).

(c) Corporate Holdings. Beneficial ownership of securities held by a corporation will not be attributed to its shareholders who are not controlling shareholders and who do not have or share investment control over the corporation's portfolio securities.

(d) Derivative Securities. Ownership of derivative securities (warrants, stock appreciation rights, convertible securities, options and the like) is treated as indirect ownership of the underlying equity securities. Acquisition of derivative securities must be reported, although the timing of such reporting depends upon the Rule 16b-3 status of the employee plan under which the grant was made.

#### **E. Delinquent Filings.**

1. Disclosure Requirements. Item 405 of Regulation S-K requires the Company to disclose in its proxy statements, information statements and Annual Reports on Form 10-KSB information regarding delinquent filings under Section 16(a) by Insiders. Our Company must identify by name its Insiders who, during the fiscal year, reported transactions late or failed to file required reports, and must disclose the number of delinquent filings and transactions for each such Insider. We do not have an obligation to research and make inquiry regarding the delinquent Section 16(a) filings but may rely on the information disclosed on Forms 3, 4 and 5. We may also rely on a written representation from the Insider that no Form 5 filing is required but should retain the representation for two years. The cover page of Form 10-KSB has been amended to provide a box which can only be checked by us if we know at the time of filing that there are no delinquent filings that will require disclosure pursuant to Item 405. The SEC has indicated that it will select for review any Form 10-KSB that does not have the box checked and that they will be using the disclosure of delinquencies to assist in their enforcement efforts.

2. Correcting Late Filings. If a particular transaction or holding has not been reported, the Insider must file a new form for the transaction. The transaction reported in an untimely manner would be disclosed pursuant to Item 405 for the fiscal year in which the report was filed, even if the transaction related to and should have been reported in a prior fiscal year.

3. Potential Liability. The SEC has been empowered by Congress to seek civil penalties against those who fail to comply with the reporting requirements of Section 16. Penalties may be sought for any violations occurring on or after October 15, 1990. Penalties for failure to timely file may range from \$5,000 to \$100,000 per violation. Moreover, if the SEC obtains a cease-and-desist order prohibiting future violations of the reporting requirements under Section 16, each day that a filing is late may be treated as a separate offense, thereby multiplying the penalty amount by the number of days that the form is delinquent.

#### **F. Other Prohibited Insider Transactions Under Section 16(c).**

Section 16(c) of the Exchange Act provides that it is unlawful for an Insider to sell any equity security (including a derivative security) of the corporation if the person selling the security (1) does not own the security sold, or (2) owns the security but does not deliver it against such sale within 20 days thereafter, or does not, within five days after such sale, deposit it in the mails or other usual channels of transportation.

Clause (1) above is directed to the tradition "short sale" where the seller borrows stock to make delivery on sale and repays his or her loan with securities purchased thereafter.

Clause (2) above is directed to either long sales or "short sales against the box" where delivery is not made within the required time limits.

The interactions of Section 16(c) with the derivative securities concept is not entirely clear, but the establishment of or increase in a "put equivalent position" (a broadly defined term that includes any type of short position) is considered functionally and economically equivalent to a prohibited short sale if the Insider does not own underlying securities sufficient to cover the put equivalent position.

### **Exhibit C**

#### Pre-Clearance Checklist

Individual Proposing to Trade: \_\_\_\_\_

Number of Shares covered by Proposed Trade: \_\_\_\_\_

Date: \_\_\_\_\_

\_\_\_\_ Trading Window. Confirm that the trade will be made during our "trading window."

\_\_\_\_ Section 16 Compliance. Confirm, if the individual is subject to Section 16, that the proposed trade will not give rise to any potential liability under Section 16 as a result of matched past (or intended future) transactions. Also, ensure that a Form 4 has been or will be completed and will be timely filed.

\_\_\_\_ Prohibited Trades. Confirm, if the individual is subject to Section 16, that the proposed transaction is not a "short sale," put, call or other prohibited or strongly discouraged transaction.

\_\_\_\_ Rule 144 Compliance. Confirm that:

\_\_\_\_ Current public information requirement has been met;

\_\_\_\_ Shares are not restricted or, if restricted, the one year holding period has been met;

\_\_\_\_ Volume limitations are not exceeded (confirm that the individual is not part of an aggregated group);

\_\_\_\_ The manner of sale requirements have been met; and

\_\_\_\_ The Notice of Form 144 Sale has been completed and filed.

\_\_\_\_ Rule 10b-5 Concerns. Confirm that (i) the individual has been reminded that trading is prohibited when in possession of any material information regarding us that has not been adequately disclosed to the public, and (ii) the Insider Trading Compliance Officer has discussed with the individual any information known to the individual or the Insider Trading Compliance Officer which might be considered material, so that the individual has made an informed judgment as to the presence of inside information.

\_\_\_\_\_  
Signature of Insider Trading Compliance Officer

Transactions Report

Officer or Director:

**I. Transactions in \_\_\_\_\_ (specify dates):**

\_\_\_\_ No transactions

\_\_\_\_ The transactions described below

Owner of Record	Transaction Date (1)	Transaction Code (2)	Security (Common, Preferred)	Number of Securities Acquired	Number of Securities Disposed of	Purchase/Sale Unit Price

- (1) (a) Brokerage transactions - trade date  
(b) Other purchases and sales - date firm commitment is made  
(c) Option and SAR exercises - date of exercise

- d) Acquisitions under stock bonus plan - date of grant  
(e) Conversion - date of surrender of convertible security  
(f) Gifts - date on which gift is made

**(2) Transaction Codes:**

- (P) Pre-established Purchase or Sale  
(N) Purchase or Sale (not "Pre-established")  
(G) Gift  
(M) Option exercise (in the money option)

- (Q) Transfer pursuant to marital settlement  
(U) Tender of shares  
(W) Acquisition or disposition of will  
(J) Other acquisition or disposition (specify)

**II. Securities Ownership After Sale**

**A. Our Securities Directly or Indirectly Owned (other than stock options noted below):**

Title of Security (e.g., Preferred, Common, etc.)	Number of Shares/Units	Record Holder (if not Reporting Person)	Relationship to Reporting Person

**B. Stock Option Ownership:**

Vesting Dates Expiration Date Exercises to Date (Date, No. of Shares)

Date of Grant	Number of Shares	Exercise Price	Vesting Dates	Expiration Date	Exercises to Date (Date, No. of Shares)