Prospectus

DynaPel

DynaPel Systems Inc.

Partly underwritten Initial Public Offering

Share Capital Increase of minimum 5,714,286 shares
and maximum 6,000,000 shares

Subscription Price: NOK 3.50 per share

Total gross proceeds between NOK 20,000,000 and NOK 21,000,000

Subscription period from and including 13 January 2005 to and
including 18 January 2005 at 16:00 hrs (CET)

Application for listing of the shares on the SMB List of Oslo Børs

Manager

DnB NOR
Markets

13 January 2005

Important Information

This Prospectus has been prepared in connection with the initial public offering (the "IPO") of a minimum of 5,714,286 new shares and a maximum of 6,000,000 new shares (the "Shares") of DynaPel Systems, Inc ("DynaPel") on Oslo Børs (the "Share Issue") as more fully described herein.

Except for the approval by Oslo Børs as described below, no action has been taken or will be taken to permit the offering of the Shares, or the distribution of this Prospectus or any other documents relating to the Share Issue, in any country or jurisdiction where specific action would be required for such purposes. Accordingly, this Prospectus may not be distributed into, or used for the purpose of an offer for or solicitation of any securities, under any circumstances or in any jurisdiction in which such offer or solicitation is not lawful or authorised, including but not limited to the United States, the United Kingdom, Canada, Australia and Japan. No person is authorised to give any information or to make any representation not contained in this Prospectus in connection with the Share Issue, and any information or representation not so contained must not be relied upon as having been authorised by or on behalf of DynaPel.

This Prospectus does not constitute an offer to sell, or a solicitation to purchase, any of the securities offered hereby, by or on behalf of DynaPel, the Manager, any of their respective affiliates or any other person in any jurisdiction in which it is unlawful for any person to make such an offer or solicitation. The distribution of this Prospectus and the Share Issue may in certain jurisdictions be restricted by law. Persons into whose possession this Prospectus may come are required by DynaPel and the Manager to inform themselves about, and to observe, such restrictions. DynaPel does not accept any legal responsibility for any violation by any person, whether or not a prospective purchaser of the Shares, of any such restrictions.

The Share Issue is being offered outside the United States, in offshore transactions in reliance on Regulation S ("Regulation S") under the United States Securities Act of 1933, as amended (the "Securities Act"). The Share Issue has not been and will not be registered under the Securities Act, has not been approved or disapproved by the United States Securities Exchange Commission, any state securities commission of the United States or any other regulatory authority thereunder, and none of the foregoing authorities have passed upon or endorsed the merits of the Share Issue or the accuracy or adequacy of this Prospectus. As a result, the Shares may not be offered or sold within the United States except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state securities laws. Prospective subscribers of Shares in the Share Issue are hereby notified that the offered Shares are also subject to certain additional restrictions on transfer. See "Transfer Restrictions" in section 2.10.

Persons into whose possession this Prospectus may come are required by the Company and the Manager to inform themselves about, and to observe such restrictions.

The information contained herein is as of the date hereof and subject to change, completion or amendment without notice. In accordance with section 14-6 of the Norwegian Stock Exchange Regulation (the "Stock Exchange Regulation") and section 5-5 of the Norwegian Securities Trading Act (the "Securities Trading Act"), if any significant new factor or inaccuracy arises that might have a significant effect on the assessment of the Shares offered in connection with the Share Issue that emerges between the time of disclosure of the Prospectus and the end of the subscription period described herein, it will be included in a supplement to the Prospectus as required under the Securities Trading Act and the Stock Exchange Regulation. Neither the publication nor distribution of this Prospectus nor any sale made hereunder shall under any circumstances create any implication that the information herein is correct as of any date subsequent to the date of the Prospectus.

All inquiries relating to this Prospectus should be directed to the Manager.

In the ordinary course of their respective businesses, the Manager and/or certain of its affiliates may have engaged in, and may in the future be engaged in investment banking and commercial banking transactions with DynaPel and its subsidiaries and affiliates.

This Prospectus has been prepared to comply with the Stock Exchange Regulation and the Securities Trading Act. The Prospectus has been prepared solely in the English language. The Oslo Børs has reviewed and approved this Prospectus in accordance with the Securities Trading Act section 5-7 and the Stock Exchange Regulation section 14-4.

Any disputes that might arise regarding this Prospectus or the offer of the securities described herein are subject to Norwegian law and the exclusive jurisdiction of the Norwegian courts.

This Prospectus includes certain "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the United States Securities Exchange Act of 1934 (the "Exchange Act") that are based on DynaPel's current expectations, estimates and projections. Pursuant to those sections, DynaPel may obtain a "safe harbor" for forward-looking statements by identifying those statements and by accompanying those statements with cautionary statements, which identify factors that could cause actual results to differ from those expressed in the forward-looking statements. The words "believe", "expect", "anticipate", "aim", "intend", "will" and "plan" and similar expressions identify forward-looking statements. All statements other than statements of historical fact included in this Prospectus, including without limitation, those regarding DynaPel's financial position, business strategy, plans and objectives of management for future operations (including development plans and objectives relating to DynaPel's products), are forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of DynaPel to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such forward-looking statements are based on numerous assumptions regarding DynaPel's present and future business strategies and the environment in which DynaPel will operate in the future. The important factors that could cause DynaPel's actual results, performance or achievements to differ materially from those in the forward-looking statements include, among others, the lack of market acceptance of DynaPel's products, DynaPel's inability to manage growth, the competitive environment in relation to DynaPel's business area and market, DynaPel's inability to attract and retain qualified personnel, changes and development in technology which may render DynaPel's products obsolete, and other factors discussed herein, under "Risk Factors". Additional factors that could cause actual results, performance or achievements to differ materially include, but are not limited to, those discussed under "Risk Factors". Further, certain forward-looking statements are based upon assumptions of future events which may not prove to be accurate. The forward-looking statements in this document speak only as of the date of this Prospectus. DynaPel expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statement contained herein to reflect any change in DynaPel's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

DynaPel prepares its financial statements in conformity with generally accepted accounting principles in the United States ("U.S. GAAP"). DynaPel prepares its financial statements in U.S. Dollars. Financial information in this Prospectus has been presented in U.S. Dollars and has been translated from U.S. Dollars to NOK's at the exchange rate referred to herein.

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Definitions

Board	The Board of Directors of the Company.
Company or Group	DynaPel Systems Inc and subsidiaries.
Company Registry	The Norwegian Register of Business Enterprises (Foretaksregisteret).
DnB NOR Markets	DnB NOR Bank ASA, DnB NOR Markets.
DynaPel	DynaPel Systems Inc, a US public limited company incorporated in the State of Delaware, and including its subsidiary Holon Technology GmbH when applicable. DynaPel Systems Inc's organisation number is 2309086, and its principle office is at 2235 First Street, Suite 215 Fort Myers, Florida, USA.
EBT	Earnings before taxes.
EBIT	Earnings before interest and taxes.
EBITDA	Earnings before interest, taxes, depreciation and amortization.
EUR	The currency of the European Union (Euro).
Holon Technology GmbH	Holon Technology GmbH, a 100% subsidiary of DynaPel Systems Inc, is a German private limited company with its office in Munich.
Initial Public Offering (IPO)	Initial Public Offering of the DynaPel shares on the SMB List on Oslo Børs as described in this Prospectus.
Manager	DnB NOR Bank ASA, DnB NOR Markets.
NOK	The currency of the Kingdom of Norway (Norwegian kroner).
Oslo Børs	Oslo Børs ASA.
Prospectus	This Prospectus prepared in connection with the Share Issue and application for stock exchange listing and any attachments hereto.
Subscription Office	DnB NOR Markets.
Subscription Period	From and including 13 January 2005 to and including 16.00 hrs CET on 18 January 2005.
Securities Trading Act	The Norwegian Securities Trading Act of 19 June 1997 No. 79.
Share Issue	The issue of minimum 5,714,286 and maximum 6,000,000 new shares of DynaPel as described herein in relation to the IPO.
Shares	Shares of DynaPel, including the shares to be issued according to the Share Issue when applicable.
Stock Exchange Regulation	The Norwegian Stock Exchange Regulation of 17 January 1994 No. 30.
Subscription price	The price to be paid per DynaPel share in the Share Issue.
Underwriting Syndicate	Existing and new investors guarantee for the underwritten amount as described in section 2 of this Prospectus.
USD	The currency of the United States of America (US Dollar).
VPS	The Norwegian Central Securities Depository (Verdipapirsentralen).
VPS-account	An account with the VPS to register ownership of the DynaPel shares.

Terms and expressions

ASF	Advanced Streaming Format (extension to AVI)
AVI	Audio/Video Interlaced
CCTV	Closed Circuit Television
Codec	Video compression/decompression application
DNA	Name of DynaPel Co-Processor
DSL	Digital Subscriber Line
DSP	Digital Signal Processing chips
LAN	Local Area Network
MPEG	Moving Picture Expert Group, a part of the International Standards Organisation (ISO)
OEM	Original Equipment Manufacturer
SDK	Software Development Kit
PTZ	Pan Tilt Zoom camera

Statements of Responsibility

The Board of Directors

This Prospectus has been prepared in connection with the Initial Public Offering and the issue of new common shares with par value USD 0.50 in DynaPel Systems Inc on Oslo Børs ASA. This Prospectus has been prepared with the intention of giving as full and accurate picture of DynaPel Systems Inc and Holon Technology GmbH as possible.

The Board of Directors of DynaPel Systems Inc acknowledges responsibility for the information contained in this Prospectus and confirms that to the best of our knowledge, the information is in accordance with the facts and contains no omissions likely to affect the import of this Prospectus.

DynaPel Systems Inc's future results of operations involve a number of risks and uncertainties. Factors that could affect DynaPel Systems Inc's future operating results, hereunder cause actual results to vary materially from expectations, include, but are not limited to, rapid technology change, uncertainty of market acceptance of DynaPel Systems Inc's products and services, competition from substitute products and larger companies, protection of proprietary technology, the ability to generate sufficient capital to fund operations, strategic relationships and dependence on key individuals, in addition to the "Risk Factors" described in section 9 in this Prospectus.

Management expectations, plans for the future, opinions, beliefs and other forward looking statements described in this Prospectus have been made to the best of our existing knowledge and belief and should be considered together with the information set forth in "Risk Factors" in section 9 of this Prospectus.

Oslo, 13 January 2005

The Board of Directors of DynaPel Systems Inc

Helge Nielsen Chairman of the Board	Ralph Carballal Board member	Live Haukvik Aker Board member	Ivar Formo Board member

Manager

DnB NOR Markets has as Manager assisted DynaPel Systems Inc in preparing this prospectus in co-operation with the Board of Directors and the Management in DynaPel Systems Inc on the background of information sent from and obtained in co-operation with the Board of Directors and the Management in DynaPel Systems Inc.

The Manager has been aiming to give complete and correct information of DynaPel Systems Inc including its subsidiary. The Manager does however not take any responsibility, for whatever reason, for the accuracy or completeness of the information included in this Prospectus or for any legal or financial liability related to possible decisions based on information presented in the Prospectus.

The Board of Directors, the managing director and the financial director in DynaPel Systems Inc have given a declaration of completeness relating to the information the Manager has received in relation to the preparation of this Prospectus.

A legal due diligence review of DynaPel Systems Inc has been coordinated by Advokatfirmaet Selmer DA, and carried out by local counsels. A financial due diligence review of DynaPel Systems Inc has been coordinated by Kjelstrup & Wiggen, and carried out by local advisors.

DnB NOR Markets is a division in DnB NOR Bank ASA, which is owned by DnB NOR ASA. As of the date of this Prospectus, DnB NOR Bank ASA including subsidiaries owned 0 shares in DynaPel.

Oslo, 13 January 2005

DnB NOR Bank ASA, DnB NOR Markets

Legal Advisor to the Manager

Advokatfirmaet Selmer DA has acted as Norwegian legal advisor to DnB NOR Bank ASA, DnB NOR Markets in connection with the Share Issue of DynaPel Systems Inc and the preparation of this Prospectus.

On behalf of DnB NOR Bank ASA, DnB NOR Markets, Advokatfirmaet Selmer DA has coordinated a legal due diligence review of DynaPel Systems Inc and Holon Technology GmbH, which has been carried out by local counsels in the United States and in Germany, and engaged by DnB NOR Bank ASA, DnB NOR Markets. Advokatfirmaet Selmer DA has not itself performed any due diligence of DynaPel Systems Inc and Holon Technology GmbH.

Based on the information received by us, it is our opinion that the description included in section 11.3 "Taxation of Norwegian Shareholders" and section 11.4 "Legal Issues" in this Prospectus gives a fair description of the relevant taxation and legal matters governed by Norwegian law described therein.

Our statement does not cover any other parts of this Prospectus other than referred to above, and does not include commercial, technical, accounting, financial or economical matters. Our statement is also limited to matters governed by Norwegian law.

Advokatfirmaet Selmer DA

Oslo, 13 January 2005

1 Executive Summary

This summary is produced as a supplement to the more detailed information contained in the Prospectus as a whole and the Appendices. Investors who are considering whether to subscribe for shares in the Share Issue are strongly encouraged to read the entire Prospectus, including Chapter 9 on "Risk Factors", in order to make their own judgment.

1.1 Description of the Company

1.1.1 Corporate History

In 1988, two Norwegian research scientists, Dr. Gudesen and Dr. Martens, began an R&D initiative that led to several technology companies, one of which is DynaPel. DynaPel was founded in 1992 and develops intelligent video products for the surveillance and broadcast industries. Today, the company has started to receive orders from its OEM and integrator sales channels for end user installation of DynaPel's products.

1.1.2 Business Description

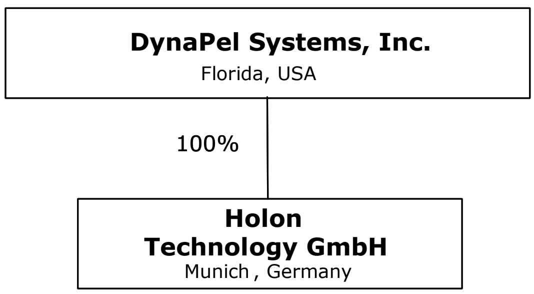
DynaPel is aiming for technology leadership for intelligent video analysis and solutions in the video surveillance industry, which is defined as the Company’s core business. This will be achieved through a close co-operation with a worldwide network of security integrators and OEM-partners. DynaPel has developed products and applications in the specific areas of video algorithm, digital video motion analysis, video compression and control.

DynaPel is organizing its sales and marketing efforts to operate effectively through both OEM channels and the well-established distributor/manufacturer’s representative/system integrator channels.

The Company emphasises on R&D activities through the 100% owned subsidiary Holon Technology GmbH. The focus area for the foreseeable future product development of DynaPel is in the Security Surveillance space.

1.1.3 Organization

The operating entities in the DynaPel Systems are shown in the following chart.



DynaPel Systems Inc is a US corporation incorporated in the state of Delaware with headquarter in Fort Myers, Florida, USA, where the accountant, sales, marketing, technical support and logistic functions are located. DynaPel’s research and development activities, including the engineering team, are located in Munich, Germany, through the 100% owned subsidiary Holon Technology GmbH.

DynaPel’s former German subsidiary, DynaPel Laboratories GmbH, filed for insolvency proceedings in January 2004. The insolvency proceedings are not finished. The newly incorporated subsidiary, Holon Technology GmbH, has continued the former subsidiary’s operations. See section 7.1 for further details.

1.2 Risk factors

DynaPel Systems Inc is a relatively young company, with new products in an immature market. Therefore, investing in DynaPel involves inherent risks. Prospective investors should carefully consider the risk factors discussed in chapter 9, other information contained in this Prospectus, and their own information and analysis before making an investment decision.

Investors should especially be aware of that DynaPel in 2004, prior to the IPO, has been in a very difficult financial position with very limited liquidity. According to the independent auditor's report (dated 27 August, 2004) for the audited annual accounts for 2003 and the interim report for the first half year 2004 (Appendix 2 and 3 to this Prospectus), DynaPel had a net capital deficiency which raises substantial doubt about its ability to continue as a going concern. Hence, DynaPel was obliged to issue a convertible bridge loan described in section 8.8, section 8.9 and section 10.7 , to secure ongoing business before the IPO.

DynaPel's success is heavily dependent on proprietary technology. However, protection from laws and procedures is only limited. Despite precautions, investors should be aware that unauthorized third parties may copy or reverse engineer aspects of the current or future products, or independently develop similar or superior technology to DynaPel. Third parties, including competitors and former employees, may also claim that DynaPel's current or future products infringe their proprietary rights. Such claims, rightful or not, can potentially have a very negative effect. No such claim have been put forward by any third party against DynaPel to date.

1.3 Financial information

The following table provides a summary of the profit and loss account, balance sheet and selected key figures for the Company for the years 2001, 2002, 2003 and the three first quarters of 2003 and 2004. A more extensive description of the Company's financial situation can be found in Chapter 8 of this Prospectus and the Company's Annual Report and Accounts for 2003 in Appendix 3 to this Prospectus.

Figures in USD	**Q3 2004 (unaudited)**	**Q32003 (unaudited)**	**2003**	**2002**	**2001**
Operating income	644,323	1,204,583	1,590,036	1,432,287	1,424,168
Operating expenses	2,056,262	2,770,488	3,986,488	3,572,809	3,812,239
Net result	6,882,932	(1,565,788)	(2,393,325)	(2,556,847)	(2,404,153)
Per share data	**Q3 2004**	**Q3 2003**	**2003**	**2002**	**2001**
Earnings per share	0.22	(0.17)	(0.29)	(0.68)	(1.18)
Earnings per share fully diluted	0.20	(0.12)	(0.18)	(0.50)	(0.98)
Outstanding shares	30,855,458	9,429,237	8,383,336	3,747,815	2.035,022
Outstanding shares fully diluted	33,879,934	12,754,940	12,948,957	5,163,834	2,442,297
Per share data (after reverse split 5:1)					
Earnings per share	1.12	(0.83)	(1.43)	(3.41)	(5.91)
Earnings per share fully diluted	1.02	(0.61)	(0.92)	(2.48)	(4.92)
Outstanding shares	6,171,092	1,885,847	1,676,667	749,563	407,004
Outstanding shares fully diluted	6,775,987	2,550,988	2,589,791	1,032,767	488,459
Figures in NOK	**Q3 2004**	**Q3 2003**	**2003**	**2002**	**2001**
Total current assets	579,121	449,980	106,384	185,912	792,590
Total fixed assets	76,744	57,978	49,914	75,372	113,238
Total assets	655,865	507,958	156,298	261,284	905,828
Total equity (shareholders´deficit)	(697,091)	(9,636,516)	(10,480,194)	(9,676,998)	(8,354,963)
Total liabilities	1,352,956	10,244,193	10,636,492	9,938,282	9,260,791
Total equity and liabilities	655,865	507,958	156,298	261,284	905,828

1.4 The Share Issue and Stock Exchange listing

In connection with the IPO, a public offer for the subscription of minimum 5,714,286 new shares and maximum 6,000,000 new shares will be completed at a subscription price of NOK 3.50 per new share. The gross proceeds from the Share Issue is between NOK 20 million and NOK 21 million.

The admission of the DynaPel shares on the SMB List on Oslo Børs is, as described in section 2.12 and section 10.3, conditioned that a share issue with proceeds of minimum NOK 20 million is completed. The Share Issue is conditioned that the Company in relation to the Share Issue receives proceeds of minimum NOK 20 million. In addition, the Share Issue is conditioned that the exchange rate between USD and NOK provide for a subscription price in NOK in the Share Issue of more than the par value of USD 0.50 per share.

The Company's share capital following the Share Issue will be minimum USD 6,065,828.50 consisting of 12,131,657 shares and maximum USD 6,208,685.50 consisting of 12,417,371 shares.

The Share Issue has been partly guaranteed by an Underwriting Syndicate, consisting of existing and new investors, in order to subscribe and pay for shares of an amount of NOK 20 million (the underwritten amount).

1.5 Bridge Loan

In September 2004, in order to finance operations in Q4 2004, DynaPel entered into a short term secured convertible bridge loan. The initial loan was NOK 4.2 million and in October and December additional funds were drawn down under the bridge loan so that a total of NOK 7 million has been loaned to the Company per 31 December, 2004. The loan has an interest rate of 20% p.a. At the discretion of each lender, the loan, plus accrued interest plus a risk premium factor of 25% can be converted into shares of the Company at a conversion price equal to the Subscription Price in the Share Issue described in section 2. The loan is secured by DynaPel's assets. See section 8.8, section 8.9 and section 10.7 for further details on the short term secured bridge loan.

1.6 Authorized Share Capital

The Company currently has a total of 14,000,000 authorized shares. Following the Share Issue the maximum number of outstanding shares will be 12,417,371 shares. In addition, the Company has outstanding options under the Company's stock option plans as described in section 10.6 and warrants as described in section 10.7. Further, the convertible bridge loan, as described in section 1.5 above, will, if fully converted, be converted into approximately 2,670,000 shares. This can be summarized as follows:

	Shares
Currently issued shares	6,417,371
Maximum under the Share Issue	6,000,000
Outstanding options	88,800
Warrants to Dieter Kondek*	500,000
Warrants to Procon AS*	400,000
Conversion of bridge loan**	Approx. 2,670,000
2004 Stock option plan***	1,230,000
Total	**17,306,171**

* The warrants for Mr. Kondek and Procon AS are subject to completion of the IPO, and conversion into shares will be subject to an increase in authorized shares.

** A majority of the lenders in the short term secured convertible bridge loan have, if they decide to exercise their conversion rights under the loan agreement, accepted to postpone conversion and the delivery of new shares to their VPS accounts until DynaPel has held a shareholder meeting and subject to an authorisation to increase the number of authorised shares sufficient to issue the shares (one of the lenders has specified that the shareholder meeting to be held no later than July 2005). The number of shares to be converted under the short term bridge loan may vary depended on the accrued interest which also may be converted into shares.

*** The options related to the 2004 stock option plan have not been granted. The option grant agreements will include provisions that exercise will be subject to the Company having sufficient number of authorized shares at time of exercise.

Because the Company has not a sufficient number of authorized shares to accommodate all of the potential share distributions listed above, the Company will, at the next shareholders meeting (planned held before the end of April 2005), propose to increase the number of authorized shares.

2 Details of the Share Issue

In connection with the IPO, a public offering for the subscription of between 5,714,286 new shares and 6,000,000 new shares will be completed at a subscription price of NOK 3.50 per new share. The gross proceeds from the Share Issue will be between NOK 20 million and NOK 21 million.

The Share Issue has been partly guaranteed by an underwriting syndicate consisting of existing and new investors (the "Underwriting Syndicate"). The Underwriting Syndicate has agreed to subscribe and pay for Shares of DynaPel in the amount of NOK 20 million (the "Underwritten Amount").

The admission of the DynaPel shares on the SMB List on Oslo Børs is, as described in section 2.12 and section 10.3, conditioned that a share issue with proceeds of minimum NOK 20 million is completed. The Share Issue is conditioned that the Company in relation to the Share Issue receives proceeds of minimum NOK 20 million. In addition, the Share Issue is conditioned that the exchange rate between USD and NOK provide for a subscription price in NOK in the Share Issue of more than the par value of USD 0.50 per share.

2.1 The Company's share capital before and after the Share Issue

DynaPel's share capital as of the date of this Prospectus was USD 3,208,685.50 consisting of 6,417,371 shares, each of par value USD 0.50 and fully paid. DynaPel has one class of shares and each share carries one vote at DynaPel's general shareholder meeting.

DynaPel's share capital following the Share Issue will be a minimum of USD 6,065,828.50 consisting of 12,131,657 shares and a maximum of USD 6,208,685.50 consisting of 12,417,371 shares.

DynaPel conducted a reverse stock split in November 2004 whereby each share of common stock of DynaPel issued and outstanding or in treasury was combined into shares of common stock of DynaPel at a ratio of 5:1.

2.2 The Share Issue

DynaPel will issue a minimum of 5,714,286 new shares and a maximum of 6,000,000 new shares, each with a par value of USD 0.50, corresponding to a share capital increase of a minimum of USD 2,857,143 and a maximum of USD 3,000,000. The Board of Directors of DynaPel adopted on 6 January, 2005 a formal resolution authorizing the Share Issue which resolution authorised DynaPel to issue up to a maximum of 6,000,000 shares.

The new shares shall be issued at a subscription price of NOK 3.50 per share.

The gross proceeds from the Share Issue will be between NOK 20 million and NOK 21 million.

The Share Issue will be carried out as a public share offering and allocated to investors according to the allocation criteria described in section 2.8. The shareholders of DynaPel do not have pre-emption rights in relation to this Share Issue (see section 11.2 with regards to pre-emption rights for shareholders in DynaPel). DynaPel has a limited number of shareholders in various jurisdictions. DynaPel deems the cost of preparing offering documents in each of such jurisdictions to exceed the benefit from each such subscriber, especially taking into account the fact that such shareholders may acquire DynaPel's Shares on the Oslo Børs immediately following the IPO. If made in accordance with applicable law, subscriptions from foreign shareholders and investors will be accepted as described in section 2.8 below.

The admission of the DynaPel shares on the SMB List on Oslo Børs is, as described in section 2.12 and section 10.3, conditioned by Oslo Børs that a share issue with proceeds of minimum NOK 20 million is completed. The Share Issue is conditioned that the Company in relation to the Share Issue receives proceeds of minimum NOK 20 million.

In addition, the Share Issue is conditioned that the exchange rate between USD and NOK provide for a subscription price in NOK in the Share Issue of more than the par value of USD 0.50 per share.

Subscription for Shares in the public offering shall be made pursuant to the subscription form attached to this Prospectus as Appendix 4 and shall take place during the period beginning and including 13 January 2005 and ending on 18 January 2005 at 16.00 hrs CET.

The Shares carry rights to dividends, if declared by the Board of Directors of the Company, from and including DynaPel's fiscal year 2004 and shall otherwise rank equally with the existing shares from the time when the share capital increase is registered with DynaPel's shareholder register with the Norwegian Central Securities Depository (the "VPS").

The Share Issue has been authorised by a resolution of shareholders of DynaPel at a shareholder meeting held on 18 November 2004, which meeting also decreased the authorised share capital of DynaPel from 70,000,000 to 14,000,000 shares in respect of the 1 for 5 reversed stock split.

2.3 Underwriting Syndicate

The Share Issue has been partly guaranteed by an Underwriting Syndicate consisting of existing and new investors. The Underwriting Syndicate has agreed to subscribe and pay for Shares of DynaPel in the amount of NOK 20 million. The guaranteed Underwritten Amount shall be distributed pro-rata among the participants in the Underwriting Syndicate. Participating in the Underwriting Syndicate carries a right to an allotment of Shares corresponding to 50% of the Underwritten Amount and which corresponds to 2,857,143 Shares of the Share Issue. The allotment criteria is described in section 2.8 below. Subject to the consummation of the Share Issue, the Underwriting Syndicate is entitled to receive an underwriting commission of 5% of the Underwritten Amount.

The underwriting agreements for the Underwriting Syndicate are conditioned that DynaPel resolves the necessary corporate resolutions in order to complete the Share Issue, that the exchange rate between USD and NOK provide for a subscription price in NOK in the Share Issue of more than the par value of USD 0.50 per share, and that the board of directors of Oslo Børs approves the listing of DynaPel’s shares on the SMB List on Oslo Børs.

Below is a table of all the underwriters and respective underwritten amounts (figures in approx. numbers):

Name	Amount NOK mill
Simask AS	3,600,000
Ousdal AS	2,600,000
Haakon Sæter	2,300,000
Spencer Trading Inc.	2,300,000
Caicos Investment Ltd	1,500,000
Portfolio Management AS	1,400,000
Frans Enger AS	1,000,000
Novestra AS	1,000,000
Predator Capital Management AS	1,000,000
Morten Werrings Rederi AS	750,000
Brødr. Hetland AS	750,000
Lars Sigvart Gran Andersen	500,000
Atlas Capital Management Ltd	500,000
Chico AS	500,000
Andersen Holding AS	200,000
Terje Veel	100,000
Total	**20,000,000**

2.4 Subscription Price

The price of each share issued or sold through the Share Issue will be NOK 3.50 per Share.

The subscription price has been calculated on the basis of an overall evaluation of DynaPel, including due consideration of the historical trading price on the over-the-counter market (the "OTC"), the marketing process on behalf of the Underwriting Syndicate, previous share issues, DynaPel's historical and expected future earnings, future market prospects, as well as the expected demand for DynaPel's Shares.

2.5 Subscription for shares

Subscriptions for Shares in the Share Issue must be made on the subscription form attached hereto as Appendix 4 during the period from and including 13 January 2005 and ending on 16.00 hrs CET on 18 January 2005 (the "Subscription Period"). Copies of the Prospectus and the subscription forms can be obtained on request from the Manager.

Subscription forms must be received by the Subscription Office no later than 16.00 hrs CET on 18 January 2005. Subscriptions received are legally binding on the subscriber upon receipt by the Subscription Office. Unlawful, incorrect or incomplete subscription forms or subscriptions forms received after the expiry of the Subscription Period, may be disregarded without notice to the subscriber.

Subscribers must have a VPS account in order to be allotted Shares. If a subscriber does not have a VPS account, such account must be opened by the Subscriber by contacting the Subscription Office, or by opening one with a bank, post office or investment firm in Norway.

2.6 Minimum subscription

The minimum subscription amount has been set at a round lot expected to consist of 2,000 Shares. Subscriptions made for an aggregate number of Shares less than 2,000 will be disregarded without any further notice or warning to the subscriber.

2.7 Subscription Office

The Subscription Office is:

DnB NOR Bank ASA
DnB NOR Markets

0021 OSLO

Telephone: +47 22 94 88 80
Fax: +47 22 83 20 00

2.8 Allotment of Shares

In the event of over-subscription, the allotment of Shares under the Share Issue will be based according to the following allocation criteria and priority:

- First, Shares will be allocated to the Underwriting Syndicate according to each of the underwriter's right to the allotment of Shares as described in section 2.3 (up to 50% of the Underwritten Amount).
- Second, Shares will be allocated to DynaPel shareholders of record in the Company's VPS-register as of 12 January 2005 and resident in Norway on a pro-rata basis in accordance with the subscribed amount. If deemed to be made in accordance with applicable law, subscriptions from foreign shareholders will be accepted accordingly. Underwriters that are also DynaPel shareholders of record in the Company's VPS-register as of 12 January, 2005, will have the right to an allotment of Shares both as underwriter (as described in bullet item 1 above) and as shareholder (as described in this bullet item).
- Shares not subscribed for by the Underwriting Syndicate or shareholders of DynaPel as described in this section will be allocated to new investors, (including subscriptions for shares from underwriters not allotted for under bullet items 1 and 2 above) resident in Norway on a pro rata basis based on the subscribed amount. If deemed to be made in accordance with applicable law, subscriptions from foreign investors will be accepted accordingly.

The allotment of Shares will take place after the expiry of the Subscription Period on or about 19 January, 2005. Notices of allotment will be distributed to all applicants on or about 19 January, 2005.

2.9 Payment for shares allotted

Subscribers for Shares in the Share Issue will grant, as part of the subscription, a one-time authority to the Manager to debit the cost of the Shares allotted from a specified Norwegian bank account as specified in the subscription form. Notices of allotment will be sent out on or about 19 January, 2005. Payment will be deducted from the designated bank account on or about 21 January, 2005. Please note that the amount for the subscribed Shares should be made available on the specified Norwegian bank account by 20 January, 2005, as it usually takes at least one day to transfer money from one bank account to another. Shares allotted will be, subject to the conditions under the Share Issue as described in section 2.2, transferred to the subscriber's individual VPS account as soon as practically possible following the deduction of payment from the subscriber's bank account.

Subscribers that do not have a Norwegian bank account, must transfer the NOK amount needed to pay for the allotted Shares to the following bank account number **7001.95.52363** in DnB NOR Bank ASA, SWIFT-code: DNBANOKK. The payment for the allotted Shares must be received by the Manager by 21 January, 2005.

If there are not sufficient funds on the specified Norwegian bank account to pay for the allotted Shares, or for any reason it is impossible to debit the given bank account, or the payment from subscribers not owning a Norwegian bank account is not received at the due date, the Board of Directors of DynaPel reserves the right to cancel or reduce the subscription or sell all or part of the subscribed and allotted Shares for the account and risk of the subscriber. Interest of 8.75% per annum will accrue on late payments. The subscribers will not be charged with any costs by DynaPel with respect to the subscription.

Shares allotted in the Share Issue may only be traded from and including the first day of trading on the Oslo Børs. Shares allotted may under no circumstances be traded before settlement of the Shares has been received and the Shares have been transferred to the respective subscriber's VPS account. Delivery of the Shares is conditioned on settlement being received in accordance with the payment terms set out above and that the DynaPel Shares are listed on the SMB List on the Oslo Børs as described in section 2.12 and 10.3. It is expected that it will be possible to trade the Shares allotted through the Oslo Børs at the latest 27 January, 2005.

2.10 Transfer restrictions

Each purchaser of Shares must comply with all applicable laws and regulations in force in any jurisdiction in which it purchases, offers or sells such securities or possesses or distributes this Prospectus or any part of it and must obtain any consent, approval or permission required by it for the purchase, offer or sale by it of Shares under the laws and regulations in force in any jurisdictions to which it is subject or in which it makes such purchase, offers or sales and neither DynaPel nor the Manager shall have any responsibility therefore.

United States
The Share Issue is being offered outside the United States, in offshore transactions in reliance on Regulation S ("Regulation S") under the United States Securities Act of 1933, as amended (the "Securities Act"). The Share Issue has not been and will not be registered under the Securities Act, has not been approved or disapproved by the United States Securities Exchange Commission, any state securities commission of the United States or any other regulatory authority thereunder, and none of the foregoing authorities have passed upon or endorsed the merits of the Share Issue or the accuracy or adequacy of this Prospectus. As a result, the Shares may not be offered or sold within the United States except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state securities laws.

Regulation S
Each purchaser of the Shares outside the United States pursuant to Regulation S will be deemed to have represented and agreed as follows:

(1) Such purchaser understands that the Share Issue has not been and will not be registered under the Securities Act.
(2) Such purchaser is aware that the sale of such Shares to it is being made pursuant to and in accordance with Rule 903 of Regulation S.
(3) Such purchaser certifies that it is not a U.S. person and is not acquiring the Shares for the account or benefit of any U.S. person or is a U.S. person who purchased the Shares in a transaction that did not require registration under the Securities Act.
(4) Such purchaser agrees to resell the Shares only (i) in accordance with the provisions of Regulation S of the Securities Act, (ii) pursuant to registration under the Securities Act, or (iii) pursuant to an available exemption from registration thereunder. The purchaser also agrees not to engage in hedging transactions with regard to the Shares unless in compliance with the Securities Act.
(5) The Shares, if at anytime certificated, shall contain a legend to the effect that any transfer of the Shares is prohibited except (i) in accordance with the provisions of Regulation S of the Securities Act, (ii) pursuant to registration under the Securities Act, or (iii) pursuant to an available exemption from registration thereunder. Such legend shall also state that hedging transactions involving the Shares may not be conducted unless in compliance with the Securities Act.
(6) DynaPel shall refuse to register any transfer of the shares not made (i) in accordance with the provisions of Regulation S of the Securities Act, (ii) pursuant to registration under the Securities Act, or (iii) pursuant to an available exemption from registration thereunder

Any person accepting any interest in the Shares shall be deemed to agree to and shall become bound by such restrictions.

2.11 Publication of technical information in respect of the Share Issue

DynaPel has been permitted to use the Oslo Børs company information system to publish technical information prior to the actual listing. This applies to information on the allotment percentages, etc.

2.12 Condition for stock exchange listing of DynaPel's Shares

DynaPel submitted an application to the Oslo Børs on 24 November, 2004 for listing on the SMB List. The board of directors of the Oslo Børs accepted the application during its meeting held on 22 December 2004. The acceptance of the stock exchange listing is conditioned on the following: 1) the completion of a Share Issue in a minimum amount of NOK 20 million, 2) the issuance of an IPO prospectus approved by Oslo Børs and 3) the strengthening of DynaPel's financial reporting capacity within the first quarter of 2005 by employing one or more employees for such purpose. The Company has started the recruitment process and are currently interviewing potential candidates in Fort Myers, Florida. The Company believes that the position will be filled before the end of February 2005. Subject to the completion of the Share Issue, the first quotation and trading day of DynaPel's Shares is expected to be at the latest 27 January 2005, unless otherwise decided by Oslo Børs. DynaPel's ticker code will be "DYNA".

If the conditions under the Share Issue described in section 2.2 above are *not* fulfilled, the Share Issue will be cancelled and the Shares subscribed for under the Share Issue will not be registered in the Company Registry. Amounts received from subscribers pursuant to section 2.9 above, will, in such case, be transferred back to each subscriber's bank account from which payment of the respective amounts has been made.

2.13 VPS registration

DynaPel's Shares are registered with the VPS. The share registrar is maintained by DnB NOR Bank ASA, Securities Service Department. DynaPel's securities registration number is ISIN US-4593781051.

2.14 Rights conferred by the shares offered

The Shares offered for sale through the Share Issue will confer the right to any dividend approved for a record date after the Shares are issued, if such dividend is declared by the Company. In all other respects, the Shares confer shareholder rights from such time as the Shares are issued by DynaPel.

2.15 Costs

Transaction costs related to the Share Issue and the listing of DynaPel on the SMB List of the Oslo Børs, together with all other costs directly attributable to the Share Issue, will be for the account of DynaPel and paid in cash. Share premium, less a deduction for transaction costs, will be credited to DynaPel's share premium reserve. The following table provides a breakdown of these costs.

Name	Location	Nature of work involved	Amount (NOK m)
DnB NOR Markets	Oslo	Manager	2.2
Guarantee consortium		Underwriting	1.0
Procon AS*	Oslo	Financial advisor	0.3
Payment guarantor		Payment guarantee	0.1
Advokatfirmaet Selmer DA	Oslo	Legal advisor	0.9
Jones Day	Munich	Legal due diligence	0.6
Satterlee Stephens	New York	Legal due diligence	0.1
Kjelstrup & Wiggen	Oslo	Financial due diligence	0.1
AMEX	New York	Financial due diligence	0.1
Total			**5.4**

** See section 8.8 for details on Procon AS.*

The fees charged by the Manager are calculated on the basis of a pre-agreed contract, while other costs are based on estimated time consumed. The Manager shall receive a 5% subscription fee and NOK 1.2 million as a fixed fee. Subject to the Share Issue taking place, the Underwriters will receive an underwriting commission of 5% of the Underwritten Amount.

The figures do not include any value added tax which may be payable by DynaPel. In addition to the costs detailed above, DynaPel will also be responsible for other costs incurred, including the costs of printing and distributing the Prospectus and of marketing the transaction.

2.16 Payment guarantee

The Company has entered into a payment guarantee with one existing shareholder, Lars S. Gran Andersen owning 248,349 shares, for an amount of up to NOK 5 mill. The payment guarantee shall secure an effective registration of the new shares resulting from the Share Issue. A compensation of NOK 100,000 will be paid to the guarantor. The payment guarantee will be effective until the full amount in the Share Issue is paid, or the Share Issue is cancelled.

2.17 Manager

DnB NOR Markets is Manager for the Share Issue. The Manager's address is:

DnB NOR Bank ASA
DnB NOR Markets
Stranden 21
N-0021 Oslo

Tel: +47 2294 8880
Fax: +47 2283 2000

3 Purpose of the Share Issue and Use of Proceeds

The purpose of the Share Issue described in this Prospectus is to secure sufficient funding for the continued operation of the company. As described in section 1.4 and chapter 9 in this Prospectus, the Company has a difficult liquidity situation and needs to secure financing for its current and planned operations.

The proceeds from the Share Issue of minimum NOK 20 million, before transaction costs, will enable the Company to meet the minimum liquidity requirements set by the Oslo Børs.

The proceeds from the Share Issue will strengthen the liquidity of the Company and enable the Company to maintain business activities according to its present strategic plan. The strengthened capital base will also facilitate a continued strong and dedicated effort on R&D.

3.1 Sales and marketing

DynaPel plans to increase the sales & marketing activities which are important in core markets. This will help positioning the Company as a stronger player in the field of video surveillance. DynaPel will, as part of this plan, both strengthen the channel partner network program and the OEM partner activities.

Together with its 14 US representative partners, DynaPel plans to have an own DynaPel booth at the two leading security shows ISC and ASIS in 2005, and is planning to start local product training and demonstration days with the leading security system integrators, which are active customers for the new representative channel. Based on the current reference installations for car dealers and parking lots, DynaPel will develop and send out special solution brochures combined with an active marketing program to the nationwide (US) car dealers and parking lot owners. Special marketing programs and training for the international distribution partners, including some funding for their participation at their local security shows are part of the marketing roadmap for 2005.

3.2 Research & Development

The Company’s strategy is to strengthen its market position and launch new products through following the existing R&D program (see section 5.7 below for further details). DynaPel is currently working on two major new product developments; (1) A Sony/DynaPel 360° tracking system, and (2) a 19” rack mountable versions of SteadyEye and CloseView. Both products are expected to be ready to ship during the first half of 2005, and is expected to create increased customer demand. New versions of its existing products SteadyEye and CloseView are under development. In these versions, customer requirements and ideas received from active installations have been integrated.

4 The security video surveillance market

4.1 Industry overview

Video surveillance is carried out in almost every possible area, i.e. airports, hospitals, prisons, military buildings and areas, public and corporate buildings, gas stations, parking lots, bridges, tunnels etc., with around 50 million cameras installed worldwide (CCTV Today). The video surveillance market is one of the fastest growing segments in the electronic security industry, and since September 11, 2001 every market research company has predicted a strong increase for investments of video surveillance systems (i.e. Freeman, Forrester).

The market for security industry products and services is one of the industrialized world's big businesses and one of the fastest growing markets in the high-tech industry. For the video surveillance market, millions of analog and digital cameras will be installed in the coming years for commercial, military, public and private video surveillance. The leading security-CCTV manufacturers are Pelco, Bosch, GE-Interlogix, Sony, Tyco International, Samsung and Panasonic. Leading Digital Signal Processor (DSP) suppliers to these are Equator Technologies, Analog Devices, and Texas Instruments. Forrester Research estimates that the video surveillance market for products and services is a USD 10 billion global market. Due to heightened worldwide concerns about terrorism, asset protection and crime prevention, analysts believe the market will grow at 20%+ per year over the next 10 years (source: Freeman). The 100 largest US security system integrators increased their revenues by approximately 20% to around USD 4 billion in 2003 (SDM Magazine, TOP 100 List).

A typical security installation includes various products from different suppliers, put together by a system integrator. DynaPel's products are normally a small part of an installation, which typically includes cameras, monitors, cables, installation, storage devices as well as working stations for security video guards. Of the around 50 million video surveillance cameras already installed, DynaPel estimates that between 5-10% should be applicable for using DynaPel products. In addition, new installations will increase the marked potential.

4.2 Current and future market trends within video surveillance

The video surveillance industry is in the process of switching from hardware, only focus on end-to-end software and hardware solutions including a switch from analog to digital networked based video solutions, with demand for digital compression (MPEG-4) and automation capabilities based on intelligent software algorithms. It will be crucial for the success to lower the personal costs for video monitoring and for the video surveillance to install intelligent, automatic video analysis tools, such as motion tracking (where the camera follows a "suspect"), face and license plate recognition, vision-based doorway access control and people counter.

The video surveillance market can be viewed as having two segments:

The Analog Video Surveillance Segment:
Before the advent of digital end-to-end system technology, the market was 100% driven by companies supplying systems using analog-based componentry. This is a mature market fed by system augmentation and maintenance purchases as well as plug-in compatible system enhancement products, like those offered by DynaPel.

The Digital IP-Network Based CCTV System Segment:
Commencing approximately in 1996 with the first IP-network security camera from Axis Communications (Sweden) and with the advent of reliable, commercial scale Digital Video Recorders (DVR) and video servers, manufacturers of IP-networked based cameras began introducing complete end-to-end digital CCTV systems. This segment of the market is the fastest growing and will soon dominate the market for new systems installed and systems ordered to replace existing analog CCTV systems. DynaPel's software solutions can either be incorporated as application modules into OEM (Original Equipment Manufacturer) based DVR's or integrated by system integrators into installations to add video stabilization, video compression and motion based intelligent object tracking functionality.

The market for networked video surveillance (IP surveillance) is currently experiencing a substantial growth. IMS Research predicts factory revenues for network cameras and servers will grow at around 30% (CAGR) over the next five years.

4.3 Market Outlook

Today's video surveillance is a remote operation where the input from several cameras are controlled, viewed and supervised, mainly manually by operators viewing several security monitors simultaneously to detect any irregularity. A security guard makes a decision if a certain situation requires further attention, based on his experience. Watching several security monitors simultaneously is very tiring and error prone as well as labour intensive and very expensive.

Future security systems will not replace an experienced security guard, because it is impossible to model his entire experience. Like with many other technological improvements, future Security CCTV systems will therefore try to make the job for security guards easier and more efficient. Although a human is very efficient in processing video, the huge amount of data is just overwhelming. The key to improving existing Security CCTV systems lies therefore in efficient video (pre-) processing. Video pre-processing, such that a security guard needs to watch only those security monitors that might indicate situations that require further attention. By implementing video pre-processing products the machine will do what it can do best – number crunching – and pre-process data before presenting it to a human. In addition, the technology can automatically detect irregularities and warn the human.

In Security-CCTV this translates into less dependency and risk of errors from the human factor as well as better efficiency and lower cost through higher human-machine interaction (increasing guard efficiency). In addition, digital video implies better compression, cheaper storage and easier video data retrieval – resulting in increased usability of security video for the operators.

The following summarize key factors and trends that DynaPel believes weigh heavily in the design and configuration of a next generation video surveillance system:

Base system cost: The basic cost of a system is composed of the upfront cost of the cameras, monitors etc., archive cost of preserving the 24/7 video data streams and labour costs associated with monitoring and operating the system on a daily basis, including searching stored video material and unnecessary responses to false alarms.

System functionality: Whether in respect of upgrading the functional capabilities of already installed analog systems or as an OEM component or plug-and-play integration into new analog or IP-network based digital video surveillance systems, the fastest growing subcomponent of the market is associated with the introduction of product functionality features designed to:

- improve the quality of the video generated by the system (by using SteadyEye to remove shaky or unstable video);
- reduce the workload for the security guard sitting in front of the surveillance video control station (by implementing functionality like CloseView which automatically detect incidents); and/or
- reduce the incidence of false alarms associated with daily operation of the system and the storing and archiving of the video streams generated by the system.

It is in this area that companies like DynaPel operate by selling either OEM software to camera and DVR manufacturers or plug-in devices that operate compatibly and in real time with basic analog or digital systems already installed or to be installed.

Additional growth will arise from the analog to digital switch and from IP network based systems as digital transition brings ability for digital processing such as stabilization, motion and object tracking.

4.4 Market Shares

The total market for security and surveillance installations is large and experiencing a growth. The intelligent, software based part of this market is a small fraction of the total market, but is expecting to increase as this enables enhanced features and cost reduction. To DynaPel's knowledge, there exists no specific market analysis or figures for this part of the security market.

At present, it is not meaningful to discuss market shares as the DynaPel products represent new developments just about to enter the market.

5 Presentation of DynaPel

5.1 History in brief

In 1988, two Norwegian research scientists, Dr. Gudesen and Dr. Martens, began an R&D initiative that led to several technology companies, one of which is DynaPel. Based in Norway, their mission was to apply proprietary digital data analysis algorithms to video data to enable innovative multimedia applications in digital compression and enhanced, video-based interactive services.

In 1992, the Company was incorporated in the US operating as "International Digital Technologies Inc." (IDT). Continued independent R&D work in Norway produced an advanced and unique form of digital compression technology.

With major funding, new management and Board controlled by the Kirch Group of Germany, the company in 1995 moved to a new lab near Munich, Germany and built up a strong technical capability and perfected the algorithms underlying the company's core technology. The established company concluded the technology development phase and was tasked to begin the development of commercial products. In 1999, Kirsch suspended its support of the Company.

Replacing the former company name "International Digital Technologies" with "DynaPel Systems, Inc" in 2000, the Company continued developing commercial products by licensing OEM software products for video editing to market leaders in the highly competitive consumer electronics sector.

In 2002, Dieter Kondek was appointed CEO and Chairman of the Board, and DynaPel turned its focus towards development and marketing of commercial products in the video surveillance markets. The first products for this segment were launched in Q2 2003, and through 2003 DynaPel marketed its products, primarily in the US.

By the end of 2003 DynaPel started a financial restructuring to secure new capital to fund its future commercial development and to terminate various financial and commercial agreements not reflecting its current business (for more info see chapter 8.5).

In 2004, DynaPel has started to receive orders from its OEM and integrator sales channels for end user installation, and has moved offices to Fort Myers, Florida, for further expansion in the US security market.

5.2 Vision and Goals

VISION

DynaPel will seek to become one of the leading companies for automated intelligent video surveillance and analysis of analog and digital video.

GOALS

DynaPel is aiming for technology leadership for intelligent video analysis and solutions in the video surveillance industry. This will be achieved through a close co-operation with a worldwide network of security integrators and OEM-partners.

5.3 Business high-lights in 2004

The following lists significant product and marketing accomplishments over the past 12 months:

- Kramer Electronics has purchased 100 SteadyEye units for the Broadcast Video Market.
- ISAP Inc. signed an OEM agreement with an initial order of 50 “ISAP SteadyEye” units.
- Important new customers have purchased and successfully tested DynaPel's products in 2004; Dow Chemical, Anheuser-Busch, NATO, US-Army, US Airforce, US Navy, Honda and RWE.
- Honeywell Technology Solutions successfully installed SteadyEye at the NASA.
- Western Video installed more than 15 SteadyEye units at the US-Army.
- After 6 months testing and review of all products, TITAN Group, a leading military security systems integrator, will integrate DynaPel products into future projects.
- Quickset, a leading supplier of support systems for precision instrumentation, has signed an OEM agreement including an initial purchase order.

- 14 Pelco sales representatives has signed as DynaPel representatives for the US market with more than 100 sales people and a customer base of 10,000 integrators.
- ISAP has ordered the next 55 SteadyEye units for a large US military project.
- BAE Systems has ordered the first SteadyEye units for a US military project.
- STS International, a large security system integrator has ordered 24 SteadyEye units for a large US military project.
- Dow Chemical Company is ordering SteadyEye units every month as the standard product for the video security systems at their manufacturing facilities.
- DynaPel has signed an agreement with PSA Security Network and with A.L.A.S. Security Network.
- DynaPel's products are offered through the GSA Advantage internet sales system.
- Pieper GmbH from Germany ordered the first 50 Pieper OEM SteadyEye units.
- New distributors have signed contracts for South Africa, Israel, Australia and New Zealand.

5.4 Technology

Motion is the key information in video – motion separates video from photography.

Video is composed of still frames capturing snap shots of an otherwise smooth and continuous world. Playing them back at a high frame rate gives the impression of real motion. The minimal frame rate at which individual frames dissolve into a fluent motion for a human observer is about 24 frames per second (fps). That is why movies for example are played back at 24 frames per second, and the TV frame refresh rate in Europe is 25 frames per second (PAL) and 29.97 frames per second (NTSC) in the US. The time between one frame and the next could be considered as a gap in the video.

Decreasing the frame rate to 15, 10 or even 5 frames per second increases the size of the gaps and makes you see annoying, undesirable jerkiness. The reason for decreasing the frame rate may be bandwidth limitations for Internet transmissions or cameras which in some cases do not perform well enough to capture full 30 fps video (especially web cameras). Further examples are time disparate data or time sequence photography such as weather satellite imagery, or differing frame rates in various standards may create gaps when converted to one format.

DynaPel has developed particular expertise in analysis and manipulation of this key; “motion-in-video”. DynaPel’s “PelKinetics” engine extracts motion information, and then its “Iso-cam” separates object and camera motion. Together with DynaTrack, a combination of motion estimation and moving object detection, a range of operations become possible which can smooth playback, create slow-motion effects, fill in missing frames, enhance picture quality, find and track objects, identify and index scenes and improve efficiency of compression.

DynaPel has built a platform of innovative products, partly based on patented, software-based technologies. Several of these are already included in DynaPel’s video editing products, and they are the key to the Company’s products for the security market. The basic technology however, can be applied to various other functionalities where video is used.

5.4.1 Motion Estimation

DynaPel's motion estimation software is a key component for most of DynaPel’s products. It is, for instance, used to "mend" the gaps and to smooth the playback of digital video. The improvement is realized by inserting synthesized frames by using the PelKinetic technology. The frame rate increases and makes the video appear continuous and smooth. It can also be used to fill in missing frames of an incomplete captured video.

PelKinetic is based on the physics of motion and the calculation of the dynamics of objects. It is able to describe motion within video and to calculate a new frame(s) between two existing ones. If something moves between the two frames, PelKinetics determines the motion on a pixel-by-pixel basis generating a mathematical motion model called "Dense Motion Field Components". Using motion estimation algorithms called "Optic Flow" the PelKinetics engine calculates the perfect location to place the moving object and synthesizes the new frame. When played back the PelKinetic synthesized video is smooth and sharp. Compared to the jerky original video the viewer get an enhanced visual experience.

5.4.2 Video Stabilization

DynaPel’s image steadying software is designed to remove camera shake from video at various frequencies. Video often show unsteady bouncing due to operator motion as well as camera shake in mounted cameras resulting from a variety of external factors such as wind, airflow from air-conditioning systems or building sway. It can also result from spring bounce in vehicles.

To correct such unsatisfying videos, DynaPel has created a video stabilization technology allowing the user to correct any type of camera actions. Steadying is not limited to vertical and horizontal panning but also includes zooming and rotating. DynaPel's PelKinetics™ technology analyses the motion between the particular frames. Afterwards the IsoCam technology differentiates between object motion and camera motion. According to the preceded analysis, the engine computes an ideal "stabilization" of the camera motion, obtaining a smooth camera motion across a configurable number of sequential frames ("Window"). With each new frame processed, the window is advanced by one frame as well. This allows the video to follow long-term camera movements while eliminating annoying short-term motion. The result is a smooth, steady, professional-looking video.

Further, once camera shake is removed, better video compression or image detection algorithms can be applied. This image steadying function is valuable to nearly all mounted cameras as well as mobile video cameras.

5.4.3 Motion Detection and Tracking

The Iso-Cam technology is a subsequent step to motion estimation by differentiating between object motion and camera motion. This can be used to identify objects moving within the video scene, for example a person walking or a car driving. A bounding box (a coloured frame) or an enclosing contour is included in the video so that an operator can easily follow any object movement in the video.

In connection with the DynaTrack technology it is possible to generate control commands to direct a pan-tilt-zoom (PTZ) camera towards the moving object and track the movement. While this is usually only possible when the reference camera capturing the moving object is close to the PTZ camera, DynaPel has developed a camera calibration process that even allows a significant physical separation of the two cameras. This technology culminates in the CloseViev security-CCTV application, where in combined with a zoom control, the face of a moving person or a licence plate of a moving car can be identified.

A fairly similar technology is used for alarm functions in video surveillance applications, where alarm zones can be defined in the video. Motion detection is then only performed in the defined alarm zones and not outside. This enables the system to be completely insensible to unwanted motion alarms, for instance, due to trees moving in the wind.

5.4.4 Scene Cut Detection

One important part of getting information about the content of a video, is to know which different scenes the video contain. When cutting a video it is often difficult to detect the exact beginning and end of sequences, especially if there are soft transitions. The DynaPel technology eliminates this problem by analyzing the video and marking the beginning and end of each sequence.

Technically, a scene consists of per-scene information including the starting and ending reference time (within a video stream), a scene number, and optionally a scene type and a comment describing the depicted content of the scene.

5.4.5 Image Restoration

Recording an image, while either the camera or the object of interest moves fast, leads to a special kind of blurring, so-called motion blur, which results from the spreading of object information. In extreme examples nothing at all can be recognized in the image. DynaPel has the know-how to eliminate this blurring effect by creating a corresponding image, where the undesired motion is taken out.

To reconstruct such an image DynaPel applies a motion dependent transformation, which quasi "collects" the spread object information. If the motion, which has to be eliminated, is unknown, it is estimated by the methods of the motion estimation, provided that the image is taken from a sequence of images. Otherwise the motion is determined by successive guesses in a variation procedure. Additionally the images have to be filtered before and after the transformation in order to manage the significant influence of noise. Noise is a coincidental, undesired signal fluctuation, which leads to defective bits distorting the signal (e.g. image).

Image Restoration is especially suited for the security market and the video surveillance industry.

5.5 Product portfolio

DynaPel has developed products and applications that rely on it's own patents and know-how in the specific areas of video algorithm, digital video motion analysis, video compression and control. DynaPel has built a platform of innovative, partly patented, software-based technologies, of which several are the key to the products for the security market. The basic technology however, can be applied to various other functionalities where video is used.

5.5.1 Video Security and Surveillance Products

DynaPel's core business is within the video surveillance market, where DynaPel has a suite of products for both analog-based video surveillance systems and IP-network based digital video surveillance systems.

DynaPel's initial products in this field were launched in the market in Q2 2003. To date, the products have achieved a positive response from commercial as well as military and government customers that have the need for intelligent video surveillance capabilities to protect their critical infrastructure.

The following summarizes DynaPel's initial products within this market segment:

> ***SteadyEye*** removes shake, jitter and rotational movement from security video and has unique applicability in a broad range of applications, including military (e.g. drone aircraft), police and border surveillance as well as commercial facility installations. Especially suitable for any mobile object such as buses, trains, cars, airplanes, ships as well as in locations which are exposed to vibrations (factories, tall buildings, traffic lights and windy places). The SteadyEye-SE (Special Edition) includes, among other features, the possibility to upgrade the system in the field remotely with new software versions.
>
> ***CloseView*** is an intelligent real-time video analysis and detection system which allows PTZ cameras to be automatically activated on the occurrence of motion in the camera's viewing radius, zoom in on the intruder that is moving (e.g. a person or car) and record a close-up still image of the moving subject, thereby automating the surveillance system so that this functionality does not need to be manually performed by a security guard using a "joy-stick", which is the current state of the art. This product delivers a cost/benefit for both military and high-end security commercial systems, including the reduction of false alarm rates to a low level.
>
> ***NightView*** allows a basic daylight-only camera to be upgraded to produce usable real-time surveillance video in under-lighted situations. With the new NightView appliance, virtually every camera can generate clean and crisp video from noisy, overexposed, or underexposed input video.

All DynaPel's products are available as plug-in compatible functional upgrades to the significant base of already installed analog-based video surveillance systems or OEM components to new analog-based and IP-network based video surveillance systems.

DynaPel's plug-and-play security appliances and the new 19" rack mountable units are manufactured in Germany by subcontractors. The appliances are simple to install and are working with the leading analog CCTV cameras. It plugs in between any standard camera and down-stream devices such as recorders, multiplexer or transmission systems.

DynaPel's products are currently operational for analog-based video surveillance systems, which comprise around 95% of the video cameras already installed around the world. To satisfy the emerging trend to end-to-end digital surveillance systems, DynaPel plans to introduce IP-network compatibility in 2005.

5.5.2 Future security products

The focus area of future product development of DynaPel is in the security surveillance space. All future products will be driven by the observation that current systems require a substantial amount of manual operation and human attention and DynaPel will reduce operating costs and possible human failure by introducing new products meeting these issues.

IP-network based digital surveillance systems are beginning to replace analog systems, and DynaPel plans to introduce an Intel/Windows/Linux server-based system called *Dynamic Video* which will integrate all its existing video surveillance products into one server platform, with standard equipment for video and storage. Digital camera systems make the installation process simpler, and digital video is much simpler to store and process. Making more use of digital video content is much more than just video storage: it is efficient search and retrieval, more complex analysis and recognition of objects and motion behaviour, or recognising entire events.

DynaPel's current development initiatives can be summarised as follows:

Relative to existing installed base:

- Multi channel 19" rack mountable security units
- 360° Camera Tracker in partnership with Sony and QuickSet
- Add additional functionality to current products (e.g., store alarm video or images)

Relative to next generation emerging market for digital IP-network systems:

- Tracking across several cameras – handover tracks
- Classify "relevant" moving objects (e.g. person vs. car)
- Integrate CloseView and tracking with face and car license plate recognition software
- Integrate MPEG-4 in SteadyEye and CloseView

5.5.3 Broadcast Video Products

SteadyEye is also available to the broadcast video market to improve the quality of live-feed broadcast video from cameras shooting on-location. This could be a large market for the future, and it is significant that DynaPel's first OEM partner, Kramer Electronics (Israel), is marketing the Kramer broadcast solution to their currently more than 1,000 broadcast industry customers and will integrate SteadyEye into a 19" rack.

5.5.4 MPEG-4

DynaPel has been actively involved in the international standardization activities that led to the release of the MPEG-4 video compression specification. Based on this knowledge and experience in motion estimation, DynaPel has developed MPEG-4 compliant video coding products that are currently available to customers:

- The MPEG-4 Video Encoder and Decoder (codec) SDK (Software Development Kit) complies with the new, open MPEG-4 standard. This *MPEG-4 SDK* is an MPEG-4 codec software developer kit that allows customers to develop products and applications using the MPEG-4 video compression technology, which is the open standard for IP-network based applications. Companies like Pulse Entertainment Inc. have adopted this SDK into their software solutions for the video consumer market.
- The *MPEG 2/4 Transcoder* allows efficient conversion of an MPEG-2 video stream into an MPEG-4 video stream, which is the industry protocol for receiving and decoding digital data streams. This software product is suitable for the rapidly emerging arena of capturing enhanced Internet services on computer and various handheld wireless devices, and is currently being pilot-tested by Austria Telecom.

DynaPel offers real time, compliant MPEG-4 with the flexibility to add valuable security MPEG-extensions. By using MPEG-4 within the digital security CCTV, distribution of high quality video through DSL/IP-network allows surveillance systems on existing infrastructure. These implementations are especially designed to accommodate effects such as camera movement, and streaming IP applications.

5.5.5 Video editing software

Prior to breaking into the video surveillance market, DynaPel first used its technology to create video editing products based on the Windows platform for post-production video editing. Today, these products are primarily purchased online over the web in down-loadable software form:

- ***MotionPerfect*** analyze the video for dropped or duplicate frames and synthesize new frames to replace them. Either action will smooth out a jerky video and the result is fluent and smooth motion. It can convert from any frame rate to any other frame rate or from one compression scheme to another, or to create slow motion effects.
- ***SteadyHand*** corrects unsteady camera motion in the video, enabling the user to correct difficult camera actions such as zooming, rotating and panning. A SteadyHand Plug-in for Adobe Premier is also available.
- ***SlowMotion*** allows the user to generate high quality slow motion video. Gaps are filled-in by insertion of new interpolated frames.

In addition, DynaPel has ported its consumer PC video-editing software onto the Casablanca platform from MacroSystem AG, receiving royalty under a licensing agreement.

5.6 Patents / Intellectual Property Rights

Over the years, DynaPel has received 5 patents and filed 4 additional patent applications. They cover the fields of video compression, video-encoding and -decoding, motion estimation and –compensation, image enhancement as well as video surveillance. As the business direction of the Company has evolved, DynaPel has abandoned those patents not central to its core business and is maintaining 3 patents and 4 patent applications to protect its present and planned products.

DynaPel patents

	Description	Filing date	Issue Date	Patent Number	Inventors	*Assignee*
1	Method and Apparatus for Multi-Resolution Object Oriented Motion Estimation	1997-07-28	2002-04-09 (US) 2002-12-04 (EU) 2003-10-09 (D)	6,370,196 (US) EP 0998825 B1 (EU) DE 69809920 T2 (D)	Griessl, Martens, Reberg, Roettgermann, Wittkop, Wonneberger	DynaPel Systems Inc
2	Motion Picture Enhancing System	1999-12-14	2002-02-26 (US)	6,351,545 (US)	Diepold, Edelson	DynaPel Systems Inc
3	Medical Image Display System	2001-05-31	2004-02-10 (US)	6,690,386 (US)	Diepold, Edelson	DynaPel Systems Inc

DynaPel pending patent applications

	Description	Filing date	Appl. Number	Inventors	Assignee
1	Surveillance Video Camera Enhancement System	2001-11-05	20020054211 (US)	Diepold, Edelson	DynaPel Systems Inc
2	Method and System for the Estimation and Compensation of Brightness Changes for Optical Flow Calculations	2001-03-26	20020163596 (US)	Griessl, Wittkop, Wonneberger	DynaPel Systems Inc
3	Video Super-Frame Display System	2001-12-26	20020094026 (US)	Edelson	DynaPel Systems Inc
4	System and Method for Stabilized Single Moving Camera Object Tracking	2004-10-08	Provisional application	Wonneberger	DynaPel Systems Inc

DynaPel’s current technology and products are only to a limited degree covered by the registered patents and patent applications described in this section 5.6, both concerning the Company’s products, the Company’s technology and the territorial protection of the patents. The Company and Holon Technology GmbH pursue a policy to protect their technology and products through trade secrets and know-how. The trade secrets and know-how are held by Holon Technology GmbH, and are neither documented nor verified, to the extent that provide exclusivity rights vis-à-vis third parties.

DynaPel’s patent work is handled by the law firm Venable, Baetjer, Howard & Civiletti, LLP, 1201 New York Avenue, N.W., Suite1000, Washington, D.C., 20005, USA.

All of DynaPel's technology has been developed in Germany, by employees or consultants of the bankrupt former subsidiary DynaPel Laboratories GmbH, and the newly established subsidiary Holon Technology GmbH that continues the R&D-operations of DynaPel. Under German mandatory law, the employee is the rightful owner of technology developed within a company by the employee (“inventor”). The inventor can waive its rights, and transfer their ownership to the employer through an Acknowledgment form. With the exception of two, all former and current employees and inventors of DynaPel have signed the Acknowledgement and Waiver form. The two employees refusing to sign the waiver, are co-inventors of patent 1 above, with filing date 1997-07-28. The technology of this patent is not in use in DynaPel’s current products.

Mr. Steve Edelson has only signed an abbreviated English version of the Acknowledgement and Waiver form, not in formal compliance with provisions of the German Employee Invention Act. However, Mr. Edelson, an American consultant, may not be subject to the provisions described above.

DynaPel currently holds no trademarks or copyrights.

5.7 Research and Development

The focus area for the foreseeable future product development of DynaPel is in the security surveillance space. All future products will be driven by the observation that current security surveillance systems require a substantial amount of manual operation and human attention.

Further, analysis of the current security system situation indicates not only a lack of efficient use of security guards (that makes the entire process expensive), but also a lack of usability of video content. The latter deficiency can be tackled by the introduction of digital video. Introducing digital (IP-based or network) camera systems also make the installation process simpler. But most important, digital video is much simpler to store and process. Digital video also requires efficient compression, for which MPEG-4 is an ideal candidate. Making more use of digital video content is much more than just video storage: it is efficient search and retrieval, more complex analysis and recognition of objects and motion behaviour, or recognising entire events. Detecting events captured on video, that a trained security guard would usually consider a situation that requires further attention, will be the primary long term goal. The Company's analysis shows that this direction would eventually lead to a – at least partial – replacement of a security guard. To develop this technology will take some time.

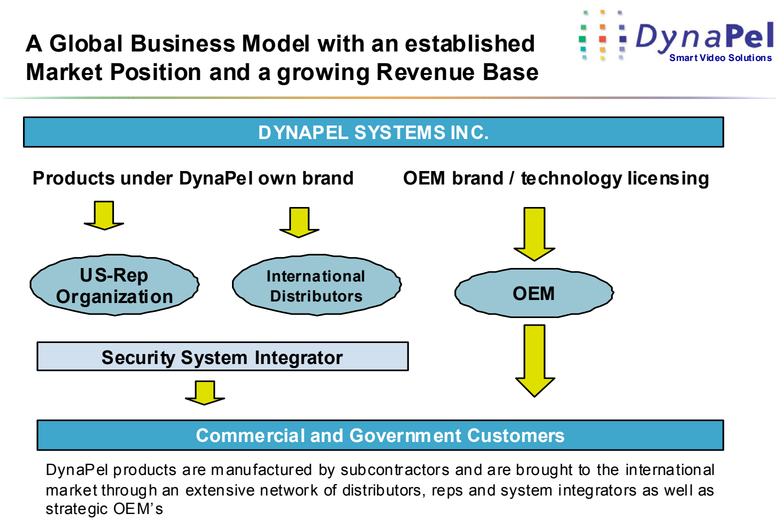
DynaPel's current product pipeline matches this observation and analysis. Built into DynaPel's business model is the benefit of getting immediate revenues by introducing products that operate – for now – on analogue video. As mentioned above, the security industry is fairly traditional and conservative, but new technologies like networked digital video and intelligent video analysis software will be growing very fast into this segment. Upgrading existing system from analogue to end–to-end digital video requires a complete new installation. DynaPel's products can be used immediately to add intelligence without changing the installed infrastructure and could also be upgraded and integrated into future new system installations.

The basis for most of current and future products is motion estimation and video stabilization. Steady is key to a more efficient video encoding and better storage efficiency. Motion estimation is key to moving object detection and tracking. Future products may include:

- Object classification (Is it a person or a car?)
- Object recognition (Who is that person? Whose car is this? What is the car license plate number?)
- Event detection (What is this person doing? Does it match a regular behaviour?)
- Matching events (Looks like that person is stealing something)
- Doorway access control (Make sure only the identified person enters the building)
- Tamper-proof MPEG-4 video coding (only genuine, un-tampered video can be used in court)

Although DynaPel has a strong focus on the security surveillance markets and to some extent on the broadcast market through its partner Kramer Electronics, its core technology can be developed into other markets where video or moving pictures are used.

5.8 Sales and distribution strategy



In the US market, the large number of product suppliers that provide the components used in video surveillance systems reach their end user customer through well-established distributors and manufacturer's representative networks, which, in turn, market either to end customer users or to a highly localized network of "system integrators".

System integrators interface directly with end user customers. There are more than 10,000 system integrators in the US, whose business is to design and install custom tailored end-to-end video surveillance systems to meet their customers functional and budget needs. In each case, they select from the wide range of OEM component choices they believe will best satisfy each customers' needs.

In Europe, the manufacturer's representative concept is not as prevalent and providers of video surveillance componentry reach their end user customer primarily through distributor and system integrator networks that operate in each European country.

DynaPel is organizing its sales and marketing efforts to operate effectively through both OEM channels and the well-established distributor/manufacturer's representative/system integrator channels. This reduces DynaPel's need to compete in the market with a high cost, end customer sales force, however DynaPel still must recruit and retain a highly qualified sales team able to communicate and market the benefits of its products to these channel outlets.

DynaPel's products were introduced to the market Q2 2003 and have gained acceptance with commercial as well as military and governmental users, like US Army, US Air-Force, US Navy, NASA, Dow Chemical, Anheusser-Busch, Honda, RWE and NATO. The key market for DynaPel is USA, where the Company has already established a significant OEM and system integrator-based group of partners such as Tyco, Siemens, Lockheed, ADT Security, Northrop, Tit an, and L-3 Communication.

North America
For the US and Canadian security market, DynaPel has signed sales agreements with 14 PELCO Representatives to market its products in these markets. PELCO is known as one of the top suppliers of security products worldwide. These Representatives work exclusively in licensed territories throughout the US and Canada with combined sales force of more than 100 people, and are responsible for selling the DynaPel intelligent video security solutions to more than 10,000 security system integrators.

The following Pelco Representatives are now representing products from DynaPel:

- **Crockett Sales** for Texas, Oklahoma, Arkansas, Louisiana, Mississippi, W. Tennessee
- **Intermountain Marketing** for Colorado, Wyoming, Montana, Idaho, Utah, New Mexico
- **Keith Parker & Associates** for Northern Illinois and Eastern Wisconsin
- **T.H.Grogan** for Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island
- **FCM Inc**. for Central and Eastern Tennessee, Florida
- **Charles & Associates** for Ohio, West Virginia, Western Pennsylvania
- **Milsk Company Inc.** for Michigan
- **Langbaum Associates Inc.** for Delaware, New Jersey, New York, Eastern Pennsylvania
- **GP Marketing** for Washington, Oregon, Alaska, West Idaho, and West Montana
- **1Volt Associates** for District of Colombia, Maryland, North and South Carolina, and Virginia
- **Bruce Dawson & Associates** for Indiana and Kentucky
- **R.W. Sales, Inc.** North Dakota, Minnesota, and Western Wisconsin
- **Access Direct Sales** for Canada
- **SpecPoint** for Alabama and Georgia

EMEA (Europe, Middle East, Africa)
In EMEA DynaPel has started to establish relationships with the leading security distributors per country. The Company is currently negotiating contracts for UK, the Netherlands, Germany, Italy, Spain, Scandinavia and France.

Contracts with distributors from Israel and South Africa has been signed:

- **GOLDTEC Technologies Ltd.** for Israel
- **ICS Trading SA Ltd.** for South Africa

Rest of the world
In Asia and South America DynaPel has started to establish relationships with the leading security distributors per country. DynaPel is currently negotiating contracts for 13 countries in South America. Contracts with distributors for Asia, Australia, New Zealand and Pakistan has been signed:

- **Latimer Clarke LTD.** for Australia and New Zealand
- **E2Vision** for Asia

5.9 Manufacturing

The DynaPel security video appliances are currently produced at BMK Electronic GmbH ("BMK") in Augsburg, Germany. BMK was founded in January 1994, as a "spin off" of NCR/ AT&T, one of the world's leading computer manufacturers. Since then it has grown at a considerable speed. The success is due to the positive synergy of a medium-sized company structure with "short ways" and intensive customer contact plus the take-over of a highly developed company production process with qualified personnel from the SMT production. BMK currently employs more than 250 people. DynaPel benefits from the fact that BMK is a medium-sized company with short communications paths, that offers everything within hardware design, PCB layout, production licensing (CE, FCC, UL), prototyping, world wide procurement, board assembly, final assembly, and fulfilment and logistics. BMK ships large orders directly to the customers.

DynaPel does not have a written running supply agreement with BMK, but makes orders on an ad hoc basis.

BMK is doing components procurement, board assembly, and final assembly, basically the entire contract manufacturing for DynaPel. Besides BMK, DynaPel has additional suppliers for housings, power supplies, DSP, and pre-programmed memory chips, with direct contact to Equator, the DSP manufacturer. The housings and keypads are supplied by Bopla (Germany) for SteadyEye, CloseView, and NightView, and Schroff (Germany) for the DP-192X, the 19” rack mountable version. Both Bopla and Schroff are worldwide known, large manufacturers of any kind of housing for electronics components.

5.9.1 Technical Service

The technical service for DynaPel's products will mainly be delivered from the Company's distribution and system integration partners. Upon requests from end customers or DynaPel's partners, enquiries will be handled by the DynaPel support team in Europe and USA and/or the Company's engineering team in Munich, Germany.

6 Competition

DynaPel's video surveillance products have different competitors in different segments and applications. Based on its analysis, DynaPel believes that it is the only company competing in the market with video surveillance products that are based totally on captive technology and intellectual property know-how where:

- The products incorporate the most advanced video algorithms for real-time video stabilization, motion estimation, motion detection, and video compression and are available to the market in multiple formats such as stand-alone, plug-in compatible box devices, in a soon-to-be- released multi-unit 19" rack- mountable device format or in OEM "HOLON board" format.

- The products are built using a programmable system-on-a-Chip (DSP), which enables them to be more easily integrated, installed and upgraded in new or existing video surveillance systems than those competing products which operate on either an ASIC-based or PC server-based platform.

6.1 SteadyEye

DynaPel has knowledge of the following products offered in competition to SteadyEye:

Pyramid Vision Technologies (US) is marketing a product called Arcadia Video Stabilizer, which is a complete solution with their own ASIC chip platform as PCI card for Intel PC's. DynaPel believes that Arcadia is the closest functional competitor to SteadyEye, but Arcadia needs a server to run the application, and the price is higher at approximately USD 10,000 versus approximately USD 3,000 for SteadyEye (end user price).

QinetiQ in UK has a product called Stable Eyes, which is an old Trimedia DSP. This is also a box product, but has no rotation, no OEM board and much lower performance compared to SteadyEye. The price is approximately USD 3,500 versus approximately USD 3,000 for SteadyEye (end user price).

FOR-A in Japan has a product called IVS-300 which is developed for the broadcast video market, competing against the Kramer OEM 19" box. IVS-300 is packaged as a 19" single box with its own ASIC chip and the performance is compatible. The price is higher, at approximately USD 5,000 versus approximately USD 3,000 for the DynaPel/Kramer solution (end user price).

6.2 CloseView

For its CloseView product, DynaPel is aware of the following companies with comparable products:

Object Video in US has a product called VME, which is PC Server based and needs high installation and training costs. It is focusing on larger enterprise installations with a price per camera of approximately USD 5,000 plus an extra PC server to run the software application. Further, the personnel need computer know how to run the system. This compares to an end user price of approximately USD 2,500 for CloseView.

The GuardianWATCH Enterprise from Guardian Solutions (US) is also a PC server based enterprise solution like Object Video's VME. The price is approximately USD 5,000 per camera plus extra PC server, versus approximately USD 2,500 for CloseView (end user price).

Other potential competitors, which have not been researched in detail, are: Bosch, VistaScape, IOImage, SmartCatch, ActiveEye, Pyramid Vision.

6.3 NightView

DynaPel is not aware of any known competitor in this segment. However, the Company's NightView products will compete against high-end day/night cameras which are priced at approximately USD 2,000 against NightView at approximately USD 1,500.

6.4 Competitive edge

Overall, DynaPel believes its intelligent video surveillance products are less costly to purchase and install relative to competing products, provide users with video quality improvements and reduced system operating costs. Furthermore, because these products are made using a programmable DSP chip, as DynaPel introduces new functionality to its software, already installed boxes and OEM HOLON boards can be upgraded versus having to be replaced, as would be the case for ASIC-based products.

7 Company organisation, Board and Management

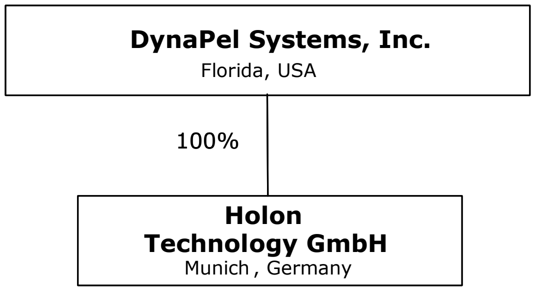
DynaPel Systems Inc is a US public limited company incorporated in the State of Delaware. The Company's organisation number is 2309086, and its principle office is at 2235 First Street, Suite 215 Fort Myers, Florida, USA.

The Company's objective is to develop and market intelligent video software, tools and appliances for the security and broadcast industries based on patents in digital video motion analysis and control.

7.1 Company Organisation

The Company was incorporated in the US in 1992 operating under the company name "International Digital Technologies, Inc." In 2000 the company changed its name to "DynaPel Systems, Inc.

The operating entities in the DynaPel group are shown in the following chart.



DynaPel Systems Inc is a US corporation with its headquarter in Fort Myers, Florida, USA, where the accountant, sales, marketing, technical support and logistic functions are located. DynaPel Systems Inc currently employs six people. All commercial activities are carried out by DynaPel Systems Inc.

DynaPel's research and development activities, including the engineering team, are located in Munich, Germany, through the 100% owned subsidiary Holon Technology GmbH. Holon Technology GmbH was established in January 2004 after DynaPel's former operating company DynaPel Laboratories GmbH (see below), filed for insolvency. The development team, consisting of 10 people, whereof 8 are scientists working in the product research and development function.

One DynaPel Systems Inc employee is located in Oslo as CFO and investor relation's manager. In total, DynaPel currently employs 16 people. The average number of employees for the last years has been 24 (2001), 21 (2002) and 16 (2003).

DynaPel has no commitments towards its employees except normal contracts and option plans.

Up to December 2003, the research and development activities were carried out through the former German subsidiary, DynaPel Laboratories GmbH. In 2003 DynaPel Laboratories GmbH was advised of certain tax issues related to an audit of the now bankrupt German Kirch Group, in which had tight relations to DynaPel Laboratories GmbH. Consequently, the management of the subsidiary declared itself insolvent to protect it from claims of the tax authorities and other creditors. In the opinion of the Board of Directors, the insolvency of the German subsidiary has not materially affected DynaPel and its current financial and marketing efforts. Its engineering team has for the most part continued to work for DynaPel through Holon Technology GmbH. Retaining as many of the engineers as possible has prevented any loss of technological knowledge and assured uninterrupted support of customers and partners. For further description of the insolvency, hereunder description of the settlement agreement with the Insolvency estate, see section 8.7, 8.9 and section 11.4.

7.2 Board of Directors

The following table shows the shares, options and warrants held by the members of the Board of Directors of DynaPel:

Name	Position	Address	Number of Shares	Number of Options	Number of Warrants
Helge Nielsen	Chairman	Bergen, Norway	138,559	0	0
Ralph Carballal	Director	New York, New York, USA	366,010	6,300	0
Ivar Formo*	Director	Oslo, Norway	125,665	2,200	0
Live Haukvik Aker	Director	Tønsberg, Norway	0	0	0

* Ivar Formo's holding of shares includes 72,590 shares in DynaPel owned by the company Ullevål Utvikling AS where Ivar Formo has a controlling 50% ownership.

Helge Nielsen (52), Bergen, Norway
Mr. Nielsen was elected as chairman and new member of the board on the special shareholder meeting held 18 November, 2004. Helge Nielsen is Siviløkonom from Norges Handelshøyskole 1975, with an extensive experience from various top management positions. 11 years of international experience in SCA, a listed Swedish company, where he had the position as President of the Health Care Division. Today he works partially for the Grieg Group in Bergen.

Ralph Carballal (57), Director, New York, USA
Mr. Carballal brings senior Wall Street experience to DynaPel, having spent the last 26 years as an investment banker. He was previously Managing Director of two Wall Street firms: Smith Barney and Prudential Securities. In 1991, Mr. Carballal and two other senior bankers founded the Private Merchant Banking Company, which specialized in M&A and private equity investments in small and mid-cap companies. Mr. Carballal holds an MBA from the Wharton School of the University of Pennsylvania and he is a Director on the Board of Opticom ASA.

Ivar Formo (53), Director, Oslo, Norway
Mr. Formo is an investor and board member of the listed companies Ignis ASA, PSI Group ASA and Cashguard AB. Earlier he served as Chief Executive Officer of Kistefos Venture Capital AS, a venture capital company. Formo holds a postgraduate business administration degree from Norwegian Business Institute and an engineering degree from the Norwegian Technical College.

Live Haukvik Aker, (41), Tønsberg, Norway
Mrs. Aker was elected as new member of the board on a special shareholder meeting held on 18 November, 2004. Mrs Aker has a Master of Management from BI, Oslo and business degree from Fribourg, Switzerland. She is currently CEO of Goodtech ASA, a company listed on Oslo Børs and has extensive experience from Norwegian trade companies and KPMG as auditor. Mrs Aker is currently a board member of Eksportfinans ASA, Borgestad ASA, MiTrans AS and various companies related to Goodtech ASA.

7.2.1 Remuneration of the Board of Directors and CEO

DynaPel has until now not paid its board members any compensation for attending the Board and Board meetings. In February 2003, Ralph Carballal and Ivar Formo each received 13,000 shares as compensation for work related to financial issues. For the 2004 financial restructuring of DynaPel, Ralph Carballal and Ivar Formo have each received compensation in DynaPel shares in the amount of USD 50,000.

Becoming a listed company, DynaPel will compensate its Board members at a normal competitive level, and may also offer stock options.

The CEO Dieter Kondek receives a yearly compensation of USD 216,000 plus health and life insurance. In addition, Mr. Kondek has warrants as described in section 7.3 and section 10.7. Mr. Kondek is entitled to severance payment of 6 months salary if the employment is terminated by DynaPel.

7.2.2 Ownership related to the Board of Directors

In addition to the ownership of the members of the Board of Directors described in section 7.2 above, Ivar Formo is closely related to Ullevål Utvikling AS that holds 72,590 shares in DynaPel.

Ralph Carballal is personal lender as described in section 8.8, to the secured convertible Bridge loan described in section 8.9. If the loan is converted, Ralph Carballal will receive 75,186 additional shares. Family members of the Board members Helge Nielsen and Ivar Formo are participating in the Bridge loan as described in section 8.8.

7.3 Management

The following lists the executive officers in the Company.

Name	Position	Address	Number of Shares	Number of Options	Number of Warrants
Dieter Kondek**	CEO	Fort Myers, Florida, USA	205,026	0	500,000
Dr. Dieter Koller	CTO	Munich, Germany	5,820	9,000	0
Tore Formo*	CFO	Oslo, Norway	94,226	0	0

* Tore Formo's holding of shares includes 93,752 shares in DynaPel owned by the company Ullevål Invest AS where Tore Formo has a controlling 40% ownership.

** See section 10.7 with regards to the most significant conditions of the warrants held by Dieter Kondek.

Dieter Kondek (48), Chief Executive Officer - DynaPel Systems Inc, Fort Myers, Florida, USA
Mr. Kondek was named President & Chief Executive Officer of DynaPel Systems Inc in February 2002. Drawing on more than 27 years of experience in the high tech industry, Kondek joined DynaPel from KBP Consulting, a Business Development organization, which he co-founded in 2000. His career began at IBM Corporation in 1976 where he spent more than 6 years in system engineering and sales. Since then, he served as Managing Director and VP at Computer 2000, Managing Director at Dell Computer, VP EMEA at MetaCreations, Executive VP worldwide sales, marketing and service at Linotype-Hell and Executive VP at Webfair. Mr. Kondek has strong management skills from past experience in larger organisations as well as entrepreneurial skills in growing small start-up companies into successful larger companies.

Dr. Dieter Koller (38), Chief Technology Officer - DynaPel Systems Inc, Munich, Germany
Dr. Dieter Koller joined DynaPel in April 2002 in the capacity of Technical Director, managing the Company's software and hardware engineering department. Dr. Koller brings 15 years of experience in image processing, video analysis and computer graphics into the Company. His former employment as senior researcher and manager includes the European Computer Research Centre (ECRC) in Munich, Germany, and Autodesk, California. Until recently he served as VP of Engineering at Enroute Imaging, Palo Alto, California. Dr. Koller holds a MS in Physics and PhD in Computer Science, both from the University of Karlsruhe, Germany. He has also held post-doctoral research positions at the University of California at Berkeley and the California Institute of Technology in Pasadena, USA. Dr. Koller is author or co-author of more than twenty international research publications.

Tore Formo (40), Chief Financial Officer – DynaPel Systems Inc, Oslo, Norway
Tore Formo has been engaged by DynaPel on a consultancy basis since 2002 and has been employed as CFO and employed by DynaPel from 1 November, 2004. Mr. Formo has 14 years of financial experience, from both the equity and debt markets as well as smaller technology companies in Norway. Mr. Formo has his education from BI, Norway (siviløkonom) and Mannheim, Germany.

7.3.1 Employees

As of the date of this Prospectus, DynaPel had 16 employees.

The table below shows the development per function in the number of employees since 2001.

	2001	2002	2003	Q4 2004
Sales and marketing	4	3	2	3
Research and Development	15	13	10	9
Administration	5	5	4	4
Total	**24**	**21**	**16**	**16**

11 employees are based in Munich, Germany, with one sales person and one office administrator in addition to the 9 engineers. Based in Fort Myers, Florida, are the remaining two sales people and two office and accounting persons. The CFO is based in Oslo for maintaining contact with the Oslo Stock Exchange and the financial markets.

7.3.2 Reporting routines

DynaPel has employed a professional and experienced accounting officer at its head office in Fort Myers, Florida, which is in charge for the daily accounting and preparation of monthly and quarterly financial information. Holon Technologies GmbH has an office manager who is responsible for daily routines and preparing all necessary accounting information for the outside accounting firm Ringel & Hillebrand in Munich, Germany, which is preparing the monthly and quarterly financial statements for consolidation in Fort Myers, Florida.

In addition to internal resources, DynaPel has engaged the accounting firm Schulz & Chaipel CPA in Fort Myers, Florida, which are US-GAAP certified and have experience with international accounting, taxation and consolidation. This is to ensure competent back-up resources available at DynaPel's discretion. In 2004 DynaPel's US auditor has assisted in preparing quarterly consolidated figures, and has also assisted in implementing quality accounting and reporting routines for correct, timely and effective accounting.

DynaPel will strive to obtain and maintain adequate competency with respect to ensuring a correct and timely disclosure of relevant information. The CFO will have daily contact with both the German and US operations, and be DynaPel's primary contact for communication with the Stock Exchange, shareholders and financial markets. The CEO will act as substitute and the Company will have further back up through Norwegian based directors.

8 Financial Information

The following financial data for the years ended December 2001, 2002 and 2003 are based on the audited financial statements for the Company. The financial data for the third quarter 2003 and 2004 is not audited. The financial data are prepared in accordance with US GAAP.

The Annual report for the year ended 31 December 2003, the audited interim report for the first half year 2004 and the unaudited interim report for the third quarter 2004 are included in Appendix 2 and 3.

8.1 Accounting policies

Accounting principles
The preparation of financial statements are prepared in conformity with US Generally Accepted Accounting Principles (US-GAAP). The accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Principle of consolidation
The consolidated financial statements include the financial statements of DynaPel and its wholly owned subsidiary, Holon. All significant intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents
For financial statement purposes, the Company considers all highly liquid debt instruments with a maturity of three months or less when purchased to be cash equivalents. The Company maintains its cash in bank deposit accounts in the United States of America and overseas which, at times, may exceed applicable insurance limits.

Accounts Receivable
Accounts receivable have been adjusted for all known uncollectible accounts and are stated at the amount management expects to collect from outstanding balances. Based on management's evaluation of collectibility, an allowance for doubtful accounts is not required.

Inventory
Inventory is valued at the lower cost (first-in, first-out) or market.

Property and Equipment
Property and equipment are stated at cost, less accumulated depreciation. Depreciation is provided using straight-line and accelerated methods over the estimated useful lives of the assets. The estimated useful lives are as follows:

- Computer equipment and software; 3 years
- Furniture, fixtures and other; 3-5 years

Deferred Revenue (or Royalties)
Deferred revenues consisted primarily of an up-front royalty received 5 November, 1999, upon execution of a license agreement which was effective 1 January, 2000. Under terms of the license agreement, minimum future royalties were to be earned for the six-year period which began on 1 January, 2000 through 31 December, 2005. As a result the Company deferred the up-front royalty and was recognizing the corresponding revenue over the term of the minimum royalties. This agreement was terminated effective April 2004, and the remaining deferred royalties and revenue was recognised as income in Q2 2004.

Cost of Sales
Cost of sales is composed of costs related to the packaging of software and hardware for sale and depreciation of equipment used in production.

Research and Development Expenses and Capitalized Software Development Costs
Software development costs consist principally of compensation and benefits paid to the Company's employees. All software development costs not qualifying for capitalization are expensed as research and development costs when incurred.

The Company's policy is to expense all software development costs prior to establishing technological feasibility. Because the Company's products have reached this state of development almost concurrently with general release, the Company has not capitalized any software development costs.

Income Taxes

The Company accounts for income taxes using the asset and liability method, as prescribed by Statement of Financial Accounting Standards No. 109 "Accounting for Income Taxes". Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Statutory taxes not based on income are included in general and administrative expenses.

For interim periods, income tax expense is provided using the estimated effective income tax rate expected to apply for the entire taxable year.

Translation of Foreign Currencies and Foreign Currency Transactions

Financial statements of the Company's foreign subsidiary are translated into U.S. dollars at current exchange rates, except for costs and expenses, which are translated at average exchange rates during each reporting period. Net exchange gains or losses resulting from the translation of assets and liabilities are accumulated as "accumulated other comprehensive income (loss)" and are reported as a separate component of share-holders' deficit. Transactions in currencies other than the U.S. dollar are recorded in U.S. dollars at exchange rate prevailing at the transaction dates. Exchange gains and losses are included in the Company's results of operations.

Stock Option Plans

The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations, in accounting for its fixed plan stock options issued to employees and directors. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. The Company applies Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, for its stock options to non-employees and non-directors. SFAS No. 123 established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic value-based method of accounting described above for stock options issued to employees and directors, and has adopted the disclosure requirements of SFAS No. 123.

Accounting for the Impairment or Disposal of Long-Lived Assets

The Company follows the provisions of Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. These Statements require that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less cost to sell.

8.2 Consolidated statements of operations and comprehensive loss

Income Statement (figures in USD)

	Q3 2004 (unaudited)	Q3 2003 (unaudited)	2003	2002	2001
Operating income					
Royalties	291,667	875,000	1,166,667	1,166,667	1,166,667
Sales	352,656	329,583	423,369	265,620	257,501
Total royalties and sales	**644,323**	**1,204,583**	**1,590,036**	**1,432,287**	**1,424,168**
Operating expenses					
Cost of sales	156,712	83,397	93,196	49,589	0
Operating expenses	1,842,078	2,411,477	3,494,499	3,219,723	3,161,416
Interest expense	57,472	275,614	398,793	303,497	650,823
Total operating expenses	**2,056,262**	**2,770,488**	**3,986,488**	**3,572,809**	**3,812,239**
Operating result	**(1,411,939)**	**(1,565,905)**	**(2,396,452)**	**(2,140,522)**	**(2,388,071)**
Other income/(expense)					
Foreign currency exchange	-	-	(1,871)	35,126	219,282
Other income and (expenses)	8,352,871	117	4,998	(3,870)	(235,364)
Loss on early extinguishment of debt	-	-	-	(447,581)	-
Total other income/(expense)	**8,352,871**	**117**	**3,127**	**(416,325)**	**(16,082)**
Net result	**6,882,932**	**(1,565,788)**	**(2,393,325)**	**(2,556,847)**	**(2,404,153)**
Other comprehensive income/(expense)					
Foreign currency translation adjustment	**-**	**-**	**(16,141)**	**7,990**	**(13,502)**
Comprehensive result	**6,882,932**	**(1,565,788)**	**(2,409,466)**	**(2,548,857)**	**(2,417,655)**

Per share data	**3Q 2004**	**3Q 2003**	**2003**	**2002**	**2001**
Earnings per share	0.22	(0.17)	(0.29)	(0.68)	(1.18)
Earnings per share fully diluted	0.20	(0.12)	(0.18)	(0.50)	(0.98)
Outstanding shares	30,855,458	9,429,237	8,383,336	3,747,815	2,035,022
Outstanding shares fully diluted	33,879,934	12,754,940	12,948,957	5,163,834	2,442,297

Per share data (after reverse split 5:1)	**3Q 2004**	**3Q 2003**	**2003**	**2002**	**2001**
Earnings per share	1.12	(0.83)	(1.43)	(3.41)	(5.91)
Earnings per share fully diluted	1.02	(0.61)	(0.92)	(2.48)	(4.92)
Outstanding shares	6,171,092	1,885,847	1,676,667	749,563	407,004
Outstanding shares fully diluted	6,775,987	2,550,988	2,589,791	1,032,767	488,459

8.3 Consolidated balance sheets

Balance sheet (figures in USD)

Assets	**Q3 2004 (unaudited)**	**Q3 2003 (unaudited)**	**2003**	**2002**	**2001**
Current Assets					
Cash and cash equivalents	66,443	338,756	50,920	124,015	277,841
Trade accounts receivable	124,850	64,189	16,455	22,536	26,052
Other current assets	387,828	47,035	39,009	39,361	488,697
Total current assets	**579,121**	**449,980**	**106,384**	**185,912**	**792,590**
Other assets	76,744	57,978	49,914	75,372	113,238
Total assets	**655,865**	**507,958**	**156,298**	**261,284**	**905,828**
Liabilities and shareholders´ deficit					
Current liabilities					
Accounts payable	594,956	160,178	367,416	317,768	163,470
Accrued expenses and other current liabilities	458,000	1,371,794	1,840,506	498,234	479,480
Total current liabilities	**1,052,956**	**1,531,972**	**2,207,922**	**816,002**	**642,950**
Convertible note payable and accrued interest thereon, subsequently converted to equity	-	3,492,657	3,550,730	3,318,440	2,500,000
Bridge loans	300,000	1,043,671	1,093,333	852,666	-
Deferred revenues and royalties	-	4,076,174	3,784,507	4,951,174	6,117,841
Total liabilities	**1,352,956**	**10,244,193**	**10,636,492**	**9,938,282**	**9,260,791**
Shareholders´deficit					
Common stock	3,158,686	1,022,629	1,022,629	496,081	236,649
Additional paid-in capital	20,680,006	19,915,892	19,915,892	18,836,170	17,868,780
Accumulated deficit	(24,480,698)	(30,575,037)	(31,363,630)	(28,970,305)	(26,413,458)
Accumulated other comprehensive loss	(55,085)		(55,085)	(38,944)	(46,934)
Total shareholders´deficit	**(697,091)**	**(9,636,516)**	**(10,480,194)**	**(9,676,998)**	**(8,354,963)**
Total liabilities and shareholders´deficit	**655,865**	**507,958**	**156,298**	**261,284**	**905,828**

8.4 Cash flow analysis

(figures in **USD**)	**2003**	**2002**	**2001**
Cash flow from operating activities	(1,537,364)	(2,032,706)	(3,563,661)
Cash flow from investing activities	(16,981)	(19,147)	-
Cash flow from financing activities	1,499,262	1,854,911	2,601,543
Effect of exchange rate changes on cash/cash equivalents	(18,012)	43,116	(5,422)
Net change in cash and cash equivalents	**(73,095)**	**(153,826)**	**(967,540)**
Cash and cash equivalents, beginning of year	**124,015**	**277,841**	**1,245,381**
Cash and cash equivalents, end of year	**50,920**	**124,015**	**277,841**
Non-cash investing and financing activities			
Conversion of bridge loans and accrued interest to equity	(858,973)	-	-

8.5 Management's discussion and analysis of financial condition

8.5.1 Introduction

DynaPel has been a development company since its incorporation in 1992 and through 1999. In 1999 the Company saw its first revenues from the sale of video-editing products. After the decision to focus on the security surveillance market in 2002, revenue from sales of security products started in 2003. The future revenues are expected to mainly come from sales in the security market.

8.5.2 Income statement development 2001-2003

From the fiscal year 2000, DynaPel has reported non-cash royalty-revenues related to the Broadcast License Agreement, where DynaPel in 1999 received advanced royalties of USD 5.8 million which has been recognised ratably over the term of the Broadcast License (for a more detailed description, see note 3 in the enclosed 2003 Consolidated Financial Statement, appendix 3). This agreement was terminated in April 2004. Other sales are revenue related to the sale of technology, video editing products and security products.

Operating expenses consists of normal expenses such as personnel costs, rental, travel etc. DynaPel's costs related to research and development are mainly engineer work and the cost has been posted as operating expense every year.

8.5.3 Balance sheet development 2001-2003

DynaPel's assets consists mainly of bank deposits, accounts receivables and property and equipment which consists of computers and office equipment.

Accrued expenses and other current liabilities increased in 2003, mainly due to the difficult financial situation in DynaPel Laboratories GmbH. The settlement agreement with the insolvency administrator resulted in a USD 1,317,879 gain in Q2 2004 and removal of liabilities from the balance sheet.

In September 2000, the Company entered into a short-term financing arrangement ("Loan Agreement") with Technoinvest, a German entity, under which the Company could borrow a maximum of USD 2,500,000. In December 2001, the Loan Agreement was amended whereby the lender waived repayment of the outstanding balance of the loan subject to the improvement of the financial condition of the Company. In March 2004, the Company modified the terms of its existing agreement with Technoinvest whereby the outstanding convertible note payable in the amount of USD 2,500,000 and all current and accrued interest totaling approximately USD 3,603,202 was converted into 80,000 common shares of the Company (par value USD 0.50), with a value of approximately USD 57,000, and NOK 400,000 (USD 57,154). The Company recognized a gain of USD 3,546,048 on this troubled debt restructuring in Q1 2004.

Since 2002, the Company has financed its operations through private and public issues and convertible bridge loans. In August 2002, approximately NOK 6 million was raised through a convertible bridge loan that was converted into 31,7 million shares (par value USD 0.01) in January 2003. In addition, the Company raised NOK 3.5 million through a public issue in January 2003. In June 2003, a USD 1 million bridge loan was entered into which was converted into 78.2 million shares (par value USD 0.01) in January 2004. Also in January 2004, the Company raised NOK 10.14 million through a private issue and in March 2004 an additional NOK 3 million in a public issue. (For a more detailed description, see notes to the enclosed 2003 Consolidated Financial Statement).

Prepaid royalties under the Broadcast License Agreement has been booked as deferred revenues and royalties under liabilities and as been recognized ratably over the term of the agreement. The Broadcast License was terminated in April 2004, resulting in income of USD 3,492,840 in Q2 2004.

In April 2004, the Company signed a License Termination Agreement with a company related to the Kirch Group, which had the effect of terminating any and all ongoing agreements or amendments to agreements, including the Broadcast License. In connection with the termination of the License Agreement, the Company recognized all outstanding deferred royalties and deferred revenue in the second quarter of 2004 resulting in income of USD 3,492,840, which will be reported as other income in the accompanying consolidated statement of operations and comprehensive income.

In June 2004, the Company entered into a settlement agreement with the Insolvency estate of DynaPel Laboratories GmbH. Pursuant to this agreement, the Company agreed to the following in exchange for its release from all liabilities outstanding as of the time of settlement:

1. Upfront payment of USD 100,000
2. Through 31 December, 2004, pay:
    a. USD 400 per unit sold to existing customers of DynaPel Germany, with a minimum payment of USD 100,000 and a maximum payment of USD 200,000.
    b. All royalties received from existing contracts for the on-line products in Germany with a minimum payment of USD 50,000 and a maximum payment of USD 100,000.
3. Pay an additional USD 150,000 if the Company raises a minimum of USD 1,000,000 from investors through 30 June, 2005.

Based on 2004 sales in Germany, the Company expects to pay the minimum amounts under b. above. As of 30 September, 2004, the Company recorded a liability in the amount of USD 400,000 and removed from its books all assets and liabilities related to its bankrupt subsidiary, resulting in a gain of USD 1,317,879. In October 2004 the Company paid USD 50,000 against the outstanding liability.

As of 30 September, 2004, the Company had approximately USD 11,283,000 of net operating loss to carry forward, which expires at various dates beginning in tax year 2008 through to 2023. The availability to offset income taxes in future years may be restricted if the Company undergoes an ownership change, which may occur as a result of future sales of any stock and other events. In assessing the reliability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. As described in section 9.1.1, there has been no determination of whether the Company's share issuances during the years and the Share Issue related to the IPO will qualify as changes in ownership that limits net operating loss to carry forward. The ultimate realization of deferred tax assets depends on the generation of future taxable income and tax planning in making these assessments.

8.5.4 Cash flow development 2001-2003

Due to research and development of new products and lack of sales, DynaPel has experienced negative cash flow from operations. This has been financed by convertible bridge loans and share issues, mainly in the Norwegian financial market.

8.5.5 Events subsequent to Q3 2004

In order to finance operations, DynaPel has entered into a short term secured convertible bridge loan of up to NOK 7 million whereof NOK 7 million has been paid to the Company per 31 December, 2004. The loan has an interest rate of 20% p.a., and the loan plus accrued interest plus a risk premium factor of 25% can be converted into shares at a conversion price equal to the Subscription Price in the Share Issue described in section 2. The short term secured convertible bridge loan is secured by all inventories, equipment, patents and associated know-how held by DynaPel and its subsidiary, Holon Technology GmbH. In addition, all of DynaPel's shares in Holon Technology GmbH are pledged. Holon Technology GmbH guarantees for all of DynaPel's obligations under the bridge loan agreement.

8.6 Sales per product segment

Product (figures in **USD**)	**Q3 2004**	**Q3 2003**	**2003**	**2002**	**2001**
Security	240,199	115,937	181,485	0	0
Broadcast	50,700	0	0	0	0
Other	61,757	213,719	241,884	265,620	257,501
Total sales	**352,656**	**329,656**	**423,369**	**265,620**	**257,501**

8.7 Investments

Costs related to research and development has been included as costs in the P&L and not activated in the balance sheet. Other investments are limited to normal computer and office equipment investments.

During the last year, the Company has done two investments:

1. A EUR 25,000 investment when setting up the new German subsidiary Holon Technology GmbH.
2. A settlement agreement with the Insolvency estate of DynaPel Laboratories GmbH where the Company will compensate the Insolvency estate with up to USD 550,000, whereas USD 100,000 in up front payment (USD 50,000 paid in Q3 2004 and USD 50,000 in January 2005), from USD 50,000 to USD 100,000 for the transfer of existing license agreements to DynaPel, from USD 100,000 to USD 200,000 for future sales to customers of DynaPel Laboratories GmbH, and USD 150,000 upon completion of the IPO financing. In an amendment to the settlement agreement, the Insolvency estate transfers all IPRs held by DynaPel Laboratories GmbH to DynaPel.

Investments (USD)	**2004**	**2003**	**2002**	**2001**
Holon Technology GmbH	30,000	0	0	0
Insolvency estate DynaPel Laboratories GmbH	50,000	0	0	0
Other significant investments	0	0	0	0
Total investments	**80,000**	**0**	**0**	**0**

The Company has not any planned investments for the time being, and do not expect any future investments related to its current business except for the final payment to the Insolvency estate of DynaPel Laboratories GmbH.

8.8 Related party transactions

Short term secured convertible bridge loan
Three board members, Mr. Ralph Carballal, Mr. Helge Nielsen and Mr. Ivar Formo are involved, or related to lenders in the short term convertible Bridge loan described below in section 8.9. Ralph Carballal is personally lending NOK 200,000 to the Company through the convertible Bridge loan. Ivar Formo's adult son participate with NOK 300,000 in the Bridge loan and IWE AS, a company fully owned by Ivar Formo's two adult sons participate with NOK 150,000 in the Bridge loan. Helge Nielsen's adult son participate with NOK 500,000 in the Bridge loan, whereof NOK 100,000 is assigned from Helida AS, a company partly owned by Helge Nielsen (12.5%) which was initially participating in the Bridge loan with NOK 100,000. The remaining shares in Helida AS is owned by Helge Nielsen's wife and adult sons. Neither Helge Nielsen nor Ivar Formo have controlling influence of their adult sons, and shares owned by the sons are not consolidated into Helge Nielsen and Ivar Formo's holding of shares. The additional increase in ownership for Ralph Carballal from a potential conversion is described in chapter 7, and section 8.9 below.

Agreement with Procon AS
The Company has entered into an agreement with Procon AS, a financial advisor to DynaPel in relation to the IPO process and establishing the short term secured convertible bridge loan and the Underwriting Syndicate, on 21 September 2004. Procon AS currently owns 50,418 shares in DynaPel and is controlled 100% by Bjarne Støtvig. According to this agreement, and upon successful completion of the IPO, DynaPel will issue 400,000 warrants (after the reverse splits described herein) to Procon AS exercisable at a conversion price equal to the subscription price of the IPO described herein and which expire two years from the date they are granted (February 2005). In addition, the Company will compensate Procon AS with a cash consideration of 3.5% of the proceeds raised by Procon AS according to the engagement, both for proceeds raised in relation to the short term secured convertible bridge loan and certain money raised for the guarantee consortium. The warrants and the cash consideration (approximately NOK 340.000) are contingent on the successful listing of the Company on the Oslo Børs prior to February 2005, see also section 10.7.

8.9 Significant debt obligations

Short term secured convertible bridge loan
To bridge the financing requirement until the IPO, the Company entered into a short term secured convertible Bridge loan agreement of NOK 7 million in the period September - December 2004. The loan and accrued interest mature on 28 February 2005, unless an event of default or a full or partial sale or spin-off of the Company in which it matures at such time. It is defined an event of default if it becomes obvious that the Company can not be listed at the Oslo Stock Exchange during the loan period (up until 28 February 2005). The loan plus accrued interest of 20% p.a, plus a risk premium factor of 25% can be converted into

shares. The conversion right has to be declared before 28 February, 2005, and the conversion price will be equal to the Subscription Price in the Share Issue described in section 2.

The convertible Bridge loan is secured by all inventories, equipment, patents and associated know-how held by DynaPel and its subsidiary, Holon Technology GmbH. In addition, all of DynaPel's shares in Holon Technology GmbH are pledged. Holon Technology GmbH guarantees for all of DynaPel's obligations under the Bridge loan agreement.

The loan was raised in the Norwegian market, and the lenders consist partly of existing shareholders (about 50%) and some new investors (see also section 10.7). In the opinion of the Board of Directors, the Bridge loan was entered into on market terms taking into consideration the financial situation of the Company and that the Company had an alternative offer from US investors with terms that were less favorable. The Board of Directors decided that it was not practical to ask all shareholders for participation in the bridge loan, and as a US Delaware company, DynaPel's shareholders do not have pre-emptive rights related to such transactions.

Settlement agreement with the bankruptcy estate of DynaPel Laboratories GmbH
As described in section 8.5.3 and section 8.7, a settlement agreement was entered into in June 2004 between DynaPel and the Insolvency estate of DynaPel Laboratories GmbH. According to this settlement agreement, DynaPel will compensate the Insolvency estate with up to USD 550,000, whereas USD 100,000 shall be paid as up front payment, up to USD 100,000 shall be paid for the transfer of existing license agreements to DynaPel, up to USD 200,000 shall be paid for future sales to customers of DynaPel Laboratories GmbH, and up to USD 150,000 shall be paid for financial investments until 30 January 2005. In an amendment to the settlement agreement, the Insolvency estate also transfers all IPRs held by DynaPel Laboratories GmbH to DynaPel. However, the insolvency proceedings are not finalised, and the possibility for claims directed to the bankruptcy estate due to circumstances not known to date, cannot be excluded.

8.10 Use of financial instruments

The Company's operating costs are mainly in USD and EUR, with a current split of approximately 50/50. Cost of goods sold is purchased in EUR today. In addition, some costs are in NOK. Revenues are mainly in USD, but sales in Europe are in EUR. Depending on the actual mix of both cost and revenues, the Company's results may be exposed to currency risk, mainly in the EUR/USD exchange rate. The Company considers this exposure to be limited and will for the time being not do anything in order to hedge any currency positions.

8.11 Auditors

Up and including the accounting year 2001, DynaPel's auditor has been KPMG LLP, 303 Peachtree St., Atlanta GA 30308, USA.

From and including the accounting year 2002, DynaPel's auditor is Israeloff, Trattner & Co. P.C., 1225 Franklin Avenue, Garden City, NY 11530, USA. DynaPel decided to change its auditor based on an incentive from its former auditor, KPMG LLP, which also audited the German Kirch Group. The main reason for KPMG LLP's initiative was to avoid any possible problems or conflict of interest in connection with the recent bankruptcy of the Kirch Group.

9 Risk Factors

9.1 Business, markets and strategy

Investing in DynaPel involves inherent risks. Prospective investors should carefully consider the risks discussed below, other information contained in this Prospectus, and their own information and analysis before making an investment decision. The trading price of DynaPel could decline due to various factors, and investors could lose all or part of their investment. The risks include those discussed below, factors not mentioned here, additional risks that are currently not considered to be material or of which the Company is not presently aware of, and factors that become more or less important over time. If any of the following risks actually occur, DynaPel's business, financial condition and operating results could be materially and adversely affected.

All forward-looking statements included in this prospectus are based on information available on the date hereof, and DynaPel assumes no obligation to update any such forward-looking statements. Investors are cautioned that any forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties and that actual results may differ materially from those included within the forward-looking statements as a result of various factors. Factors that could cause or contribute to such differences include, but are not limited to, those described below and elsewhere in this Prospectus.

9.1.1 Factors that may affect future operating results

The following risk factors and other information should be carefully considered. The risks and uncertainties described below are not the only ones DynaPel face. Additional risks and uncertainties not presently known to DynaPel or that the Company currently deem less significant also may impair the business operations. If any of the following risks actually occur, DynaPel's business, financial condition and operating results could be materially and adversely affected.

Dependence on management and key employees

The Company is operated by a small number of employees. The key employees and management are highly qualified. The Company's ability to keep those employees within the DynaPel organization may be considered decisive for the operation of the Company's business and the development of the Company's technology. DynaPel's business will suffer if it cannot hire and retain appropriate, competent personnel. If unable to hire and retain appropriate, competent personnel, particularly operational and technical personnel, the Company's growth may be restricted, the quality of its services and revenues reduced, and the value of an investment in DynaPel may be reduced.

The Company's success will depend to a significant extent on the ability to assimilate any changes in the leadership team and to retain the services of the executive officers and other key employees. DynaPel does not have employment contracts for a defined term with the employees, including the executives and key employees. Furthermore, the employment contracts with executives and key employees do not include binding non-compete clauses. If DynaPel loses the services of one or more of the executives or key employees, including if one or more of the executives or key employees decided to join a competitor or otherwise compete directly or indirectly with the Company, this could harm the business and could affect the ability to successfully implement the business objectives.

Operating history

DynaPel was established in 1992 and began testing its technology and business concept, leading to a commercial launch currently in progress. For a relatively young company, the collective management experience spans decades. As a company in its commercialisation phase relying to some extent on products and services under development, there will be risks relating to the ability to implement the Company's strategy successfully.

Managing the operations

It will be crucial for the Company's development to efficiently and successfully expand the operations such that the expenses do not grow disproportionately to revenues or that the revenues grow more slowly than expected. There are risks and uncertainty related to the operational development and that a disproportional development could have an adverse effect on the market capitalization of DynaPel.

Failure to manage growth, improve infrastructure, and satisfactorily implement new systems may adversely affect the business. DynaPel's management personnel need to effectively manage several geographic locations, develop new products that utilize the assets of the Company, and to further develop cost-effective standards, controls, procedures and policies. If the Company does not succeed in addressing these risks or any other problems encountered in connection with growth, the business, operating results and financial condition could be adversely affected.

Any restructurings may result in management distraction, customer uncertainty, and increased costs.

DynaPel has only to a limited extent written running agreements with its customers, and most of its commercial contracts are made on ad hoc basis. In some of DynaPel's customer contracts, DynaPel has issued indemnification regarding its distributor, licence and other commercial agreements.

Company records
To some extent, DynaPel's historic company records are incomplete or missing. Furthermore, to some extent, DynaPel's agreements and other formal documentation are lacking signatures. The board of directors has reviewed these issues and in the opinion of the board they are not considered to be a material risk to the ongoing operations of the Company.

International operations
DynaPel's international sales and operations subject the Company to additional risks that can adversely affect the operating results. The international operations are subject to a variety of risks, including: the overlap of different tax regimes; differing regulatory and legal requirements and employment schemes, and the ability to identify and timely comply with such requirements and schemes; fluctuations in currency exchange rates; the need to localize and internationalise the products and licensing programs; seasonal reductions in business activity during the summer months in Europe and certain other regions; and reduced protection for intellectual property rights in some countries. To date, DynaPel has not used risk management techniques or "hedged" the risks associated with fluctuations in foreign currency exchange rates, hence the Company has foreign currency exchange risk between the following currencies USD, EUR and NOK.

Periodic operating results
DynaPel's quarterly operating results may fluctuate for a number of reasons, some of which are beyond the Company's control. These fluctuations may result in volatility in the stock price. The quarterly operating results will likely vary significantly in the future due to revenue fluctuations caused by many factors. The Company believes that quarter-to-quarter financial comparisons may not necessarily be meaningful, and should not be relied upon as single indicators of future operating results and performance. The market price of the common stock has been volatile and DynaPel expects that the stock price will continue to fluctuate. The value of an investment in the stock could decline due to the impact of a number of factors upon the market price of the common stock, including growth rate expectations for the technology sector generally, and variations in the actual and anticipated operating results and revenues. In addition, DynaPel has a history of losses and may experience losses in the future.

Net operating loss to carry forward
As of September 2004, DynaPel had approximately USD 11,283,000 of net operating loss to carry forward (see section 8.5.3). Under section 382 of the US tax code the net operating loss to carry forward could be limited by ownership changes. There has been no determination of whether the Company's share issuances during the years and the Share Issue related to the IPO will qualify as changes in ownership that limits net operating loss to carry forward.

Accounting and regulations
Changes in the way DynaPel do business may impact the operating results by changing the manner in which the Company is required to account for sales.

DynaPel did not prepare and approve its 2002 and 2003 annual accounts in a timely manner. DynaPel did not file its 2002 and 2003 income tax returns in a timely manner. Failure to prepare, file and approve such accounts and returns may carry significant penalties and interest, which may have a significant impact on the Company's financial condition.

EU has passed an ordinance of use of international accounting standards ("IFRS") for listed companies from and including 2005. US GAAP accounts do not need to comply with the injunction until, from and including 2007. As a listed company on Oslo Børs with US GAAP accounts, DynaPel must comply with IFRS from and including 2007. However, the Company has not initiated any prior compliance or consideration of IFRS.

Dependence on key customers
In most license agreements the customer retains the option not to distribute the licensed software. Many of the Company's customers and potential customers provide various products that provide competitive and overlapping capabilities to some of the solutions DynaPel offer, and they may expand their presence in this and other markets in the future or select other companies' solutions. Major customers also may determine to discontinue or diminish DynaPel's relationship at the conclusion of a current agreement.

Dependence upon immature markets

DynaPel's future results will depend upon the markets maturing so that DynaPel's solutions and new value-adding services will be regarded by customers as sufficiently interesting to be worth investing in. DynaPel is aiming at being both a first mover and a market leader. In the long run, DynaPel will be dependent upon the existence of competitors, partners, and strategic alliances so that customers will not see the risk of making themselves dependent upon a sole provider as an impediment to entering a customer relationship. DynaPel's earnings will depend primarily on existing and future customer agreements for the Company's products and services. The short-term market risk will relate mainly to breakthroughs related to its current products. Investors must be aware that DynaPel is in an early phase of conducting business within the Company's markets, and is dependent upon commercial success within sales and marketing, but also in developing new and attractive products to be acknowledged by a large scale market. A successful launch of future security products for DynaPel may also be dependent on approvals from authorities and organizations which the Company does not hold as of today.

Technological change and introduction of new products and services

The markets are characterized by rapid technological advances, changes in customer requirements, and frequent new product introductions and enhancement. DynaPel's future success will depend mainly upon its ability to enhance its current products and to develop and introduce new products and services that keep pace in the ever-evolving technological developments. Furthermore, it is essential to respond to the changes in customer requirements and to achieve continued market acceptance. Any failure to anticipate or respond adequately to technological development and customer requirements, or any significant delays in product or application development and introduction, could result in a loss of competitiveness and revenues.

To retain and increase revenue the Company must continue to enhance existing products and services and continue to develop new products and services to address the increasingly sophisticated and varied needs of existing and prospective customers. The development of new products and services, and enhancement of existing products and services, entail significant technical and business risks and require substantial lead-time and significant investments in product development. The market for some of the products is in the early stage of development, and DynaPel a recent entrant to such markets and face competition from established competitors. As is common in new and evolving industries, demand and market acceptance for recently introduced products and new market entrants are subject to high levels of uncertainty and risk. Furthermore, new products can quickly render obsolete products that were formerly in high demand, which may include products that currently provide DynaPel with significant revenue.

Intellectual Property Rights (IPR)

DynaPel's current technology and products are only to a limited degree covered by the registered patents and patent applications described in section 5.6, both concerning the Company's products, the Company's technology and the territorial protection of the patents. The Company and Holon Technology GmbH pursue a policy to protect their technology and products through trade secrets and know-how. The trade secrets and know-how are held by Holon Technology GmbH, and are neither documented nor verified, to the extent that they provide exclusivity rights vis-à-vis third parties.

If DynaPel fails to protect its intellectual property rights, competitors may be able to use DynaPel's technology and know how, and this could weaken the Company's competitive position, reduce revenue and increase costs. DynaPel's success is heavily dependent on proprietary technology. The Company relies primarily on a combination of patent, trade secrets, confidentiality procedures and contractual provisions to protect intellectual property in the products and services. These laws and procedures provide only limited protection. Furthermore, DynaPel has no trade marks or copyrights protection. DynaPel presently only maintain 3 granted patents. However, these patents may not provide sufficiently broad protection, both regarding scope, territorial protection and otherwise, or they may not be enforceable in actions against alleged infringes. As well, despite precautions that are taken, it may be possible for unauthorized third parties to copy or reverse engineer aspects of the current or future products or to independently develop similar or superior technology or design concerning the patents the Company owns.

Infringement of DynaPel's patents can be costly for DynaPel either directly (infringement process) or indirectly (loss of sales). DynaPel has spent efforts to avoid patent infringements of the products and that the patent coverage is the best possible to minimize the possibility of IPR problems. In addition, it is possible that there are pre-existing technologies similar to those for which DynaPel has made patent applications, which could undermine DynaPel's patent portfolio.

A claim of infringement against DynaPel could injure the Company's reputation and adversely affect the ability to sell products. Third parties, including competitors and former employees, may claim that DynaPel's current or future products infringe their proprietary rights, and these claims, whether they have merit or not, could harm the business by increasing costs or reducing DynaPel revenue. Such claims could affect the relationships with existing customers and may discourage future customers from purchasing DynaPel products. The intensely competitive nature of DynaPel's industry and the importance of technology to the competitors' businesses may enhance the likelihood of being subject to third party claims of this nature. Any such claims, even if without merit, could be time consuming, result in potentially significant litigation costs or damages, cause product shipment delays and require the Company to enter into royalty or licensing agreements. If DynaPel infringes third party proprietary rights, such infringement may cease the production and/or development of the products and/or technology infringing third parties. Fighting a patent suit is a particularly costly and slow procedure and can potentially have a very negative effect. No search has been conducted to discover to what extent DynaPel and Holon Technology GmbH are infringing third party rights. However, no such claim has been put forward by any third party against DynaPel to date.

Financial condition, future capital needs and uncertainty of additional funding
DynaPel's financial condition and liquidity has prior to the IPO described herein been very difficult, with very limited liquidity. According to the independent auditor's report (dated 27 August 2004) for the audited annual accounts for 2003 and the interim report for the first half year 2004 (Appendix 2 and 3 to this Prospectus), DynaPel had a net capital deficiency which raises substantial doubt about its ability to continue as a going concern. Hence, DynaPel was obliged to issue a short term secured convertible bridge loan described in section 8.9, to secure ongoing business and pay running costs before the IPO. The short term secured convertible bridge loan was taken up by the Company in the period September - December 2004 in the amount of NOK 7 million. DynaPel anticipates that its existing capital resources including net proceeds from the forthcoming equity issue will be sufficient to fund its currently planned operations. Should additional funding be needed, there is no assurance that additional funds will be available on favourable terms or that such funds, if raised, will be sufficient to permit DynaPel to conduct its operations as planned beyond this time frame.

Claims related to the bankruptcy of DynaPel Laboratories GmbH
In January 2004, the management of DynaPel's former German subsidiary, DynaPel Laboratories GmbH, was advised by its auditor to file for insolvency. See section 7.1, section 8.5.3 and section 8.7 for further details. The insolvency proceedings are not finalised as of the date hereof. Although a settlement agreement has been entered into between DynaPel and the bankruptcy estate of DynaPel Laboratories GmbH (on behalf of its creditors), claims from former creditors of DynaPel Laboratories GmbH and others cannot be excluded.

9.1.2 Market Factors

Competition
DynaPel faces competition from a number of existing competitors, as well as potential new competitors, which could result in loss of market share and diminished profits.

World Markets
Any slowdown or cutbacks in spending due to national or international conditions may affect DynaPel's market opportunities.

Exchange rate risk
A large percent of the DynaPel revenues are in USD. The remaining income is mainly in EUR and other currencies depending on sales and products. Operating expenses are divided between USD and EUR. Exchange rate affecting DynaPel is mainly the fluctuations in the USD rate against EUR, but also between USD against NOK. Exchange rate fluctuations affect DynaPel in three main areas: 1) Corporate payments in different currencies give rise to transaction risks: 2) Receivables and debt in foreign currencies give rise to exchange rate differences when accounted in USD: 3) The translation of shareholders' equity into USD carries transaction differences that affect the consolidated shareholders' equity.

Force Majeure
Natural disasters or other incidents may disrupt DynaPel's business. The Company's products are vulnerable to damage from human error, physical or electronic security breaches, power loss and other utility failures, fire, earthquake, flood, sabotage, vandalism and similar events. Any of the foregoing could impact the provision of services and fulfilment of product, and DynaPel's ability to process product orders and invoices and otherwise timely conduct business operations.

9.1.3 Different legal regimes

As described herein, DynaPel is incorporated in Delaware, United States of America, and therefore governed by Delaware and US Law. Delaware Company Law differs to a great extent from Norwegian Company Law. For example do the shareholders of DynaPel not have any pre-emption rights in relation to share issues in general. A general, brief and not exhaustive comparison between the Norwegian Public Limited Companies Act and the Delaware General Corporation Act is included in section 11.1 and section 11.2, and should be read carefully in addition to obtaining necessary legal advise before making an investment decision in DynaPel.

10 Share Capital and Shareholder Matters

10.1 Current share capital

Prior to the Share Issue, DynaPel's share capital equals USD 3,208,685.50 which is comprised of 6,417,371 shares, each with a par value of USD 0.50 and fully paid. DynaPel has only one class of shares. The shares are equal in all respects, and each share carries one vote at DynaPel's general meeting of shareholders.

10.2 Share capital development

Development in share capital (USD)

Year	Type of change	Capital increase	Share capital	New shares	Total no. of shares
2000	Balance at December 31		197 649		19 764 886
June 2001	Issuance of common stock	13 000	210 649	1 300 017	21 064 903
October 2001	Issuance of common stock	26 000	236 649	2 600 034	23 664 937
April 2002	Issuance of common stock	6 028	242 677	602 785	24 267 722
November 2002	Anti dilution, April 2002	196 769	439 446	19 676 862	43 944 584
November 2002	Conversion of Betatechnik loan	9 135	448 581	913 500	44 858 084
November 2002	Issuance of common stock	47 500	496 081	4 750 000	49 608 084
January 2003	Public Issue	176 318	672 398	17 631 770	67 239 854
February 2003	Conversion of Loan	317 300	989 699	31 730 026	98 969 880
May 2003	Issuance of common stock	21 963	1 011 662	2 196 300	101 166 180
August 2003	Issuance of common stock	10 967	1 022 629	1 096 667	102 262 847
February 2004*	Conversion of Loan	782 057	1 804 686	78 205 700	180 468 547
February 2004	Private Issue	1 014 000	2 818 686	101 400 000	281 868 547
March 2004	Rights issue	300 000	3 118 686	30 000 000	311 868 547
March 2004	Reverse split (1:10)	0	3 118 686	0	31 186 856
April 2004**	Conversion of TechnoInvest loan	40 000	3 158 686	400 000	31 586 856
November 2004	Reverse split (1:5)	0	3 158 686	0	6 317 371
December 2004	Issuance of common stock	50 000	3 208 686	100 000	6 417 371

* DynaPel entered into a short term convertible bridge loan in June 2003 under which DynaPel borrowed approximately USD 993,247. In February 2004, the loan including accrued interest was converted into 78,205,700 shares at a conversion price of NOK 0.10 per share.

** A convertible note payable of USD 2,500,000 (plus USD 1,050,730 accrued interest) outstanding towards TechnoInvest Holding GmbH has been re-paid through an agreement in March 2004 where TechnoInvest Holding GmbH accepted a repayment of NOK 400,000 and 400,000 shares, resulting in a gain of approximately USD 3,300,000 in 2004 (see note 5 in 2003 Consolidated Financial Statements attached hereinto as appendix 3).

10.3 Listing on Oslo Børs

DynaPel submitted an application to Oslo Børs on 24 November, 2004 for listing on the SMB List. The Board of Directors of Oslo Børs accepted the application in its meeting on 22 December 2004. The acceptance of stock exchange listing is conditioned upon the following; 1) the completion of a Share Issue in a minimum amount of NOK 20 million, 2) the issuance of an IPO prospectus approved by Oslo Børs, and 3) the strenghtening of DynaPel's financial reporting capability within the first quarter 2005 by employing more employees for such purpose. Subject to the completion of the Share Issue, the first quotation and trading day of the Shares is expected to be at the latest 27 January 2005, unless otherwise decided by Oslo Børs. DynaPel's ticker code will be "DYNA".

If the conditions under the Share Issue described in section 2.2 above are *not* fulfilled, the Share Issue will be cancelled and the Shares subscribed for under the Share Issue will not be registered in the Company Registry. Amounts received from subscribers pursuant to section 2.9 above, will, in such case, be transferred back to each subscriber's bank account from which payment of the respective amounts has been made.

10.4 Shareholder structure

There are approximately 1,350 shareholders in DynaPel. Approximately 25% of the outstanding shares are held by foreign shareholders. The table below lists DynaPel's 20 largest shareholders as of 3 January 2005.

No.	Shareholder	No. of shares	Percentage
1	FOUR SEASONS VENTURE	414 664	7.46 %
2	CARBALLAL RALPH	366 010	5.70 %
3	DNB NOR BANK ASA	280 000	4.36 %
4	ANDERSEN LARS SIGVART GRAN	248 349	3.87 %
5	CAICOS INVESTMENT LT	229 192	3.57 %
6	KONDEK DIETER	205 026	3.19 %
7	PORTFOLIO MANAGEMENT C/O KISTEFOS AS	192 484	3.00 %
8	MORTEN WERRINGS REDE	170 917	2.66 %
9	SIS SEGAINTERSETTLE	170 120	2.65 %
10	VEEL TERJE	167 714	2.61 %
11	SCHIMBERG HENRY AARON	156 380	2.44 %
12	KAUPTHING BANK LUXEMBOURG	147 531	2.30 %
13	ATLAS CAPITAL MANAGE	145 170	2.26 %
14	NIELSEN HELGE	138 559	2.16 %
15	BRØDR. HETLAND AS	124 256	1.94 %
16	FRANS ENGER A/S V/NICOLAI E. LORENTZ	120 634	1.88 %
17	WESSON BRUCE F.	113 190	1.76 %
18	HETLAND KJELL	103 854	1.62 %
19	ENGELSTAD TOM HVISTENDAHL	100 848	1.57 %
20	GREEN TERJE	94 574	1.47 %
	SUM 20 LARGEST	3 689 472	57.49 %
	OTHER	2 727 899	42.51 %
	TOTAL	**6 417 371**	**100.00 %**

10.5 Shareholder information and dividend policy

DynaPel's policy is to pursue a strategy of maximising the shareholder value. This will be achieved by sound business development and an aggressive growth strategy. DynaPel aims to give shareholders a competitive return on capital relative to the underlying risk through share price growth. As a result of a continued high level of research and development and future expansion, DynaPel does not plan to pay dividends to shareholders for the foreseeable future.

DynaPel aims to be an attractive investment, with an open information policy. Initially responsible for the investor relations of DynaPel will be Tore Formo (CFO). One of the main tasks of the CFO will be to handle information requests and inquiries from the market participants in order to secure efficient and consistent information to the market, all in accordance with the laws, regulations and guidelines applicable at any time. DynaPel will pursue an information policy to provide its shareholders timely, relevant and accurate information on material developments. DynaPel intends to give regular presentations of its results and make management available for questions from shareholders and other interested parties.

Information on important events which influence DynaPel valuation will be made public through announcements to Oslo Børs. At the same time the press and public will be informed via press releases. An accurate assessment of DynaPel as an investment requires correct and relevant information. DynaPel aims to make this available on the Investor Relations section of its website, www.dynapel.com.

DynaPel wants the market to have the best possible basis for evaluating its status and prospects. The objective is to enable DynaPel to attract a broad base of investors and to access equity and borrowed capital on favourable terms.

10.6 Stock option plan

DynaPel has adopted stock option plans for its employees, consultants and directors, under which 88,800 options are outstanding as of the date of this Prospectus. The following table summarizes the outstanding stock options:

Description	Options reserved	Options issued	Options expired	Options exercised	Options outstanding	Exercise Price (USD)	Expiration
1998 Plan	55,000	52,000	18,100	10,100	23,800	USD 17.50	28.09.09
2000 Plan	50,000	40,210	18,210	0	22,000	USD 27.50	05.04.10
2001 Plan	50,000	50,000	7,000	0	43,000	USD 1.50	27.12.12

* Under the 1998 Plan, 13,800 options will expire on 21 July, 2005 and 2,400 options on 12 December, 2005.
** Under the 2000 Plan, 11,700 options will expire on 21 July, 2005.

DynaPel's Stock Option plans are governed by a Committee of Non-employee directors, consisting of Live Haukvik Aker, Ralph Carballal and Ivar Formo, designated by the Board. The committee can grant options according to the plans at its own discretion, but only with the approval of the entire Board of Directors. However, the committee and the Board of Directors are subject to the limits of the plans which are approved by the shareholders at the shareholder meeting. In general, all of the Company's option plans contain certain limitations and restrictions. These limitations include a restriction on the total number of options that can be granted under the option plans which is no more than 10% of the outstanding shares in the aggregate. In addition, the option plans restrict the number of options available to non-employee directors to 10% of the option available under the option plans.

When granting options in accordance with the 2004 Stock Option Plan, each option plan dictates that the option price, which is the determined by the committee on the date of the option grant and reflected in the Award Agreement, can not be less than 100% of the fair market value of a share on the day the option is granted.

Pursuant to the Company's stock plans, in general, the issued and outstanding options normally have a 10 year duration, and are subject to the optionee holder remaining employed by the Company. If the employment should terminate, any outstanding options would expire after 90 days of such termination. The option agreements contain detailed regulations with respect to exercisability of the options upon termination of the employment.

Options outstanding under the 1998, 2000 and 2001 Plan are all exercisable as of 1 January, 2005.

Amendments to the 2004 Stock Option Plan require an affirmative vote of a majority of the shares entitled to vote on the matter. The shareholder meeting of DynaPel of 11 February, 2004 authorised the board of directors to issue shares and options at its own discretion without further instructions and authorization of the shareholders, within the limits provided at the shareholder meeting.

At the Special Meeting of Shareholders on 18 November, 2004, it was resolved to amend the 2004 Stock Option Plan to cover stock options exercisable into a maximum of 630,000 shares. Only upon successful completion of the Initial Public Offering, the aggregate number of options that may be granted under the 2004 Stock Option Plan will be increased to 1,230,000 stock options. Stock options will be issued at the discretion of the Board of Directors at exercise prices to be determined in accordance with the plan.

So far, no options have been issued under the 2004 Plan, however DynaPel expects to issue options according to the plan in the first quarter 2005.

DynaPel has considered it necessary to issue incentive plans as described above in order to attract qualified leading employees and directors. Such incentive plans are currently not in compliance with the Norwegian Code of Practise on Corporate Governance. The Company has due to its current financial situation and limited commercial operations adopted a policy of granting a limited number of options to board members as a way to reduce its overall costs and increase it chances for attracting influential industry executives to the board. Following a listing on the Oslo Børs, a strengthened financial position and commercial success, DynaPel will take into account the Norwegian Code of Practise on Corporate Governance when considering incentive plans in the future.

10.7 Warrants and options

Short term secured convertible bridge loan

In order to bridge the financing requirement and secure the running costs of DynaPel until the IPO, a short term secured convertible bridge loan of NOK 7 million with an interest rate of 20% p.a. has been taken up by DynaPel. The loan, accrued interest and a risk premium factor of 25% can be converted into shares of DynaPel at the discretion of each lender. The conversion right has to be declared before 28 February 2005, and the conversion price will be equal to the price per share in the IPO described herein. The lenders are existing shareholders of DynaPel, hereunder, directly and indirectly, the present board members Ivar Formo, Helge Nielsen and Ralph Carballal (as described in section 8.8), and new investors. Many of the lenders in the short term secured convertible bridge loan have, if they decide to exercise their conversion rights under the loan agreement, accepted to postpone conversion and the delivery of new shares to their VPS accounts until DynaPel has held a shareholder meeting and subject to an authorisation to increase the number of authorised shares sufficient to issue the shares (one of the lenders has specified that the shareholder meeting to be held no later than July 2005). See section 8.8 and section 8.9 for further details of the short term secured convertible bridge loan.

Warrants issued to Procon AS

After reviewing alternative proposals, the Company entered into an agreement with Procon AS on 21 September 2004, to be (i) a financial advisor to DynaPel in relation to the short term secured convertible bridge loan, (ii) assist the Company with the formation of an Underwriting Syndicate for the purpose of underwriting NOK 20,000,000 and (iii) assist the Company in the completion of its intended listing. Procon AS currently owns 50,418 shares in DynaPel and is controlled 100% by Bjarne Støtvig. According to this agreement, and upon successful completion of the IPO, DynaPel will issue 400,000 warrants (after the reverse splits described herein) to Procon AS exercisable at a conversion price equal to the subscription price of the IPO described herein and which expire two years from the date they are granted (February 2005). In addition, the Company will compensate Procon AS with a cash consideration of 3.5% of the proceeds raised by Procon AS according to the engagement, both for proceeds raised in relation to the short term secured convertible bridge loan and that portion of proceeds raised for the Underwriting Syndicate from their direct efforts. The warrants and the cash consideration (approximately NOK 340,000) are contingent on the successful listing of the Company on the Oslo Børs prior to February 2005. As previously stated, the Company evaluated a number of alternative actions prior to entering into the arrangement with Procon AS, including a proposal from a US based financial consultant. After careful review of all the proposals available to the Company, the Board concluded that the Procon proposal was significantly lower in cost and had a greater potential for successful completion an eventual listing on the Oslo Børs. Procon's warrants are subject to the completion of the IPO and to an authorisation to increase the number of authorised shares sufficient to issue the shares related to the warrants.

Warrants issued to the CEO of DynaPel, Dieter Kondek

Mr. Dieter Kondek, the CEO of DynaPel, entered into an employment agreement in 2002 which was amended in March of 2004. In accordance with this agreement, Mr. Kondek has received 100,000 non-restrictive shares in the Company issued in December 2004 and is entitled to an additional 500,000 warrants (after the reverse splits described herein). These warrants are exercisable at NOK 5.00 and will vest over the next two years as follows: 200,000 warrants vest on 31 December, 2004, 100,000 warrants vest on 31 December, 2005 or when the stock price exceeds NOK 15.00 per share, 100,000 warrants vest on 31 December, 2005 or when the stock price exceeds NOK 20.00 per share and 100,000 warrants vest on 31 December, 2006 or when the stock price exceeds NOK 30.00 per share. All the options shall vest immediately if more than 2/3 of DynaPel’s shares are purchased by another company or investor. All the conditions related to these warrants are not finally settled as of the date hereof, but will be settled during January, 2005. Dieter Kondek has accepted to postpone any exercise of the warrants until DynaPel has held a shareholder meeting and subject to an authorisation to increase the number of authorised shares sufficient to issue the shares related to the warrants. Dieter Kondek's warrants are supject to the completion of the IPO, and he has accepted to postpone any exercise of the warrants until DynaPel has held a shareholder meeting and subject to an authorisation to increase the number of authorised shares sufficient to issue the shares related to the warrants.

On 28 December, 2004 Dieter Kondek was awarded by the Board 100,000 new shares issued by the Company as consideration for work performed for the Company (without cash consideration).

Generally

After the IPO, the share capital will be maximum USD 6,208,685.5. Including all outstanding options and warrants, conversion of the bridge loan and the maximum options available under the 2004 Option Plan, the share capital will be increased to a maximum of USD 8,653,085.5 (which may be higher or lower depended on the accrued interest under the short term secured convertible bridge loan which also may be converted into shares), an increase of 40%. Such increase is subject to a correspondingly increase in the authorised share capital of the Company.

Other than the warrants described in this section and the options issued under the stock incentive plans described herein, DynaPel has not issued and is not familiar with any agreement or arrangement that provides the right to demand the issue of shares of DynaPel. DynaPel has not issued securities other than shares, options and warrants.

10.8 Authorization to issue Shares

On 11 February 2004, the general shareholder meeting resolved to increase the authorised share capital from 150 million shares to 700 million shares. Following the reverse stock split of 10:1 completed in March 2004 and the reverse stock split of 5:1 completed in December 2004, the authorised share capital consists of 14 million shares. The Board of Directors can issue new shares up to the authorised share capital based on its discretion.

The Board of Directors of DynaPel adopted on 6 January 2005 a formal_resolution authorizing the Share Issue, which resolution authorized DynaPel to issue up to 6 million shares under the Share Issue, based on the authorised share capital of 14 million shares.

10.9 Shareholder agreements

DynaPel is not aware of any shareholder agreements in connection with DynaPel's shares.

10.10 Lock-up agreements

The Board of Directors of DynaPel and the CEO of DynaPel have entered into Lock-Up Agreements with the Manager in which they have undertaken not to pledge, sell, agree to sell or in any other way dispose of or transfer any shares or other instruments in the Company during the period beginning on 10 January 2005 and ending three months after the first day of trading of the DynaPel shares on Oslo Børs. Any transaction restricted by the Lock-up Agreements may only take place with the prior written consent of the Manager. The Lock-Up Agreements have been entered into in order to help stabilize the market for the shares following listing on Oslo Børs. The Board members and CEO's respective shareholdings are as follows:

Name	Position	Number of Shares	Number of Options	Number of Warrants
Helge Nielsen	Chairman	138,559	0	0
Ralph Carballal	Director	366,010	6,300	0
Ivar Formo*	Director	125,665	2,200	0
Live Haukvik Aker	Director	0	0	0
Dieter Kondek	CEO	205,026	0	500,000
Total		835,260	20,700	500,000

* Ivar Formo's holding of shares includes 72,590 shares in DynaPel owned by the company Ullevål Utvikling AS where Ivar Formo has a controlling 50% ownership.

The Lock-up Agreements cover a minimum of 835,260 shares, corresponding to 13.02% of the share capital prior to the Share Issue and between 6.88% and 6.73% of the share capital after the Share Issue.

10.11 Own shares

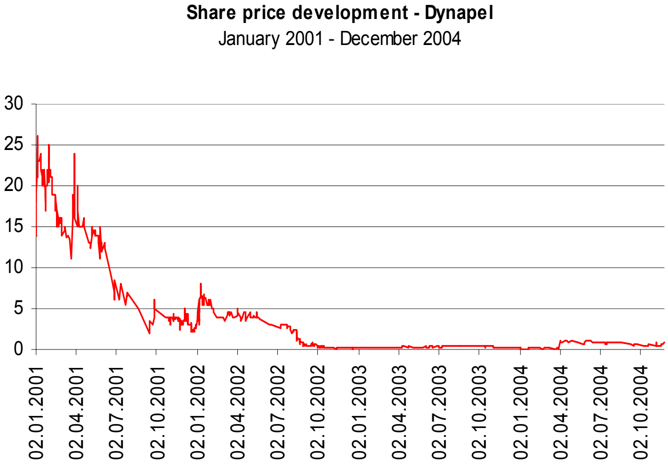
Other than shares which DynaPel may hold in treasury, DynaPel does not own any of its own shares.

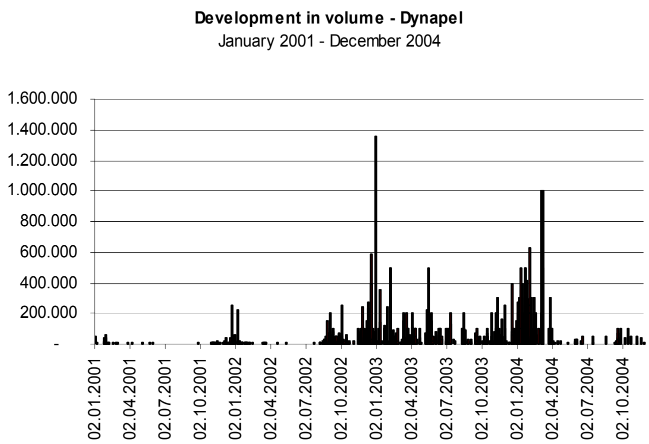
10.12 Transfer of shares

According to DynaPel's Certificate of Incorporation and By-laws, there are no general limitations on the transfer of DynaPel's shares, other than as described in section "Transfer Restrictions" in section 2.10. Except as described in "Transfer Restrictions", the shares are freely tradable.

10.13 Share price development

DynaPel's shares are not currently listed on any stock exchange, but are traded on the Norwegian Over-The-Counter market under the ticker code "DYNA". The trading price per share was NOK 3.90 as of 5 January 2005.





11 Tax and Legal Matters

11.1 Legislation and governing law of DynaPel

DynaPel is incorporated in the State of Delaware in the United States of America ("US"), and is therefore governed by the laws of the State of Delaware, or the Delaware General Corporation Law (the "DGCL"). As an US entity, DynaPel is also subject to US federal legislation, including but not limited to US securities laws. If and when the DynaPel stock is listed on Oslo Børs, DynaPel will also be governed by certain aspects of Norwegian Securities Law, in addition to its obligations under the Listing Agreement with Oslo Børs.

The Norwegian Public Limited Companies Act of June 13, 1997 No. 45 of 1997 will not apply to DynaPel as an US entity. If and when DynaPel is listed on Oslo Børs, DynaPel will be obliged to follow Oslo Børs' listing requirements, including the Norwegian Code of Practice for Corporate Governance (see Børssikulære No. 7 / 2004).

Even though DynaPel is not incorporated under Norwegian Law, certain aspects of Norwegian securities legislation will apply to the Company if and when DynaPel is listed on Oslo Børs including certain prospectus requirements and certain notice and information requirements under the Norwegian Securities Trading Act (with applicable statutory provisions). The mandatory offer requirements in the Securities Trading Act chapter 4 do not, however, apply to foreign companies listed on Oslo Børs.

11.2 Comparison of aspects of Delaware and Norwegian law

Discussed below is a comparison of certain aspects of Delaware and Norwegian and certain descriptions of the applicable law for the Company and its impact on DynaPel. The following summary should not be relied upon as an exhaustive list, nor be regarded as a detailed description, but is only meant to provide a brief introduction. There are exceptions to the general descriptions, both under Delaware and Norwegian Law, hereunder due to provisions in the specific company's certificate of incorporation or by-laws. There are no by-laws under Norwegian Law, only the Articles of Association, which corresponds to the certificate of incorporation under Delaware Law. If not mentioned specifically, DynaPel's certificate of incorporation does not provide for any amendments or provisions that significantly vary from the principles below. Prospective investors should carefully consider the impact of relevant applicable law and the Company's by-laws and certificate of incorporation attached hereto as Appendix 1, and obtain legal advise regarding the impact of such applicable laws, before making an investment decision in DynaPel.

There are certain inherent differences between Norwegian Law and the DGCL, and such differences may impact the rights and obligations of shareholders in DynaPel.

Mergers, sale of assets and other transactions
According to the Norwegian Public Limited Companies Act, extraordinary corporate transactions such as mergers, issuance of shares and granting of authority to the board to issue shares require the affirmative vote of 2/3 of the shares and the share capital represented on a duly convened shareholder meeting, unless the Articles of Association require an even higher percentage. Pursuant to the DGCL, such transactions require the approval of the board of directors of the company and the majority of the outstanding stock entitled to vote thereon, unless the certificate of incorporation provides otherwise.

Amendments to Charters
According to the Norwegian Public Limited Companies Act, changes in the Articles of Association, change in the share capital and the issuance of warrants etc, require 2/3 of the votes of the shares and the share capital represented at a duly convened shareholder meeting. Pursuant to the DGCL, a vote of a majority of all outstanding shares entitled to vote thereon is required for such corporate transactions, unless the certificate of incorporation or the by-laws provide otherwise.

Issuance of shares
According to the Norwegian Public Limited Companies Act, the shareholders meeting approves increase in share capital by the affirmative vote of 2/3 of the shares and share capital represented. The resolution must inter alia be detailed on the maximum and minimum amount of the share capital increase, the par value of the new shares, the share price, and the investors that can be invited to subscribe for shares. The vote must also detail the time and place for the deposit, and the allotment policy. The shareholders meeting may authorize the board to execute the issuance, however the authorization must at a minimum include the amount of the maximum issuance, the time limit of the authorization (being maximum two years), deviation from pre-emptive rights (described below), and certain other requirements.

Pursuant to the DGCL, a company may issue such capital stock (including classes or series thereof) as shall be stated and expressed in the certificate of incorporation or any amendment thereto, or in the resolution or resolutions providing for the issue of such stock adopted by the board of directors pursuant to the authority vested in it by the provisions of the certificate of incorporation. A vote of a majority of all outstanding shares entitled to vote thereon is required for such a change to the certificate of incorporation, unless the certificate of incorporation or the by-laws provide otherwise.

Pre-emptive rights
According to the Norwegian Public Limited Companies Act, shareholders in such Norwegian companies have pre-emptive rights in situations of share issuances etc. The shareholders may waive their pre-emptive rights upon the affirmative vote of 2/3 of the shares and the share capital represented at the shareholder meeting authorising or approving the share issuance. Pursuant to the DGCL, shareholders do not possess these types of rights, unless specifically granted pursuant to the certificate of incorporation or pursuant to a shareholder agreement or otherwise. DynaPel shareholders are not granted such rights under DynaPel's certificate of incorporation.

Dissenter rights
According to the Norwegian Public Limited Companies Act, a majority shareholder that holds more than 90% of the shares and votes of a corporation can "squeeze out" the minority shareholders. Pursuant to the DGCL, shareholders generally have an appraisal right in the event of a merger or consolidation, with certain major exceptions. Further, under the DGCL, majority shareholders may owe, under certain circumstances, certain fiduciary duties to minority shareholders in such situations. According to the Norwegian Public Limited Companies Act, any shareholder in such a Norwegian corporation may demand that a majority shareholder, holding more than 90% of the shares and votes of the company, purchase such minority holder's shares, and conversely, the shareholder with more than 90% of the shares and votes may "squeeze out" the minority shareholders.

Shareholder transactions
Pursuant to the Norwegian Public Companies Act a company cannot, without the affirmative vote of a shareholders at a shareholder meeting, enter into transactions with shareholders, or parties related to a shareholder with a value of more than 5% of the company's share capital, unless the agreements are on standard terms and within the company's ordinary course of business. Pursuant to the DGCL, a company may enter into transactions with shareholders or parties related to a shareholder if the transaction is deemed by the board of directors of the company to be fair and reasonable to the company and in the best interests of the company. Further, under the DGCL, companies are restricted from certain business combinations with interested shareholders unless certain statutory provisions are satisfied.

Dividends
According to the Norwegian Public Limited Companies Act, dividends may only be paid out of available or "free equity" as defined in the Act, and must be adopted by the affirmative vote of shareholders at a shareholder meeting. The shareholder meeting cannot authorize dividend payments exceeding the amount proposed by the board. Pursuant to the DGCL, dividends may be authorised by the board of directors of the company, and paid out of its surplus, or out of net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year, subject to any restrictions contained in the company's certificate of incorporation.

Calling of shareholder meetings
Pursuant to the Norwegian Public Limited Companies Act, the board of directors must call shareholder meetings with minimum two weeks written notice, or such longer period as the Articles of Association may provide. Shareholders representing at least 5% of the shares, may require the board to call for shareholder meetings. Pursuant to the DGCL, shareholder meetings may be called by the board of directors or other persons authorised by the company's certificate of incorporation or its by-laws. The board of directors are authorised to call shareholder meetings by DynaPel's by-laws.

Directors rights and responsibilities
According to the Norwegian Public Limited Companies Act, the number of directors are determined by the Articles of Association. Pursuant to the DGCL, the number of directors shall be fixed by, or in the manner provided in, the by-laws of the company, unless the certificate of incorporation fixes the number of directors. Pursuant to DynaPel's by-laws, the number of directors of DynaPel is required to consist of a minimum of one director and a maximum of twenty directors.

The Norwegian Public Limited Companies Act provides that directors can be removed by a majority vote of shareholders at any meeting of the shareholders called for such purpose. Pursuant to the DGCL, a director can be removed with or without cause by a majority of the shares, entitled to vote thereon, subject to provisions contained in the company's certificate of incorporation and certain other statutory provisions.

The Norwegian Public Limited Companies Act contains certain provisions regarding the company's ability to claim personal liability of the board and certain officers for negligence and wilful misconduct. Pursuant to the DGCL, a company may indemnify any person who is or was a director, officer, employee or agent of the company, or is or was serving at the request of the company, if the person acted in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the company, and, with respect to any criminal action or proceeding, had no reasonable cause to believe that the person's conduct was unlawful. DynaPel has agreed pursuant to its certificate of incorporation to indemnify its board of directors, and limit the liability of its board of directors, for certain breaches of a director's fiduciary duty.

According to the Norwegian Public Limited Companies Act, a director may not participate in company decisions where the director has a special interest as defined in the Act, and the decision may be void if the directors' unlawful participation has influenced the decision. Pursuant to the DGCL, contracts or transactions are not void or voidable solely based on a director's interest in the contract or transaction, financial or otherwise, so long as such contract or transaction was; (1) undertaken with full disclosure of the material facts and the board of directors in good faith authorised it by a majority vote of disinterested directors; or (2) undertaken with full disclosure of the material facts and the shareholders in good faith authorised it by a vote of the shareholders entitled to vote thereon; or (3) fair to the company as of the time it is authorised, approved or ratified, by the board of directors, a committee of the board of directors or the shareholders.

11.3 Taxation of Norwegian shareholders

11.3.1 Introduction

This sub-section provides a presentation of tax issues related to the Common Shares based on Norwegian tax regulations in force at the date of this Prospectus. The description is of general nature and does not intend to be a complete analysis of all possible tax issues relating to the Common Shares. Accordingly, prospective holders of Common Shares should consult their tax advisers as to the consequences under the tax laws of Norway and elsewhere.

This summary is further subject to any change in law that may take effect after the date of this Prospectus. This also includes changes taking effect on a retroactive basis.

The summary applies to Norwegian shareholders meaning shareholders being resident in Norway for tax purposes. Accordingly, the summary does not necessarily apply to shareholders being tax liable to Norway from holding Common Shares attributable to a place of business maintained by the shareholder in Norway.

The Government's outline of a Tax Reform was presented in a White Paper late March 2004, and new tax rules regarding tax on dividends and capital gains on shares were enacted December 2004. A description of the new rules is included below.

11.3.2 Norwegian Tax on dividends

Individual shareholders

Any dividend distributed from the Company to Norwegian individual shareholders is taxable as general income for the Norwegian shareholders. The current tax rate is 28%. The current Norwegian imputation system does not apply to dividends from a foreign company. According to the tax treaty between the U.S. and Norway, the withholding tax on dividends distributed from a company resident in the U.S. to a Norwegian shareholder shall not exceed 15 percent. Norwegian shareholders can be entitled to tax credit for withholding tax paid in the U.S.

As from January 1, 2006 the imputation system is abolished for individual shareholders, and dividends received by such individual shareholders will be taxable as general income at a rate of 28%. However, this will only apply for dividends exceeding a calculated risk-free return. The new legislation will apply also to dividends from a foreign company.

Joint-stock companies and similar entities

The Norwegian Government has enacted, effective from 26 March, 2004 that dividends shall not be taxable for joint-stock companies and similar entities. Exception is to be made for dividends from joint-stock companies and similar entities resident outside the European Economic Area. Such dividends are only exempt from tax if the shareholder for a continuous period of two years has owned at least 10% of the company's capital and had at least 10% of the votes on the shareholder's meeting. If these conditions are not met, the dividends are taxable as general income. The current tax rate is 28%. However Norwegian shareholders can be entitled to tax credit for withholding tax paid in the U.S.

11.3.3 Norwegian Tax on capital gains on shares

Individual shareholders
Capital gains derived from disposal of Common Shares by Norwegian individual shareholders are taxable as general income, and losses are deductible in the general income. This applies irrespective of the length of time the Common Shares are held. The current tax rate is 28%. The capital gain or loss on the disposal of Common Shares is calculated as the balance between the consideration received and the cost price. Costs in connection with both the purchase and the sale of Common Shares are deductible when calculating capital gain or loss.

The current adjustment of cost price regulations (RISK) does not apply to shares in foreign companies. A "first in - first out" principle (FIFO) will apply, implying that the Common Shares that are acquired first are deemed to be sold first.

As from January 1, 2006 capital gains on shares for individual shareholders will still be taxed as general income at a rate of 28%. However, capital gain will be exempt from tax to the extent the capital gain, included received dividend from the same share, are inside of a calculated risk-free return in the period of ownership. This will also apply to Common Shares in foreign companies.

Joint-stock companies and similar entities
The new legislation effective from 26 March, 2004 entail that capital gains on Common Shares are exempted from taxation and that losses no longer are deductible for joint-stock companies and similar entities. This will also apply to Common Shares in foreign companies. Exception is made for gains/losses derived from disposal of Common Shares in joint-stock companies and similar entities resident outside the European Economic Area. Such gains are only exempted from taxation and losses deductible if the shareholder for a continuous period of two years prior to the realization has owned at least 10% of the company's capital and had at least 10% of the votes on the shareholder's meeting. The current tax rate is 28%.

11.3.4 Norwegian net wealth tax

Shareholders resident in Norway for tax purposes, with the exception of joint-stock-companies and similar entities, will be subject to net wealth tax on their Common Shares. Listed shares in foreign companies are, from January 1, 2005, valued at 65% of the quoted values as of January 1 in the assessment year. Shares in foreign companies that are not listed are as a rule valued at 65% of the shares presumed value. The marginal net wealth tax is presently 1.1%.

The 2005 budget documents include a proposal to gradually reduce the net wealth taxation.

11.3.5 Norwegian duties on transfer of tax

No duties are currently imposed in Norway on the transfer of shares, neither on acquisition nor disposal.

11.4 Legal issues

DynaPel is not involved in any legal disputes that may have material impact on its activities or the evaluation of the Company.

The Company's former German subsidiary, DynaPel Laboratories GmbH, filed for insolvency proceedings in January 2004. Due to significant business intervention with the bankrupt German Kirch Group GmbH, DynaPel decided to wind up DynaPel Laboratories GmbH.

A settlement agreement was entered into in June 2004 between DynaPel and the Insolvency estate of DynaPel Laboratories GmbH. According to this settlement agreement, DynaPel shall compensate the Insolvency estate with up to USD 550,000, whereas USD 100,000 shall be paid as up front payment, up to USD 100,000 shall be paid for the transfer of existing license agreements to DynaPel, up to USD 200,000 shall be paid for future sales to customers of DynaPel Laboratories GmbH, and up to USD 150,000 shall be paid for financial investments until 30 January, 2005.The insolvency proceedings are not finalised, and the possibility for claims directed to the bankruptcy estate due to circumstances not known to date, cannot be excluded.

12 Norwegian Summary

Det norske sammendraget er underordnet den engelske teksten og den mer detaljerte informasjonen i Prospektet for øvrig, samt vedleggene. Investorer som vurderer å tegne aksjer i henhold til Tilbudet oppfordres innstendig til å lese hele Prospektet, herunder kapittel 9 om risikofaktorer, for å foreta sin egen vurdering.

12.1 Beskrivelse av selskapet

12.1.1 Historikk

De to norske forskerne, Dr. Gudesen og Dr. Martens, startet i 1988 et forsknings- og utviklingsinitiativ som førte til oppstart av flere teknologiselskaper, herunder DynaPel. DynaPel ble etablert i 1992 og utvikler intelligente videoprodukter for overvåkings- og kringkastingsindustriene. Selskapet har i den senere tid mottatt et økende antall ordrer gjennom sitt leverandør/salgsnettverk.

12.1.2 Beskrivelse av virksomheten

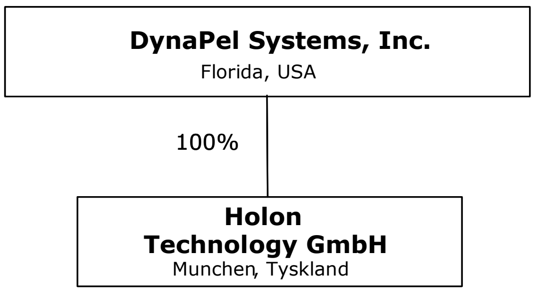
DynaPel har en målsetning om å være en teknologileder innen selskapets definerte kjerneområder; intelligent videoanalyse og løsninger innen video-overvåkingsindustrien. Dette skal oppnås gjennom et nært samarbeid med verdensomfattende leverandør/salgsnettverk. DynaPel har utviklet produkter og løsninger innen områdene videoalgoritmer, digital videobevegelsesanalyse, videokompresjon og kontroll.

DynaPel har organisert sine salgs- og markedsaktiviteter gjennom både OEM-kanaler og etablerte distributør/leverandør salgsrepresentant kanaler.

Selskapet fokuserer på forsknings- og utviklingsaktiviteter gjennom sitt heleide datterselskap Holon Technology GmbH. Sikkerhet og overvåking er fokus for selskapets fremtidige forsknings- og produktutvikling.

12.1.3 Organisasjon

DynaPel-gruppen består av to operative enheter som vist i figuren nedenfor.



DynaPel Systems Inc er et amerikansk selskap, registrert i delstaten Delaware, med hovedkontor i Fort Myers, Florida, USA. Selskapets aktiviteter innen regnskap, salg, markedsføring, teknisk støtte og logistikkfunksjoner er lokalisert i Fort Myers, Florida. DynaPels forsknings- og utviklingsaktiviteter, inkludert et ingeniørteam, er lokalisert i Munchen, Tyskland og utøves gjennom det heleide datterselskapet Holon Technology GbmH.

DynaPels tidligere tyske datterselskap, DynaPel Laboratories GmbH, søkte om konkursbeskyttelse i januar 2004. Denne prosessen pågår fortsatt. Det nylig etablerte datterselskapet, Holon Technology GmbH, har fortsatt det tidligere datterselskapets virksomhet. Se kapittel 7.1 for ytterligere beskrivelse.

12.2 Risikofaktorer

DynaPel Systems Inc er et relativt ungt selskap med nye produkter i et umodent marked. All investering i aksjer innebærer risiko og potensielle investorer oppfordres til å gjøre seg kjent med hele Prospektet og spesielt innholdet av kapittel 9 som omhandler risiko, samt innhente egen informasjon og gjøre egen analyse før investeringsbeslutning fattes.

Investorer bør spesielt være oppmerksom på at DynaPel har vært i en svært vanskelig finansiell situasjon med svært begrenset likviditet i store deler av 2004. I henhold til revisors uavhengige revisjonsrapport (datert 27. august 2004) for det reviderte regnskapsåret 2003 samt den reviderte delårsrapporten for første halvår 2004 (vedlegg 2 og vedlegg 3), hadde DynaPel et netto kapitalunderskudd som reiste vesentlig tvil om hvorvidt Selskapet var i stand til å fortsette videre drift. DynaPel var derfor avhengig av å utstede et konvertibelt lån beskrevet i kapittel 8.8, 8.9 og 10.7 for å sikre videre drift i forkant av pågående børsnotering.

DynaPels suksess er avhengig av proprietær teknologi. Beskyttelse fra gjeldende regelverk og prosedyrer er begrenset. Potensielle investorer bør være kjent med at ikke-autoriserte tredjeparter kan kopiere ulike aspekter av gjeldende eller fremtidige produkter, eller utvikle tilsvarende eller bedre teknologi. Tredjeparter, inkludert konkurrenter og tidligere ansatte, kan også hevde at DynaPels nåværende eller fremtidige produkter krenker deres immaterielle rettigheter. Slike krav, berettigede eller ikke, kan ha en svært negative effekt for selskapet. Ingen slike krav er fremmet fra tredjepart mot DynaPel per dato for dette prospekt.

12.3 Finansielle opplysninger

Tabellen nedenfor gir et sammendrag av resultatregnskap, balanse og nøkkeltall for Selskapet for årene 2001, 2002 og 2003, samt 3. kvartal 2003 og 2004. En mer inngående beskrivelse av Selskapets finansielle stilling finnes i kapittel 8 av Prospektet og Selskapets årsrapport og regnskap for 2003 (vedlegg 3 til Prospektet).

Tall i USD	**3.kv. 2004**	**3.kv. 2003**	**2003**	**2002**	**2001**
Driftsinntekter	644.323	1.204.583	1.590.036	1.432.287	1.424.168
Driftskostnader	2.056.262	2.770.488	3.986.488	3.572.809	3.812.239
Ordinært resultat	6.882.932	(1.565.788)	(2.393.325)	(2.556.847)	(2.404.153)
Per aksje	**Q3 2004**	**Q3 2003**	**2003**	**2002**	**2001**
Resultat per aksje	0,22	(0,17)	(0,29)	(0,68)	(1,18)
Resultat per aksje fullt utvannet	0,20	(0,12)	(0,18)	(0,50)	(0,98)
Utestående aksjer	30.855.458	9.429.237	8.383.336	3.747.815	2.035.022
Utestående aksjer fullt utvannet	33,879,934	12,754,940	12,948,957	5,163,834	2,442,297
Per aksje (etter spleis 5:1)					
Resultat per aksje	1,12	(0,83)	(1,43)	(3,41)	(5,91)
Resultat per aksje fullt utvannet	1,02	(0,61)	(0,92)	(2,48)	(4,92)
Utestående aksjer	6,171,092	1,885,847	1,676,667	749,563	407,004
Utestående aksjer fullt utvannet	6,775,987	2,550,988	2,589,791	1,032,767	488,459
Tall i NOK	**Q3 2004**	**Q3 2003**	**2003**	**2002**	**2001**
Sum omløpsmidler	579.121	449.980	106.384	185.912	792.590
Sum anleggsmidler	76.744	57.978	49.914	75.372	113.238
Sum eiendeler	655.865	507.958	156.298	261.284	905.828
Sum egenkapital	(697.091)	(9.636.516)	(10.480.194)	(9.676.998)	(8.354.963)
Sum gjeld	1.352.956	10.244.193	10.636.492	9.938.282	9.260.791
Sum gjeld og egenkapital	655.865	507.958	156.298	261.284	905.828

12.4 Aksjeemisjon og børsnotering

I forbindelse med børsnoteringen vil det bli foretatt en aksjeemisjon for tegning av minimum 5.714.286 og maksimum 6.000.000 aksjer til en tegningskurs NOK 3,50 per aksje. Bruttoemisjonsproveny fra aksjeemisjonen vil være mellom NOK 20 millioner og NOK 21 millioner.

Noteringen av DynaPels aksjer på Oslo Børs' SMB liste, som beskrevet i kapittel 2.12 og kapittel 10.3, er betinget av at aksjeemisjonen gjennomføres og skaffer til veie minimum NOK 20 millioner. Aksjeemisjonen er betinget av at minimum NOK 20 millioner tilføres til Selskapet ved emisjonen, se kapittel 2.2. I tillegg er aksjeemisjonen betinget av at vekslingskursen mellom USD og NOK gir en tegningskurs i NOK større enn pålydende på USD 0,50 pr aksje.

Selskapets aksjekapital etter gjennomføringen av aksjeemisjonen vil være minimum USD 6.065.828,50 bestående av 12.131.657 aksjer og maksimum USD 6.208.685,50 bestående av 12.417.371 aksjer.

Aksjeemisjonen er delvis garantert av et garantikonsortium, bestående av eksisterende og nye investorer, for å tegne og betale for aksjer for et beløp i størrelse NOK 20 millioner.

12.5 Brofinansiering

For å sikre videre drift i 4. kvartal 2004 inngikk DynaPel en avtale om et kortsiktig, sikret konvertibelt lån, i september 2004. Det initielle lånet var på NOK 4,2 millioner. I oktober og desember ble brofinansieringen utvidet slik at det totale lånet per 31. desember 2004 var på NOK 7 millioner. Renten på lånet er 20% p.a. Lånet pluss påløpt rente, pluss en risikopremie på 25% kan konverteres til aksjer i Selskapet til en konverteringskurs lik tegningskursen i aksjeemisjonen som beskrevet i kapittel 12.4. Lånet har sikkerhet i DynaPels eiendeler. Se kapittel 8.8, kapittel 8.9 og kapittel 10.7 for ytterligere detaljer.

12.6 Autorisert aksjekapital

DynaPel har per dato for dette Prospektet totalt 14.000.000 autoriserte aksjer. Etter aksjeemisjonen vil det maksimale antall utestående aksjer være 12.417.371. I tillegg har Selskapet utstedt opsjoner i henhold til Selskapets opsjonsprogram, som beskrevet i kapittel 10.6, og warrants som beskrevet i kapittel 10.7. Videre vil det konvertible lånet,, dersom det blir fullt ut konvertert, bli konvertert til ca 2.670.000 aksjer, se kapittel 12.5. Dette kan oppsummeres i følgende tabell:

	Aksjer
Utestående aksjer	6.417.371
Maksimalt antall aksjer i aksjeemisjonen	6.000.000
Utstedte opsjoner	88.800
Warrants til Dieter Kondek*	500.000
Warrants til Procon AS*	400.000
Konvertering av brofinansiering**	Ca. 2.670.000
2004 opsjonsprogram***	1.230.000
Total	**17.306.171**

* Warrants til Kondek og Procon AS er betinget av børsnotering, og konvertering til aksjer vil videre være betinget av en økning i autoriserte aksjer.

** Majoriteten av långivere i det kortsiktige, sikrede, konvertible lånet har, dersom de velger å utøve deres konverteringsrett i henhold til låneavtalen, akseptert å utsette konvertering og levering av nye aksjer til sine respektive VPS konti inntil DynaPel har avholdt nytt aksjonærmøte. Konverteringsretten er også betinget av at Selskapet har autorisasjon til å utstede tilstrekkelig antall nye aksjer (en av långiverne har spesifisert at aksjonærmøtet skal avholdes senest innen juli 2005). Antall aksjer som kan konverteres i henhold til brofinansieringen kan variere avhengig av påløpt rente.

***Opsjoner relatert til 2004 opsjonsprogrammet er ikke utstedt. Opsjonsavtalene vil inkludere betingelse om at Selskapet har autorisasjon til å utstede tilstrekkelig antall aksjer på tidspunkt for utøvelse.

Da Selskapet per dato for dette Prospektet ikke har tilstrekkelig antall autoriserte aksjer til å oppfylle aksjeutvidelsen i henhold til tabellen over, vil Selskapet på neste aksjonærmøte (planlagt holdt før utgangen av april 2005), fremme forslag om å øke antall autoriserte aksjer.

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Appendix 1 - Articles of Association

State of Delaware
Secretary of State
Division of Corporations
Delivered 01:28 PM 12/22/2004
FILED 01:30 PM 12/22/2004
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CERTIFICATE OF AMENDMENT

OF

CERTIFICATE OF INCORPORATION

OF

DYNAPEL SYSTEMS, INC.

DynaPel Systems, Inc., a corporation organized and existing under the State of Delaware, does hereby certify that:

1. The name of the corporation is DynaPel Systems, Inc. (the "Corporation")

2. The certificate of incorporation of the Corporation, as amended to date, is hereby amended by striking out Article IV thereof and substituting in lieu of said Article the following new Article:

"ARTICLE IV

Effective as of 5:00, p.m., Eastern time, on the date on which this Certificate of Amendment is filed, the total number of shares of stock which the Corporation is authorized to issue is 14 million (14,000,000) shares of Common Stock with the Par Value of fifty cents ($0.50) per share and a reverse 5-for-1 stock split of the Corporation's common stock shall become effective (the "Effective Time"), pursuant to which each five shares of common stock outstanding and held of record by each stockholder of the Corporation immediately prior to the Effective Time shall be reclassified and combined into one share of common stock (with fractional shares being rounded up to the nearest whole number) automatically and without any action by the holder thereof upon the Effective Time and shall represent one share of common stock from and after the Effective Time."

3. The Certificate of Amendment herein certified as been duly adopted in accordance with the provisions of Sections 222 and 242 of the General Corporation Law of the State of Delaware.

IN WITNESS WHEREOF, said Corporation has caused this certificate to be signed by its Chief Financial Officer, this 21st day of December, 2004.

By:
Name: Ralph Carballal
Title: Chief Financial Officer

NYB 1487915.2

BY-LAWS
of
INTERNATIONAL DIGITAL TECHNOLOGIES, Inc
(A Delaware Corporation)

ARTICLE I

Stockholders

Section 1. Place of Meetings
Meetings of stockholders shall be held at such place, either within or without the State of Delaware, as shall be designated from time to time by the Board of Directors.

Section 2. Annual Meetings
Annual meetings of stockholders shall be held on such date during the first half of each year and at such time as shall be designated from time to time by the Board the Directors. At each annual meeting the stockholders shall elect a Board of Directors by plurality vote and transact such other business as may be properly brought before the meeting.

Section 3. Special Meetings
Special meetings of the stockholders may be called by the Board of Directors.

Section 4. Notice of Meetings
Written notice of each meeting of the stockholders stating the place, date and hour of the meeting shall be given by or at the direction of the Board of Directors to each stockholder entitled to vote at the meeting at least ten, but not more than sixty, days prior to the meeting. Notice of any special meeting shall state in general terms the purpose or purposes for which the meeting is called.

Section 5. Quorum; Adjournments of Meetings
The holders of one third of the issued and outstanding shares of the capital stock of the corporation entitled to vote at a meeting, present in person or represented by proxy, shall constitute a quorum for the transaction of business at such meeting; but, if there be less than a quorum, the holders of a majority of the stock so present or represented may adjourn the meeting to another time or place, from time to time, until a quorum shall be present, whereupon the meeting may be held, as adjourned, without further notice, except as required by law, and any business may be transacted thereat which might have been transacted at the meeting as originally called.

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Section 6. Voting

At any meeting of the stockholders every registered owner of shares entitled to vote may vote in person or by proxy and, except as otherwise provided by statute, in the Certificate of Incorporation or these By-Laws, shall have one vote for each such share standing in his name on the books of the corporation. Except as otherwise required by statute, the Certificate of Incorporation or these By-Laws, all matters, other than the election of directors, brought before any meeting of the stockholders shall be decided by a vote of a majority in interest of the stockholders of the corporation present in person or by proxy at such meeting and voting thereon, a quorum being present.

Section 7. Inspectors of Election

The Board of Directors, or, if the Board shall not have made the appointment, the chairman presiding at any meeting of stockholders, shall have power to appoint one or more persons to act as inspectors of election at the meeting or any adjournment thereof, but no candidate for the office of director shall be appointed as an inspector at any meeting for the election of directors.

Section 8. Chairman of Meetings

The Chairman of the Board or, in his absence, the President shall preside at all meetings of the stockholders. In the absence of both the Chairman of the Board and the President, a majority of the members of the Board of Directors present in person at such meeting may appoint any other officer or director to act as Chairman of the meeting.

Section 9. Secretary of Meetings

The Secretary of the corporation shall act as secretary of all meetings of the stockholders. In the absence of the Secretary, the chairman of the meeting shall appoint any other person to act as secretary of the meeting.

Section 10. Stockholders' Action Without Meetings

Any action required or permitted to be taken at any meeting of the stockholders may be taken without a meeting, if a written consent thereto is signed by all the stockholders, and such written consent is filed with the minutes of proceedings of the stockholders.

ARTICLE II

Board of Directors

Section 1. Number of Directors

The Board of Directors shall consist of at least one (1) and not more than twenty (20) members; provided, however, that such number may from time to time be increased or decreased by the Board of Directors or by the stockholders.

Section 2. Vacancies

Whenever any vacancy shall occur in the Board of Directors by reason of death, resignation, removal, increase in the number of directors or otherwise, it may be filled by a majority of the directors then in the office, although less than a quorum, or by a sole remaining director, for the balance of the term, or, if the Board has not filled such vacancy, it may be filled by the stockholders.

Section 3 First Meeting

The first meeting of each newly elected Board of Directors, of which no notice shall be necessary, shall be held immediately following the annual meeting of stockholders or any adjournment thereof at the place the annual meeting of stockholders was held at which such directors were elected, or at such other place as a majority of the members of the newly elected Board who are then present shall determine, for the election or appointment of officers for the ensuing year and the transaction of such other business as may be brought before such meeting.

Section 4. Regular Meetings

Regular meetings of the Board of Directors, other than the first meeting, may be held without notice at such times and places as the Board of Directors may from time to time determine.

Section 5. Special Meetings

Special meetings of the Board of Directors may be called by order of the Chairman of the Board, the President or any two directors. Notice of the time and place of each special meeting shall be given by or at the direction of the person or persons calling the meeting by mailing the same at least three days before the meeting or by telephoning, telegraphing or delivering personally the same at least twenty-four hours before the meeting to each director. Except as otherwise specified in the notice thereof, or as required by statute, the Certificate of Incorporation or these By-Laws, any and all business may be transacted at any special meeting.

Section 6. Place of Conference Call Meeting

Any meeting at which one or more of the members of the Board of Directors or of a committee designated by the Board of Directors shall participate by means of conference telephone or similar communications equipment shall be deemed to have been held at the place designated for such meeting, provided that at least one member is at such place while participating in the meeting.

Section 7. Organization

Every meeting of the Board of Directors shall be presided over by the Chairman of the Board, or, in his absence, the President. In the absence of the Chairman of the Board and the President, a presiding officer shall be chosen by a majority of the directors present. The Secretary of the corporation shall act as secretary of the meeting, but, in his absence, the presiding officer may appoint any person to act as secretary of the meeting.

Section 8. Quorum; Vote

A majority of the directors then in office (but in no event less than one-third of the total number of directors) shall constitute a quorum, for the transaction of business, but less than a quorum may adjourn any meeting to another time or place from time to time until a quorum shall be present, whereupon the meeting may be held, as adjourned, without further notice. Except as otherwise required by statute, the Certificate of Incorporation or these By-Laws, all matters coming before any meeting of the Board of Directors shall be decided by the vote of a majority of the directors present at the meeting, a quorum being present.

Section 9. Removal of Directors

Any one or more of the directors shall be subject to removal with or without cause at any time by the stockholders.

Section 10. Directors' Action Without Meetings

Any action required or permitted to be taken at any meeting of the Board of Directors may be taken without a meeting, if a written consent thereto is signed by all members of the Board of Directors, and such written consent is filed with the minutes of proceedings of the Board of Directors.

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ARTICLE III

Officers

Section 1. General

The Board of Directors shall elect the officers of the corporation, which shall include a President, a Secretary and a Treasurer and such other or additional officers (including, without limitation, a Chairman of the Board, one or more Vice-Chairmen of the Board, Vice-Presidents, Assistant Vice-Presidents, Assistant Secretaries and Assistant Treasurers) as the Board of Directors may designate.

Section 2. Term of Office; Removal and Vacancy

Each officer shall hold his office until his successor is elected and qualified or until his earlier resignation or removal. Any officer or agent shall be subject to removal with or without cause at any time by the Board of Directors. Vacancies in any office, wheter occurring by death, resignation, removal or otherwise, may be filled by the Board of Directors.

Section 3. Powers and Duties

Each of the officers of the corporation shall, unless otherwise ordered by the Board of Directors, have such powers and duties as generally pertain to his respective office as well as such powers and duties as from time to time may be conferred upon him by the Board of Directors. Unless otherwise ordered by the Board of Directors after the adoption of these By-Laws, the Chairman of the Board, or, when the office of Chairman of the Board is vacant, the President, shall be the chief executive officer of the corporation.

Section 4. Power to Vote Stock

Unless otherwise ordered by the Board of Directors, the Chairman of the Board and the President each shall have full power and authority on behalf of the corporation to attend and to vote at any meeting of stockholders of any corporation in which this corporation may hold stock, and may exercise on behalf of this corporation any and all of the rights and powers incident to the ownership of such stock at any such meeting and shall have power and authority to execute and deliver proxies, waivers and consents on behalf of the corporation in connection with the exercise by the corporation of the rights and powers incident to the ownership of such stock. The Board of Directors, from time to time, may confer like powers upon any other person or persons.

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ARTICLE IV

Capital Stock

Section 1. Certificates of Stock
Certificates for stock of the corporation shall be in such form as the Board of Directors may from time to time prescribe and shall be signed by the Chairman of the Board or a Vice Chairman of the Board or the President or a Vice-President and by the Treasurer or an Assistant Treasurer or the Secretary or an Assistant Secretary. The Stock of the corporation may, should the Board of Directors so wish, be uncertificated and be registered in a paper less securities system.

Section 2. Transfer of Stock
Shares of capital stock of the corporation shall be transferable on the books of the corporation only by the holder of record thereof, in person or by duly authorized attorney, if certificated, upon surrender and cancellation of certificates for a like number of shares, with an assignment or power of transfer endorsed thereon or delivered therewith, duly executed, and with such proof of the authenticity of the signature and of authority to transfer, and of payment of transfer taxes, as the corporation or its agents may require.

Within a reasonable time after the issuance or transfer of uncertificated stock, the corporation shall send to the registered owner thereof a written notice containing the information required to be set forth or stated on certificates pursuant to Section 151, 156, 202(a) or 218(a) of the Delaware General Corporation Law or a statement that the corporation will furnish without charge to each stockholder who so requests the powers, designations, preferences and relative participating, optional or other special rights of each class of stock or series thereof and the qualifications, limitations or restrictions of such preferences and/or rights.

Section 3. Ownership of Stock
The corporation shall be entitled to treat the holder of record of any share or shares of stock as the owner thereof in fact and shall not be bound to recognize any equitable or other claim to or interest in such shares on the part of any other person, wheter or not it shall have express or other notice thereof, except as otherwise expressly provided by law.

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ARTICLE V

Miscellaneous

Section 1. Corporate Seal
The seal of the corporation shall be circular in form and shall contain the name of the corporation and the year and State of incorporation.

Section 2. Fiscal Year
The Board of Directors shall have power to fix, and from time to time change, the fiscal year of the corporation.

ARTICLE VI

Amendment

The Board of Directors shall have the power to make, alter or repeal the By-Laws of the corporation subject to the power of the stockholders to alter or repeal the By-Laws made or altered by the Board of Directors.

ARTICLE VII

Indemnification

The corporation may indemnify any director, officer, employee or agent of the corporation to the full extent permitted by law.

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Appendix 2 - Q3 2004 Report & Audited half year 2004

DynaPel Systems, Inc.
2235 First Street, Suite 215
Fort Myers, Florida 33901, USA

Oslo/Fort Myers, November 29, 2004

HIGHLIGHTS

- Sales of DynaPel's products continue to grow, with an increase of 36 % in the third quarter compared to the second quarter of 2004 and an increase of 27% compared to the third quarter of 2003.
- The process of being listed on the OSE has been further delayed, possible listing date is now January 2005.
- A secured convertible short term bridge loan agreement with a NOK 7 million limit was completed in October, securing operations until possible listing in January 2005.
- At the end of September Pieper GmbH, a German security company, specialising in European airport security, confirmed their decision to sell DynaPel products under their own brand. An initial order of 50 SteadyEye units was received in the beginning of October.

SUMMARY

Third quarter sales amounted to US$ 186.706, compared to second quarter sales of US$ 135.381, an increase of 38 %. The Company is showing an additional order backlog of US$ 140.883 at the beginning of October. For the nine months ending September 2004, the total sales, excluding royalties, were US$ 352.656 compared to US$ 329.583 for the same period in 2003.

The **Security Market** sales represent 46% of the total turnover, with the US as the number one market, representing 90% of the Company's turnover within this segment. The European market represents 10%. There are no systematic customer approaches for this segment outside these two markets due to lack of sales personel.

The **Broadcast Market** sales represented 28% of total sales, primarily consisting of sales to the Company's OEM partner Kramer Electronics in Israel.

The **Video Editing** sales represented the remaining turnover of 26%, mainly due to invoicing of 2004 license fee to Macro Systems in the 3rd quarter.

The average gross margin in the third quarter was 60%. The operating result was negatively influenced by non-recurring costs primarily related to the Due Diligence process associated with the listing application.

DynaPel Systems, Inc.
2235 First Street, Suite 215
Fort Myers, Florida 33901, USA

GENERAL INFORMATION

Markets and products
The potential market segments for DynaPel's technology and derived products are believed to be several. However, due to capacity restrictions, both financially and organizationally, the main focus today is, within security and broadcast, with a clear priority on the security market. Due to the same restrictions described above, geographically, only the US and to a certain extent the European markets are being addressed at this time.

Security
The US market for security products is booming, and the growth and market-potential for DynaPel's products are significant both short and long term. Within the security market, three stand alone products (SteadyEye, CloseView and NightView) are now being offered. All products are simple to install, they plug in-between any standard camera and downstream devices such as recorders, multiplexers or transmission systems. All three products are suitable both for new installations and the retro-fit market.

Broadcast
SteadyEye is available to the broadcast video market and improves the quality of live-feed broadcast video from cameras shooting on-location. DynaPel's first OEM partner, Kramer Electronics, is marketing the Kramer broadcast solution to their currently more than 1.000 broadcast industry customers worldwide, and has integrated SteadyEye into a 19" rack solution.

Sales and marketing
Due to the size of the market, the great number of decision makers to approach, as well as lack of capacity within its own organization, DynaPel has chosen to sell its own branded products through already established and experienced sales organisations. DynaPel is also selling products and technical solutions under customer's brands and as part of other customer's products (OEM agreements). At present, the number one priority is the US security market. In the US market, we are currently reaching the end users and decision makers through the Pelco dealer network. Pelco is the leading security camera manufacturer in the US, and has an excellent reputation. Pelco has appoximately 10.000 system integrators in their customer base, with their main focus on the commercial market. The Governmental- and military market is more systematically approached through our OEM partners and their dedicated specialized integrators.

SHAREHOLDER MATTERS

Due, primarily to the uncertainty created by the insolvency of the German operation, the planned listing onto the OSE in the first half of 2004 was delayed. The process of being listed is ongoing, and the listing application has been submitted to OSE on November 24, 2004, with an IPO in January 2005 and possible listing ultimo January 2005.

A Special Shareholder Meeting was held on November 18, 2004 in Oslo, and all issues were resolved in accordance with the notice dated November 8, 2004:

DynaPel Systems, Inc.
2235 First Street, Suite 215
Fort Myers, Florida 33901, USA

1. Approval of the listing of DynaPel shares on the Oslo Stock Exchange and a share issue (IPO) in connection with the listing of a minimum of 20,000,000 and a maximum of 30,000,000 of Dynapel's currently authorized but unissued stock.
2. Approval of the assembly of an underwriting consortium for the purpose of guaranteeing NOK 20,000,000 million of the IPO.
3. Approval of a 1 for 5 reverse stock split.
4. Approval of an amendment to the 2004 Stock Option Plan.
5. Two new board members were elected by the general meeting, Mrs. Live Haukvik Aker and Mr. Helge Nielsen.

Mr. Dieter Kondek (CEO) leaves the Board, and DynaPel's new Board of Directors are: Helge Nielsen (Chairman), Live Haukvik Aker, Ivar Formo and Ralph Carballal.

1 for 5 Reverse Stock Split
As of November 25, 2004 the DynaPel share will trade on the basis of par value at USD 0,50 as a result of the 1 for 5 reverse split approved by the Special Shareholder Meeting on November 18, 2004. 5 existing shares in DynaPel Systems Inc. will be 1 new share, rounded upwards. Last day of trading with the existing share, par value USD 0,10, will be November 24, 2004. The total number of shares will be reduced from 31,586,856 to 6.317.371, each with a par value of USD 0,50. The new par value and resulting number of shares will be reflected in VPS as of November 30, 2004.

Short Term Bridge loan
Due to the delay of the planned IPO, the Company experienced a severe liquidity constraint during the summer. In September 2004, the Company entered into a secured short-term bridge loan arrangement, secured by the assets of the Company, under which the Company could borrow a maximum of NOK 7 million, at an interest of 20 % p.a. As of today, NOK 5,6 million has been drawn under the loan agreement.

The loan falls due on February 28, 2005. According to the arrangement, the lender reserved the right to convert the outstanding balance, plus accrued interest, plus a risk factor premium of 25 % into common stock of the Company at a share price equal to the price at the upcoming public offering.

FUTURE OUTLOOK

The agreements with the highly reputable Pelco sales organization, covering the whole of North America, as well as OEM agreements with important market players in both security and the broadcast market, combined with the positive market reaction to the products, lead us to believe that the positive trend experienced during the last two quarters will continue. One should however not underestimate the time it will take to educate a conservative market to specify the Company's products for retrofit and or new installation. With the capital to be raised in the forthcoming IPO, we will prioritize to increase the Company's capacity in sales, marketing and engineering support. This should lead to acceleration in sales over time.

DynaPel Q3 2004 Interim Report

DynaPel Systems, Inc.
2235 First Street, Suite 215
Fort Myers, Florida 33901, USA

ABOUT DYNAPEL

DynaPel Systems, Inc. develops intelligent video products for the surveillance and broadcast industries, which increase the effectiveness of security and broadcast professionals.

Founded in 1992 and headquartered in Fort Myers, Florida, the company's think tank is based in Germany and consists of a technical team of engineers and scientists that are experts in digital video, motion estimation and MPEG-4 video compression. The company has sales offices in New York, Los Angeles, Munich and Oslo, and markets its products through a network of representatives, distributors, system integrators, and OEM's.

DynaPel shares are traded on the Norwegian OTC stock market with the symbol "DYNA".

DynaPel Systems, Inc. can be seen at: www.dynapel.com.

For further information please contact:

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DynaPel Q3 2004 Interim Report

DynaPel Systems, Inc.
2235 First Street, Suite 215
Fort Myers, Florida 33901, USA

Consolidated statement of operations (USD)	July- September		January-September		
	2004	2003	2004	2003	2003
Royalties	0	291.667	291.667	875.000	1.166.667
Sales	186.706	145.141	352.656	329.583	423.369
Total sales and royalties	**186.706**	**436.808**	**644.323**	**1.204.583**	**1.590.036**
Cost of sales	75.576	42.642	156.712	83.397	93.196
Operating expenses	644.382	875.525	1.842.078	2.411.477	3.494.499
Interest expense	5.000	123.093	57.472	275.614	398.793
Total operating expenses	**724.958**	**1.041.260**	**2.056.262**	**2.770.488**	**3.986.488**
Loss from operations	**-538.252**	**-604.452**	**-1.411.939**	**-1.565.905**	**-3.563.119**
Other income/expences	-2.528	-2.604	8.352.871	117	-13.014
Provision for Income Taxes	-22.000	0	-58.000	0	0
Comprehensive loss	**-513.780**	**-607.056**	**6.882.932**	**-1.565.788**	**-3.576.133**
Per share data:					
Basic and diluted income per share	-0,02	-0,06	0,22	-0,17	-0,43
Weighted average shares outstanding	31.586.856	10.171.452	30.855.458	9.429.237	8.383.336
Segment information:					
Security	87.502	*47%*	240.199	*68%*	
Broadcast	50.700	*27%*	50.700	*14%*	
Other	48.504	*26%*	61.757	*18%*	
Total sales	186.706	*100%*	352.656	*100%*	

Group equity (USD)	January-September		
	2004	2003	2003
Equity at January 1st.	-10.480.194	-9.676.998	-9.676.998
Sale of stock / share issues	1.806.838	747.297	747.297
Conversion of bridge loan	1.093.333	858.973	858.973
Net Income (loss)	6.882.932	-1.565.788	-2.393.325
Unrealized currency gain	0	117	-16.141
Equity at September 30 / December 31	-697.091	-9.636.516	-10.480.194

DynaPel Q3 2004 Interim Report

DynaPel Systems, Inc.
2235 First Street, Suite 215
Fort Myers, Florida 33901, USA

Consolidated balance sheets (USD)	September 30th		December
	2004	2003	2003
Cash and cash equivalents	66.443	338.756	50.920
Trade accounts receivables	124.850	64.189	16.455
Other current assets	387.828	47.035	39.009
Total current assets	579.121	449.980	106.384
Other assets	76.744	57.978	49.914
TOTAL ASSETS	**655.865**	**507.958**	**156.298**
Accounts payable	594.956	160.178	367.416
Accrued expenses and other current liabilities	758.000	1.371.794	1.840.506
TOTAL CURRENT LIABILITIES	1.352.956	1.531.972	2.207.922
Convertible note incl. interest	0	3.492.657	3.550.730
Bridge loans	0	1.043.671	1.093.333
Deferred revenues and royalties	0	4.076.174	3.784.507
TOTAL LIABILITIES	1.352.956	10.244.193	10.636.492
Common stock	3.159.199	1.022.629	1.022.629
Additional paid-in equity	20.680.006	19.915.892	19.915.892
Accumulated deficit and comprehensive loss	-24.535.783	-30.575.037	-31.418.715
TOTAL SHAREHOLDERS DEFICIT	-697.091	-9.636.516	-10.480.194
TOTAL LIABILITIES AND EQUITY	**655.865**	**507.958**	**156.298**

Consolidated statement of cash flow (USD)	January-September		
	2004	2003	2003
Net loss	6.882.932	-1.565.788	-2.393.325
Adjustments to reconcile net loss to net cash	-8.686.600	292.532	855.961
Net cash used in operating activities	-1.803.668	-1.273.256	-1.537.364
Cash flow from investing activities	-96.341	-11.265	-16.981
Cash flow from financing activities	1.915.532	1.499.262	1.499.262
Net Increase (decrease) in cash	15.523	214.741	-73.095
Cash and cash equivalents, beginning	50.920	124.015	124.015
Cash and cash equivalents, end	66.443	338.756	50.920

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED FINANCIAL STATEMENTS
AND
AUDITORS' REPORT

SIX AND THREE MONTHS ENDED JUNE 30, 2004 AND

THE YEAR ENDED DECEMBER 31, 2003

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INDEPENDENT AUDITORS' REPORT

The Board of Directors
of DynaPel Systems, Inc.

We have audited the accompanying consolidated balance sheets of DynaPel Systems, Inc. and Subsidiary as of June 30, 2004 and December 31, 2003, and the related statements of operations and comprehensive income (loss) for the six months and three months ended June 30, 2004 and the year ended December 31, 2003, and the statements of shareholders' deficits and cash flows for the six months ended June 30, 2004 and the year ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of DynaPel Systems, Inc. and Subsidiary as of June 30, 2004 and December 31, 2003, the results of their operations for the six months and three months ended June 30, 2004 and the year ended December 31, 2003 and their cash flows for the six months ended June 30, 2004 and the year ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the financial statements, the Company has suffered recurring losses from operations and has a net capital deficiency, which raises substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Israeloff, Trattner & Co., P.C.

Garden City, New York
August 27, 2004

ALLIOTT GROUP

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

JUNE 30, 2004 AND DECEMBER 31, 2003

	June 30, 2004	December 31, 2003
ASSETS		
Current Assets:		
Cash and cash equivalents (Note 1)	$ 101,171	$ 50,920
Trade accounts receivable (Note 1)	142,380	16,455
Inventory (Note 1)	113,765	-
Prepaid expenses	8,400	397
Other current assets	10,000	38,612
Total Current Assets	375,716	106,384
Property and Equipment, Net (Notes 1 and 2)	78,380	44,114
Other Assets	9,000	5,800
TOTAL ASSETS	$ 463,096	$ 156,298
LIABILITIES AND SHAREHOLDERS' DEFICIT		
Current Liabilities:		
Accounts payable	$ 189,220	$ 367,416
Accrued expenses and other current liabilities (Note 9)	400,000	1,840,506
Income taxes payable (Note 4)	80,000	-
Total Current Liabilities	669,220	2,207,922
Convertible note payable and accrued interest thereon, subsequently converted to equity (Note 5)	-	3,550,730
Bridge loans subsequently converted to equity (Note 6)	-	1,093,333
Deferred revenues and royalties (Notes 1 and 3)	-	3,784,507
	669,220	10,636,492
Shareholders' Deficit:		
Common stock, $0.10 par value, 70,000,000 shares authorized, 31,586,856 and 10,226,286 shares issued and outstanding at June 30, 2004 and December 31, 2003, respectively.	3,159,199	1,022,629
Additional paid-in capital	20,646,680	19,915,892
Accumulated deficit	(23,961,918)	(31,363,630)
Accumulated other comprehensive loss	(50,085)	(55,085)
Total Shareholders' Deficit	(206,124)	(10,480,194)
TOTAL LIABILITIES AND SHAREHOLDERS' DEFICIT	$ 463,096	$ 156,298

See the accompanying notes to the consolidated financial statements.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

FOR THE SIX AND THREE MONTHS ENDED JUNE 30, 2004

AND FOR THE YEAR ENDED DECEMBER 31, 2003

	Six Months Ended June 30, 2004	Three Months Ended June 30, 2004	Year Ended December 31, 2003
Royalties	$ 291,667	$ -	$ 1,166,667
Sales	165,950	135,381	423,369
Total sales and royalties	457,617	135,381	1,590,036
Operating Expenses:			
Cost of sales	81,136	66,786	93,196
Research and development	396,000	255,000	1,845,827
Marketing, general and administrative	801,696	412,806	1,648,672
Interest expense	52,472	-	398,793
Total operating expenses	1,331,304	734,592	3,986,488
Loss from operations	(873,687)	(599,211)	(2,396,452)
Other Income (Expense):			
Gain on extinguishment of debt	3,546,048	-	-
Gain on recognition of deferred royalties upon termination of agreement	3,492,840	3,492,840	-
Gain on settlement of liabilities of bankrupt subsidiary	1,317,879	1,317,879	-
Other income	-	-	4,998
Foreign currency exchange losses	(1,368)	(2,368)	(1,871)
Total other income	8,355,399	4,808,351	3,127
Pre-tax income (loss)	7,481,712	4,209,140	(2,393,325)
Provision for Income Taxes	80,000	10,000	-
Net Income (Loss)	7,401,712	4,199,140	(2,393,325)
Other Comprehensive Income (Expense):			
Foreign currency translation adjustment	5,000	2,000	(16,141)
Comprehensive Income (Loss)	$ 7,406,712	$ 4,201,140	$ (2,409,466)
Per Share Data:			
Basic and diluted income (loss) per share	$ 0.24	$ 0.13	$ (0.29)
Basic and diluted weighted average common shares outstanding	30,483,698	31,591,985	8,383,336

See the accompanying notes to the consolidated financial statements.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED JUNE 30, 2004 AND THE YEAR ENDED DECEMBER 31, 2003

	Six Months Ended June 30, 2004	Year Ended December 31, 2003
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	$ 7,401,712	$ (2,393,325)
Adjustments to reconcile net income (loss) to net cash used by operating activities:		
Interest accrued on notes and loans payable	52,472	338,683
Deferred royalties and revenues	(3,784,507)	(1,166,667)
Gain on extinguishment of debt	(3,546,048)	-
Depreciation	23,000	42,439
Abandonment of fixed assets	44,114	-
Foreign currency exchange losses	1,368	1,871
Non-cash stock-based compensation	101,339	241,282
Change In assets and liabilities:		
Inventory	(113,765)	-
Trade accounts receivable	(125,925)	6,081
Prepaid expenses	(8,003)	8,813
Other current assets	28,612	(8,461)
Other assets	(3,200)	-
Accounts payable	(178,196)	49,648
Accrued expenses and other current liabilities	(1,440,506)	1,342,272
Income taxes payable	80,000	-
Net cash used by operating activities	(1,467,533)	(1,537,364)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(101,380)	(16,981)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment of convertible note payable	(57,154)	-
Proceeds from short-term bridge loan	-	993,247
Proceeds from common stock issuance	1,672,686	506,015
Net cash provided by financing activities	1,615,532	1,499,262
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	3,632	(18,012)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	50,251	(73,095)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	50,920	124,015
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 101,171	$ 50,920

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Organization

DynaPel Systems, Inc. ("DynaPel US") was incorporated in the State of Delaware in 1992. DynaPel's corporate offices are located in New York, New York, Fort Myers, Florida and Munich, Germany. In 1994, DynaPel formed a subsidiary, DynaPel Laboratories GmbH ("DynaPel Germany"), located in Ismaning, Germany. In January 2004, management of this subsidiary declared it to be insolvent.

As a result of the insolvency of Dynapel Germany, the Company formed a new subsidiary in March 2004. The new subsidiary, Holon Technology GmbH ("Holon") is located in Munich, Germany. Holon is providing engineering and production services to its parent company, Dynapel US.

DynaPel US develops and markets intelligent video software tools and appliances for the security and broadcast industries based on patent-protected software technology and in-house developed video algorithm and compression technologies. DynaPel has an existing suite of products that offer function and cost benefits to owners of existing and/or planned video surveillance systems employed in a wide range of applications.

DynaPel's products are sold to commercial as well as military and governmental users. Sales are either pre-paid or made to highly credit-rated customers.

Going Concern

The Company's operations involve a number of risks and uncertainties. Factors that could affect the Company's future operating results and cause actual results to vary materially from expectations include, but are not limited to, rapid technology change, uncertainty of market acceptance of the Company's products and services, competition from substitute products and larger companies, protection of proprietary technology, the ability to generate sufficient capital to fund operations, strategic relationships and dependence on key individuals.

As reported in the accompanying financial statements, the Company incurred losses from operations of $873,687 and $2,396,452 for the six months ended June 30, 2004 and the year ended December 31, 2003, respectively. At June 30, 2004, the Company has a shareholders' deficit of $206,124. The Company raised approximately $1,670,000 of equity capital during the six months ended June 30, 2004. Management of the Company plans to raise additional equity capital through the issuance of shares during the third and fourth quarter of 2004. The ability of the Company to continue as a going concern is dependent upon its raising sufficient equity capital to meet its short term needs and its future ability to generate revenues and profits from the sale of its products. There is no assurance that the Company will be successful in attaining these objectives. The accompanying financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Principles of Consolidation

The consolidated financial statements include the financial statements of DynaPel US and, for the applicable period, its wholly-owned subsidiaries, DynaPel Germany and/or Holon. All significant intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

For financial statement purposes, the Company considers all highly liquid debt instruments with a maturity of three months or less when purchased to be cash equivalents. The Company maintains its cash in bank deposit accounts in the United States of America and overseas which, at times, may exceed applicable insurance limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

Accounts Receivable

Accounts receivable have been adjusted for all known uncollectible accounts and are stated at the amount management expects to collect from outstanding balances. Based on management's evaluation of collectibility, an allowance for doubtful accounts is not required.

Inventory

Inventory is valued at the lower of cost (first-in, first-out) or market.

Property and Equipment

Property and equipment are stated at cost, less accumulated depreciation. Depreciation is provided using straight-line and accelerated methods over the estimated useful lives of the assets. The estimated useful lives are as follows:

Computer equipment and software	3 years
Furniture, fixtures and other	3-5 years

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deferred Revenue

Deferred revenue consisted primarily of an up-front royalty received November 5, 1999, upon execution of a license agreement which was effective January 1, 2000. Under terms of the license agreement, minimum future royalties were to be earned for the six-year period which began on January 1, 2000 through December 31, 2005. As a result, the Company deferred the up-front royalty and was recognizing the corresponding revenue over the term of the minimum future royalties. This agreement was terminated effective April 2004. (See Note 3).

Cost of Sales

Cost of sales is composed of costs related to the packaging of software and hardware for sale and depreciation of equipment used in production.

Research and Development Expenses and Capitalized Software Development Costs

Software development costs consist principally of compensation and benefits paid to the Company's employees. All software development costs not qualifying for capitalization are expensed as research and development costs when incurred.

The Company's policy is to expense all software development costs prior to establishing technological feasibility. Because the Company's products have reached this state of development almost concurrently with general release, the Company has not capitalized any software development costs.

Income Taxes

The Company accounts for income taxes using the asset and liability method, as prescribed by Statement of Financial Accounting Standards No. 109 "Accounting for Income Taxes". Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Statutory taxes not based on income are included in general and administrative expenses.

For interim periods, income tax expense is provided using the estimated effective income tax rate expected to apply for the entire taxable year.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Translation of Foreign Currencies and Foreign Currency Transactions

Financial statements of the Company's foreign subsidiary are translated into U.S. dollars at current exchange rates, except for costs and expenses, which are translated at average exchange rates during each reporting period. Net exchange gains or losses resulting from the translation of assets and liabilities are accumulated as "accumulated other comprehensive income (loss)" and are reported as a separate component of shareholders' deficit. Transactions in currencies other than the U.S. dollar are recorded in U.S. dollars at exchange rates prevailing at the transaction dates. Exchange gains and losses are included in the Company's results of operations.

Stock Option Plans

The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations, in accounting for its fixed plan stock options issued to employees and directors. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. The Company applies Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, for its stock options to non-employees and non-directors. SFAS No. 123 established accounting and disclosure requirements using a fair value-based method of accounting for stock-based compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic value-based method of accounting described above for stock options issued to employees and directors, and has adopted the disclosure requirements of SFAS No. 123.

Accounting for the Impairment or Disposal of Long-Lived Assets

The Company follows the provisions of Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This Statement requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell. The provisions of this Statement did not have a material impact on the Company's financial position, results of activities or liquidity for the six months ended June 30, 2004 and year ended December 31, 2003.

Reverse Stock Split

All share references have been adjusted to reflect a one for ten reverse stock split effected in April 2004.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income (Loss) Per Common Share

Basic and diluted income (loss) per common share is computed by dividing net income (loss) by the weighted average number of common shares outstanding after giving effect to the reverse stock split. Outstanding common stock options to purchase 528,200 and 581,450 common shares at June 30, 2004 and December 31, 2003, respectively, are anti-dilutive and are accordingly excluded from the calculation.

2. PROPERTY AND EQUIPMENT

Property and equipment consist of the following as of June 30, 2004 and December 31, 2003:

	2004	2003
Computer software	$ 5,000	$ 31,747
Furniture, fixtures and computer equipment	96,380	700,312
	101,380	732,059
Less: Accumulated depreciation	23,000	687,945
	$ 78,380	$ 44,114

As a result of the insolvency of Dynapel Germany, property and equipment with a net book value of $44,114 at December 31, 2003 were removed from the books of the Company. (See Note 9).

Depreciation expense for the six months ended June 30, 2004 and the year ended December 31, 2003 were $23,000 and $42,439, respectively.

3. COOPERATION AND BROADCAST LICENSE AGREEMENTS

Cooperation Agreement

Effective May 29, 1995, in conjunction with a reorganization of the Company, the Company entered into a Cooperation Agreement (the "Cooperation Agreement") with a shareholder (the "Cooperation Shareholder"). Under the terms of the Cooperation Agreement, the Cooperation Shareholder agreed to pay certain outstanding obligations of the Company and to fund the Company's operations. In return for funding the Company's operations, the Cooperation Shareholder received the right to license the Company's technology. All funds received by the Company from the Cooperation Shareholder as a result of the Cooperation Agreement were accounted for as deferred royalties.

Effective October 31, 1999, funding of the Company's operations under the Cooperation Agreement ceased and the Cooperation Agreement was terminated. The Cooperation Shareholder entered into a license agreement with the Company on November 5, 1999.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

3. COOPERATION AND BROADCAST LICENSE AGREEMENTS (CONTINUED)

Broadcast License

On November 5, 1999, the Company entered into an agreement (the "Broadcast License") with the Cooperation Shareholder to license the Company's Broadcast Technology. The Broadcast License was effective January 1, 2000 and was to continue through December 31, 2005. The Broadcast License was non-exclusive and covered the continents of Europe and Africa (the "Broadcast Territory"). Under the terms of the Broadcast License, the Cooperation Shareholder could: 1) incorporate the Broadcast Technology into other products; 2) manufacture, distribute, sell, use, promote or otherwise produce products using the Broadcast Technology available in the Broadcast Territory; 3) use the Broadcast Technology to encode broadcast transmissions of moving images for viewing in the Broadcast Territory; and, 4) grant sublicenses to its affiliates and third parties.

The Company received an advance of $5,800,000 upon execution of the Broadcast License, which was recorded as Deferred Royalties. In addition, the Company was to receive a percentage of the net receipts of any sublicenses granted to third parties and a percentage of the revenues from the sales of products developed using any part of the Broadcast Technology (the "Earned Royalties"). Earned Royalties, subject to a $200,000 annual minimum, were to be offset against Deferred Royalties. The deferred revenue of $5,800,000 was being recognized ratably over the term of the Broadcast License.

During 2000, the Broadcast License was amended. The amendment stated that if the Cooperation Shareholder did not use the licensed rights, and the market price of the Company's stock exceeded $10 per share, the Cooperation Shareholder and/or the Company had the right to terminate the Broadcast License. Upon termination of the Broadcast License, the Company would pay the Cooperation Shareholder the outstanding balance of the Deferred Royalties in the form of Company stock, not to exceed 500,000 shares.

In April 2004, the Broadcast License was terminated. The Termination Agreement had the effect of terminating any and all ongoing agreements or amendments to agreements, including the Broadcast License, which they had entered into over the course of their relationship. Further, as a result of this agreement, neither the Cooperation Shareholder nor the Company (or any subsidiary of the Company) will be entitled to any additional royalty or revenue from the other party, whether currently due or accrued, notwithstanding anything to the contrary in any agreements between the two parties, as of December 31, 2003. In connection with the License Agreement, the Company recognized all outstanding deferred royalties and deferred revenue in the second quarter of 2004 resulting in income of $3,492,840, which is reported as other income in the accompanying consolidated statement of operations and comprehensive income.

4. INCOME TAXES

As of June 30, 2004 and December 31, 2003, the Company had approximately $10,241,000 and $14,150,000 of net operating loss carryforwards, respectively, which expire at various dates beginning in tax year 2008 through 2023. The availability to offset income taxes in future years may be restricted if the Company undergoes an ownership change, which may occur as a result of future sales of any stock and other events.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

4. INCOME TAXES (CONTINUED)

The tax effect of temporary differences that give rise to the Company's deferred tax assets and liabilities are as follows as of June 30, 2004 and December 31, 2003:

	June 30, 2004	December 30, 2003
Net operating loss carryforwards	$ 4,096,400	$ 5,660,000
Less: Valuation allowance	4,096,400	5,660,000
Net deferred income tax asset	$ -	$ -

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. The ultimate realization of deferred tax assets depends on the generation of future taxable income and tax planning in making these assessments.

The net change in the valuation allowance for deferred income taxes for the six months ended June 30, 2004 and the year ended December 31, 2003 was $1,563,600 and $2,796,000, respectively.

5. CONVERTIBLE NOTE PAYABLE

In September 2000, the Company entered into a short-term financing arrangement ("Loan Agreement") with Technoinvest, a German entity, under which the Company could borrow a maximum of $2,500,000. At December 31, 2003, $2,500,000 was outstanding. The outstanding balance accrued interest at 7% per annum. Accrued interest outstanding at December 31, 2003 was $1,050,730.

According to the original Loan Agreement, the Company could repay the outstanding principal and interest at any time without penalty, but no later than September 11, 2001. Additionally, the lender reserved the right to convert the outstanding balance of the loan into common stock if the Company undertook an offering of securities during the term of the loan.

In September 2001, the Company began negotiations with the lender to amend the repayment provisions of the original Loan Agreement. An agreement was reached in December 2001, whereby the lender waived repayment of the outstanding balance of the loan subject to the improvement of the financial condition of the Company. At such time as the Company could repay the loan without endangering its financial existence, the outstanding balance of the loan would become payable in full including interest earned up to the date of repayment. This agreement also provided for the lender, at its discretion, to convert the outstanding balance of the loan including interest into common stock at a conversion price of 14 Norwegian Crowns (NOK) per share. As a result of these provisions the Company classified this loan and the accrued interest thereon as non-current liabilities.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

5. CONVERTIBLE NOTE PAYABLE (CONTINUED)

In March 2004, the Company modified the terms of its existing agreement with Technoinvest whereby the outstanding convertible note payable in the amount of $2,500,000 and all current and accrued interest totaling $3,603,202, was converted into 400,000 common shares of the Company, with a current value of approximately $57,000, and 400,000 NOK ($57,154). The Company recognized a gain of $3,546,048 on this troubled debt restructuring.

6. SHORT-TERM BRIDGE LOANS

In August 2002, the Company entered into a short-term bridge loan arrangement under which the Company could borrow a maximum of $1,100,000. A December 31, 2002, principal of $795,384 was borrowed and outstanding. The outstanding balance accrued interest at 20% per annum. At December 31, 2002, accrued interest was $57,282.

According to the original arrangement, the Company could have repaid the outstanding principal and interest at any time without penalty, but no later than January 15, 2003. Additionally, the lender reserved the right to convert the outstanding balance of the loan and accrued interest into common stock, at a fixed rate of NOK 0.20 per share, if the Company undertook an offering of securities during the term of the loan. In August 2003, the short-term bridge loan and the related accrued interest, totaling approximately $859,000, were fully converted, in accordance with its existing terms, into 3,173,003 shares of common stock of the Company.

In June 2003, the Company entered into a secured short-term bridge loan arrangement, secured by the assets of the Company, under which the Company could borrow a maximum of $1,000,857. At December 31, 2003, $993,247 was borrowed and outstanding. The outstanding balance accrued interest at 20% per annum and was due to mature in March 2004. At December 31, 2003, interest accrued was $100,086.

According to the original arrangement, the lender reserved the right to convert the outstanding balance plus accrued interest into common stock of the Company at a share price of NOK 0.30. Also, the arrangement had anti-dilution provisions to protect the lender if the Company subsequently sold shares at a price below the conversion price.

In January 2004, the outstanding secured short-term bridge loan was converted into 7,825,701 shares of common stock of the Company, pursuant to its existing terms.

7. SHAREHOLDERS' DEFICIT

Private Placement/Exchange

In January 2003, the Company completed a private placement of common shares. This offering was transacted in the form of a Rights Offering to all shareholders at a subscription price of NOK 0.20. A total of 1,763,177 shares were issued for proceeds of $506,015.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

7. SHAREHOLDERS' DEFICIT (CONTINUED)

Also in January 2003, the Company issued 219,630 shares for compensation of $63,032 in lieu of cash compensation for certain consultants and in lieu of salary for certain employees, and also reached an agreement with a former officer, whereby 109,667 common shares of the Company, with a current value of approximately $47,000, were issued in settlement of certain consulting services.

In August 2003, the Company issued 3,173,003 shares of common stock upon conversion of its original short-term bridge loan. (See Note 6).

In January 2004, in conjunction with the conversion of the short-term bridge loan, the Company raised 10,140,000 NOK ($1,357,000) with the sale of 10,140,000 common shares of the Company in a private placement to existing investors and certain new investors. Of the 10,140,000 common shares issued, 250,000 and 550,000 of the common shares were issued to employees and management and directors and officers, respectively.

In February 2004, a Special Meeting of Shareholders was held in Oslo, Norway. At that meeting, the following points on the agenda were approved: (1) Approval of a Rights Issue and Listing on the Oslo Stock Exchange; (2) approval of the formation of an Underwriting Consortium in conjunction with the Listing described previously; (3) Approval of the 2004 Stock Option Plan; (4) Approval of an increase in the authorized common shares of the Company from 150 million to 700 million; and (5) Approval of a 1 for 10 reverse common stock split and an increase of the par value of common stock from $0.01 to $0.10. The 1 for 10 reverse common stock split was effected April 1, 2004. All changes to the Company's authorized capital has been given retroactive effect in the accompanying financial statements.

In March 2004, the Company did a follow-on equity placement to all existing shareholders (a Rights Offering) in the amount of 3,000,000 NOK ($428,000) before transaction expenses. The result of this transaction was the placement of an additional 3,000,000 common shares of the Company. After completing this offering, the Company had approximately 31,190,000 shares outstanding.

In May 2004, the number of authorized common shares was reduced from 700 million to 70 million.

Stock Option Plans

Effective January 27, 1999, the Board of Directors adopted the DynaPel Systems, Inc. 1998 Stock Option Plan (the "1998 Plan") and reserved 275,000 shares of common stock for issuance under the 1998 Plan. Aggregate grants to non-employee directors under the 1998 Plan cannot exceed 25,000 shares.

Effective March 23, 2000, the Board of Directors adopted the DynaPel Systems, Inc. 2000 Stock Option Plan (the "2000 Plan") and reserved 250,000 shares of common stock for issuance under the 2000 Plan. Aggregate grants to non-employee directors under the 2000 Plan cannot exceed 25,000 shares.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

7. SHAREHOLDERS' DEFICIT (CONTINUED)

Stock Option Plans (Continued)

Effective December 27, 2002, the Board of Directors adopted the DynaPel Systems, Inc. 2001 Stock Option Plan (the "2001 Plan") and reserved 250,000 shares of common stock for issuance under the 2001 Plan. Aggregate grants to non-employee directors under the 2001 Plan cannot exceed 25,000 shares.

Options granted under the 1998 Plan, the 2000 Plan and the 2001 Plan may be incentive stock options or nonqualified stock options, as determined by a Committee of the Board of Directors (the "Committee") at the time of grant.

Incentive stock options are generally to be granted at a price not less than the fair market value of the stock on the date of grant, or at a price not less than 110% of the fair market value, if granted to a participant who is greater than a 10% owner of the Company. Furthermore, the aggregate fair market value of the common stock, determined as of the date of grant, for which options are granted to any participant, shall not exceed $100,000. Nonqualified stock options may be granted at a price to be determined by the Committee, which may be equal to, greater than, or less than the fair market value at the date of grant. Option vesting terms are established by the Committee at the time of grant. The expiration date of all options granted under the 1998 Plan, the 2000 Plan and the 2001 Plan is determined at the time of grant and may not exceed ten years from the date of the grant, or five years from the date of grant for participants who own greater than 10% of the Company. At December 31, 2003, there were 140,000 options available for grant under the 1998 Plan, 288,500 options available for grant under the 2000 Plan and no options available for grant under the 2001 Plan.

During the six months ended June 30, 2004 and the year ended December 31, 2003, the Company recognized stock-based compensation expense of $65,625 and $131,250, respectively, in connection with stock options granted to employees and directors with exercise prices less than the market price of the stock on the date of grant. The compensation expense was calculated using the intrinsic value method.

The per share weighted average fair value of stock options granted in 2002 to employees and directors was $0.15 on the date of grant using the Black Scholes option-pricing model (excluding a volatility assumption) with the following weighted average assumptions: no expected dividend yield, risk-free interest rate of 2.89%, and an expected life of two years.

With respect to the options granted in 2002, the fair values of the options equaled their intrinsic value. No options were granted during the six months ended June 30, 2004 and in the year ended December 31, 2003.

The Company applies APB Opinion No. 25 in accounting for its stock options issued to employees and directors. Had the Company determined compensation cost based on the fair value at the grant date for its stock options granted prior to 2002, which vested subsequent to 2002, the Company's net loss for the year ended December 31, 2003 would have been changed to the pro forma amount indicated below and no pro forma changes would be made to the net income for the three and six months ended June 30, 2004, as such options did not vest subsequent to 2003:

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

7. SHAREHOLDERS' DEFICIT (CONTINUED)

Stock Option Plans (Continued)

	Six Months Ended June 30, 2004	Three Months Ended June 30, 2004	Year Ended December 31, 2003
Net income (loss):			
As reported	7,481,712	4,209,140	(2,393,325)
Pro forma	7,481,712	4,209,140	(2,395,979)

The following summarizes stock option activity under the 1998 Plan, the 2000 Plan and the 2001 Plan for the six months ended June 30, 2004 and the year ended December 31, 2003:

	Number of Shares	Weighted Average Exercise Price
Options outstanding at January 1, 2003	581,450	$ 2.60
Granted	-	-
Exercised	-	-
Expired	-	-
Options outstanding at January 1, 2004	-	$ -
Granted	-	-
Exercised	-	-
Expired	53,250	-
Options outstanding at June 30, 2004	528,200	$ 2.60

The following table summarizes information about stock options outstanding at June 30, 2004:

Range of exercise prices	Number outstanding at June 30, 2004	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at June 30, 2004	Weighted average exercise price
$ 0.30	250,000	8.99	$ 0.30	231,250	$ 0.30
3.50	144,200	5.55	3.50	144,200	3.50
5.50	134,000	6.16	5.50	134,000	5.50
$0.30-5.50	528,200	7.18	$ 2.60	509,450	$ 3.00

8. COMMITMENTS AND CONTINGENCIES

The Company leases an office facility in New York City from a shareholder under a month-to-month operating lease agreement. Rental expense under this agreement was approximately $34,000 and $45,000, respectively, for the six months ended June 30, 2004 and the year ended December 31, 2003.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

8. COMMITMENTS AND CONTINGENCIES (CONTINUED)

In addition, the Company is obligated under lease agreements in Munich, Germany and Florida for office spaces.

Minimum lease payments under these leases as of December 31, 2003 are approximately:

2004	$ 58,000
2005	86,000
2006	76,500
2007	13,000
	$ 233,500

9. INSOLVENCY OF DYNAPEL GERMANY

During the second quarter of 2004, an agreement was reached with the insolvency administrator in Munich, Germany. Pursuant to the agreement, the Company agreed to the following in exchange for its release from all liabilities outstanding as of the time of settlement:

a. Pay $100,000 in cash.

b. Through December 31, 2004, pay $400 per unit for each unit sold to existing customers of Dynapel Germany, with a minimum payment of $100,000 and a maximum payment of $200,000.

c. Through December 31, 2004, pay all royalties received from existing contracts for the products "Macro System" and "Asknet" with a minimum payment of $50,000 and a maximum payment of $100,000.

d. Pay an additional $150,000 provided the Company raises a minimum of $1,000,000 from investors from the date of the settlement through June 30, 2005.

As of June 30, 2004, the Company recorded a liability in the amount of $400,000 and removed from its books all assets and liabilities related to its bankrupt subsidiary. As a result of the above settlement, the Company recognized a gain of $1,317,879.

10. SUPPLEMENTAL CASH FLOW INFORMATION:

Additional cash flow information is as follows:

	Six Months Ended June 30, 2004	Year Ended December 31, 2003
Interest paid during the year	$ -	$ -
Income taxes paid during the year	$ -	$ -

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE PERIODS ENDED JUNE 30, 2004 AND YEAR ENDED DECEMBER 31, 2003

10. SUPPLEMENTAL CASH FLOW INFORMATION (CONTINUED):

NON-CASH INVESTING AND FINANCING ACTIVITIES:

	Six Months Ended June 30, 2004	Year Ended December 31, 2003
Conversion of bridge loans and accrued Interest to equity	$ 1,093,333	$ 858,973
Gain on settlement of liabilities of bankrupt subsidiary	$ 1,317,879	$ -

11. SUBSEQUENT EVENTS

The Company is considering to approve:

a. A share issue to existing shareholders at a subscription price of NOK 1.0 per share (0.14 US cents) (before any share splits) in connection with the listing of the Company's shares on the SMB list of the Oslo, Norway exchange.

The Share Issue will represent an offer for the subscription of a minimum of 20,000,000 shares and a maximum of 30,000,000 new shares, sufficient to generate issue proceeds for the Company of between NOK 20 million and NOK 30 million in the Share Issue. The Share Issue will be comprised as follows:

A retail offer to the public with an upper and lower limit for the number of shares that may be subscribed for (the "Retail Offering")

- An offer to institutions and other professional investors with a lower limit for the number of shares that may be subscribed for (the "Institutional Offering")

The Company anticipates that 30% of the Share Issue will be initially reserved for subscriptions through the Retail Offering and 70% of the Share Issue will be initially reserved for subscriptions through the Institutional Offering. However, the final allocation between the tranches will be decided on the basis of the subscription level in the respective tranches relative to the overall subscription level for the Share Issue.

The Share Issue will be conditional upon admission of the Company's shares to the SMB List of the Oslo exchange.

b. The assembly of an underwriting consortium, consisting of existing and new investors, for the purpose of guaranteeing NOK 20 million of the Share Issue. The underwriting consortium will receive an underwriting fee of 5% of the guaranteed amount, and, in the event the issue is oversubscribed, will be granted the right to subscribe for shares in the rights issue for an amount equivalent to 50 % of its total underwriting obligation.

c. A 1 for 5 stock exchange. Under this plan each shareholder will receive one new share of DynaPel Common Stock for each 5 shares currently held at the time such exchange becomes effective. The Board of Directors anticipates that the exchange will take place as soon as possible after approval.

Appendix 3 - Annual Report 2003

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED FINANCIAL STATEMENTS
AND
AUDITORS' REPORT

YEARS ENDED DECEMBER 31, 2003 AND 2002

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Israeloff, Trattner & Co. P.C.
CERTIFIED PUBLIC ACCOUNTANTS · FINANCIAL CONSULTANTS

INDEPENDENT AUDITORS' REPORT

The Board of Directors
of DynaPel Systems, Inc.

We have audited the accompanying consolidated balance sheets of DynaPel Systems, Inc. and Subsidiary as of December 31, 2003 and 2002, and the related statements of operations and comprehensive (loss), shareholders' deficits, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of DynaPel Systems, Inc. and Subsidiary as of December 31, 2003 and 2002, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the financial statements, the Company has suffered recurring losses from operations and has a net capital deficiency, which raises substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Israeloff, Trattner & Co., P.C.

Garden City, New York
April 23, 2004

ALLIOTT GROUP

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2003

ASSETS

	2003	2002
Current Assets		
Cash and cash equivalents (Note 1)	$ 50,920	$ 124,015
Trade accounts receivable (Note 1)	16,455	22,536
Prepaid expenses	397	9,210
Other current assets	38,612	30,151
Total Current Assets	106,384	185,912
Property and Equipment, net (Notes 1 and 2)	44,114	69,572
Other Assets	5,800	5,800
TOTAL ASSETS	$ 156,298	$ 261,284

LIABILITIES AND SHAREHOLDERS' DEFICIT

	2003	2002
Current Liabilities		
Accounts payable	$ 367,416	$ 317,768
Accrued expenses and other current liabilities	1,840,506	498,234
Total Current Liabilities	2,207,922	816,002
Convertible note payable and accrued interest thereon, subsequently converted to equity (Note 5)	3,550,730	3,318,440
Bridge loans subsequently converted to equity in 2004 and 2003, respectively (Note 6)	1,093,333	852,666
Deferred revenues and royalties (Notes 1, 3 and 9)	3,784,507	4,951,174
	10,636,492	9,938,282
Shareholders' Deficit		
Common stock, $0.10 par value, 700,000,000 shares authorized, 10,226,286 and 4,960,809 shares issued and outstanding at December 31, 2003 and 2002, respectively.	1,022,629	496,081
Additional paid-in capital	19,915,892	18,836,170
Accumulated deficit	(31,363,630)	(28,970,305)
Accumulated other comprehensive loss	(55,085)	(38,944)
Total Shareholders' Deficit	(10,480,194)	(9,676,998)
TOTAL LIABILITIES AND SHAREHOLDERS' DEFICIT	$ 156,298	$ 261,284

See the accompanying notes to the consolidated financial statements.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' DEFICIT

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

	Common Stock		Additional Paid-in	Accumulated	Accumulated Other Comprehensive	Total Shareholders'
	Shares	Amount	Capital	Deficit	Loss	Deficit
BALANCE AT JANUARY 1, 2002	2,366,494	$ 236,649	$ 17,868,780	$ (26,413,458)	$ (46,934)	$ (8,354,963)
Sale of stock	60,279	6,028	528,498	-	-	534,526
Issuance of anti-dilutive common stock to majority investors for no consideration	1,827,279	182,728	(182,728)	-	-	-
Issuance of common stock in consideration of capital raising efforts	308,313	30,831	(30,831)	-	-	-
Issuance of common stock to director for compensation	200,000	20,000	34,795	-	-	54,795
Sale of anti-dilutive common stock in combination with convertible debt	198,444	19,845	505,156	-	-	525,001
Issuance of stock options to employees and directors	-	-	112,500	-	-	112,500
Net loss	-	-	-	(2,556,847)	-	(2,556,847)
Unrealized foreign currency translation gain	-	-	-	-	7,990	7,990
BALANCE AT DECEMBER 31, 2002	4,960,809	$ 496,081	$ 18,836,170	$ (28,970,305)	$ (38,944)	$ (9,676,998)
Sale of stock	1,763,177	176,318	329,697	-	-	506,015
Issuance of common stock to director for compensation	329,297	32,930	77,102	-	-	110,032
Conversion of bridge loan and accrued interest for equity	3,173,003	317,300	541,673	-	-	858,973
Issuance of stock options to employees and directors	-	-	131,250	-	-	131,250
Net loss	-	-	-	(2,393,325)	-	(2,393,325)
Unrealized foreign currency translation loss	-	-	-	-	(16,141)	(16,141)
BALANCE AT DECEMBER 31, 2003	10,226,286	$ 1,022,629	$ 19,915,892	$ (31,363,630)	$ (55,085)	$ (10,480,194)

See the accompanying notes to the consolidated financial statements.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

	2003	2002
Royalties	$ 1,166,667	$ 1,166,667
Sales	423,369	265,620
Total sales and royalties	1,590,036	1,432,287
Operating Expenses:		
Cost of sales	93,196	49,589
Research and development	1,845,827	1,543,763
Marketing, general and administrative	1,648,672	1,675,960
Interest expense	398,793	303,497
Total operating expenses	3,986,488	3,572,809
Loss from operations	(2,396,452)	(2,140,522)
Other Income (Expense):		
Foreign currency exchange (losses) gains	(1,871)	35,126
Other income and (expenses)	4,998	(3,870)
Loss on early extinguishment of debt	-	(447,581)
Total other income (expense)	3,127	(416,325)
Net loss	(2,393,325)	(2,556,847)
Other Comprehensive (Expense) Income:		
Foreign currency translation adjustment	(16,141)	7,990
Comprehensive loss	$ (2,409,466)	$ (2,548,857)
Per Share Data:		
Basic and diluted loss per share	$ (0.29)	$ (0.68)
Basic and diluted weighted average common shares outstanding	8,383,336	3,747,815

See the accompanying notes to the consolidated financial statements.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2003

	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (2,393,325)	$ (2,556,847)
Adjustments to reconcile net loss to net cash used by operating activities:		
Interest accrued on notes and loans payable	338,683	271,865
Deferred royalties	(200,000)	(200,000)
Deferred revenue	(966,667)	(966,667)
Depreciation	42,439	66,118
Foreign currency exchange losses (gain)	1,871	(35,126)
Loss on early extinguishment of debt	-	447,581
Non-cash stock-based compensation	241,282	167,295
Change In assets and liabilities:		
Trade accounts receivable	6,081	3,516
Prepaid expenses	8,813	(9,210)
Other current assets	(8,461)	(18,516)
Other assets	-	20,316
Accounts payable	49,648	154,297
Accrued expenses and other current liabilities	1,342,272	622,672
Net cash used by operating activities	(1,537,364)	(2,032,706)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(16,981)	(19,147)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from short-term bridge loan	993,247	795,384
Proceeds from common stock issuance	506,015	1,059,527
Net cash provided by financing activities	1,499,262	1,854,911
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(18,012)	43,116
NET DECREASE IN CASH AND CASH EQUIVALENTS	(73,095)	(153,826)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	124,015	277,841
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 50,920	$ 124,015
ADDITIONAL CASH FLOW INFORMATION:		
Interest paid during the year	$ -	$ -
Income taxes paid during the year	$ -	$ -
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Conversion of bridge loans and accrued interest to equity	$ (858,973)	$ -

See the accompanying notes to the consolidated financial statements.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Organization

DynaPel Systems, Inc. ("DynaPel US") was incorporated in the State of Delaware in 1992. DynaPel's corporate office is located in New York, New York. In 1994, DynaPel formed a subsidiary, DynaPel Laboratories GmbH ("DynaPel Germany"), located in Ismaning, Germany. In January 2004, management of this subsidiary declared it to be insolvent. (See Note 9).

DynaPel US develops and markets intelligent video software tools and appliances for the security and broadcast industries based on patent-protected software technology and in-house developed video algorithm and compression technologies. DynaPel has an existing suite of products that offer function and cost benefits to owners of existing and/or planned video surveillance systems employed in a wide range of applications.

DynaPel's products are sold to commercial as well as military and governmental users. Sales are either pre-paid or made to highly credit-rated customers.

Going Concern

The Company's operations involve a number of risks and uncertainties. Factors that could affect the Company's future operating results and cause actual results to vary materially from expectations include, but are not limited to, rapid technology change, uncertainty of market acceptance of the Company's products and services, competition from substitute products and larger companies, protection of proprietary technology, the ability to generate sufficient capital to fund operations, strategic relationships and dependence on key individuals.

As reported in the accompanying financial statements, the Company incurred net losses of $2,393,325 and $2,556,847 for the years 2003 and 2002, respectively. At December 31, 2003, the Company has a shareholders' deficit of $10,480,194. Management of the Company plans to raise capital through the issuance of shares during 2004 and to restructure the liabilities of the insolvent German subsidiary. (See Note 9). The ability of the Company to continue as a going concern is dependent on the amount of money raised, the successful restructuring of the German subsidiaries' liabilities and the Company's future ability to generate revenues and profits from the sale of its products. There is no assurance that the Company will be successful in attaining these objectives. The accompanying financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Principles of Consolidation

The consolidated financial statements include the financial statements of DynaPel US and its wholly-owned subsidiary, DynaPel Germany. All significant intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

For financial statement purposes, the Company considers all highly liquid debt instruments with a maturity of three months or less when purchased to be cash equivalents. The Company maintains its cash in bank deposit accounts in the United States of America and overseas which, at times, may exceed applicable insurance limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

Accounts Receivable

Accounts receivable have been adjusted for all known uncollectible accounts and are stated at the amount management expects to collect from outstanding balances. Based on management's evaluation of collectibility, an allowance for doubtful accounts is not required.

Property and Equipment

Property and equipment are stated at cost, less accumulated depreciation. Depreciation is provided using straight-line and accelerated methods over the estimated useful lives of the assets. The estimated useful lives are as follows:

Computer equipment and software	3 years
Furniture, fixtures and other	3-5 years

Deferred Revenue

Deferred revenue consists primarily of an up-front royalty received November 5, 1999, upon execution of a license agreement which was effective January 1, 2000. Under terms of the license agreement, minimum future royalties were to be earned for the six-year period which began on January 1, 2000 through December 31, 2005. As a result, the Company deferred the up-front royalty and has been recognizing the corresponding revenue over the term of the minimum future royalties. This agreement was terminated effective March 2004. (See Notes 3 and 9).

Cost of Sales

Cost of sales is composed of costs related to the packaging of software and hardware for sale and depreciation of equipment used in production.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Research and Development Expenses and Capitalized Software Development Costs

Software development costs consist principally of compensation and benefits paid to the Company's employees. All software development costs not qualifying for capitalization are expensed as research and development costs when incurred.

The Company's policy is to expense all software development costs prior to establishing technological feasibility. Because the Company's products have reached this state of development almost concurrently with general release, the Company has not capitalized any software development costs.

Income Taxes

The Company accounts for income taxes using the asset and liability method, as prescribed by Statement of Financial Accounting Standards No. 109 "Accounting for Income Taxes". Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Statutory taxes not based on income are included in general and administrative expenses.

Translation of Foreign Currencies and Foreign Currency Transactions

Financial statements of the Company's foreign subsidiary are translated into U.S. dollars at current exchange rates, except for costs and expenses, which are translated at average exchange rates during each reporting period. Net exchange gains or losses resulting from the translation of assets and liabilities are accumulated as "accumulated other comprehensive income (loss)" and are reported as a separate component of shareholders' deficit. Transactions in currencies other than the U.S. dollar are recorded in U.S. dollars at exchange rate prevailing at the transaction dates. Exchange gains and losses are included in the Company's results of operations.

Stock Option Plans

The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations, in accounting for its fixed plan stock options issued to employees and directors. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. The Company applies Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, for its stock options to non-employees and non-directors. SFAS No. 123 established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic value-based method of accounting described above for stock options issued to employees and directors, and has adopted the disclosure requirements of SFAS No. 123.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Accounting for the Impairment or Disposal of Long-Lived Assets

The Company follows the provisions of Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This Statement requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell. The provisions of this Statement did not have a material impact on the Company's financial position, results of activities or liquidity for the years ended December 31, 2003 and 2002.

Reverse Stock Split

All share references have been adjusted to reflect a one for ten reverse stock split effected in April 2004.

Loss Per Common Share

Basic and diluted loss per common share is computed by dividing net loss by the weighted average number of common shares outstanding after giving effect to the reverse stock split Outstanding common stock options to purchase 581,450 common shares are anti-dilutive and are accordingly excluded from the calculation.

2. PROPERTY AND EQUIPMENT

Property and equipment consist of the following as of December 31:

	2003	2002
Computer software	$ 31,747	$ 30,556
Computer equipment	600,262	587,968
Furniture and fixtures	100,050	96,554
	732,059	715,078
Less: Accumulated depreciation	687,945	645,506
	$ 44,114	$ 69,572

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

3. COOPERATION AND BROADCAST LICENSE AGREEMENTS

Cooperation Agreement

Effective May 29, 1995, in conjunction with a reorganization of the Company, the Company entered into a Cooperation Agreement (the "Cooperation Agreement") with a shareholder (the "Cooperation Shareholder"). Under the terms of the Cooperation Agreement, the Cooperation Shareholder agreed to pay certain outstanding obligations of the Company and to fund the Company's operations. In return for funding the Company's operations, the Cooperation Shareholder received the right to license the Company's technology. All funds received by the Company from the Cooperation Shareholder as a result of the Cooperation Agreement were accounted for as deferred royalties and are offset, to the extent possible, against any future license royalty earned.

Effective October 31, 1999, funding of the Company's operations under the Cooperation Agreement ceased and the Cooperation Agreement was terminated. The Cooperation Shareholder entered into a license agreement with the Company on November 5, 1999.

Broadcast License

On November 5, 1999, the Company entered into an agreement (the "Broadcast License") with the Cooperation Shareholder to license the Company's Broadcast Technology. The Broadcast License was effective January 1, 2000 and was to continue through December 31, 2005. The Broadcast License was non-exclusive and covered the continents of Europe and Africa (the "Broadcast Territory"). Under the terms of the Broadcast License, the Cooperation Shareholder could: 1) incorporate the Broadcast Technology into other products; 2) manufacture, distribute, sell, use, promote or otherwise produce products using the Broadcast Technology available in the Broadcast Territory; 3) use the Broadcast Technology to encode broadcast transmissions of moving images for viewing in the Broadcast Territory; and, 4) grant sublicenses to its affiliates and third parties.

The Company received an advance of $5,800,000 upon execution of the Broadcast License, which was recorded as Deferred Royalties. In addition, the Company was to receive a percentage of the net receipts of any sublicenses granted to third parties and a percentage of the revenues from the sales of products developed using any part of the Broadcast Technology (the "Earned Royalties"). Earned Royalties, subject to a $200,000 annual minimum, were to be offset against Deferred Royalties. The deferred revenue of $5,800,000 was being recognized ratably over the term of the Broadcast License.

During 2000, the Broadcast License was amended. The amendment stated that if the Cooperation Shareholder did not use the licensed rights, and the market price of the Company's stock exceeded $10 per share, the Cooperation Shareholder and/or the Company had the right to terminate the Broadcast License. Upon termination of the Broadcast License, the Company would pay the Cooperation Shareholder the outstanding balance of the Deferred Royalties in the form of Company stock, not to exceed 500,000 shares.

Subsequent to December 31, 2003, the Broadcast License was terminated. (See Note 9).

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

4. INCOME TAXES

As of December 31, 2003 and 2002, the Company had approximately $22,200,000 and $19,800,000, respectively, of net operating loss carryforwards, which expire at various dates beginning in tax year 2008 through 2023. The availability to offset income taxes in future years may be restricted if the Company undergoes an ownership change, which may occur as a result of future sales of any stock and other events.

The tax effect of temporary differences that give rise to the Company's deferred tax assets and liabilities are as follows as of December 31, 2003 and 2002:

	2003	2002
Net operating loss carryforwards	$ 10,971,133	$ 10,013,803
Less: Valuation allowance	10,971,133	10,013,803
Net deferred income tax asset	$ -	$ -

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. The ultimate realization of deferred tax assets depends on the generation of future taxable income and tax planning in making these assessments.

The net increase in the valuation allowance for deferred income taxes for the years ended December 31, 2003 and 2002 was $957,330 and $1,019,543, respectively.

5. CONVERTIBLE NOTE PAYABLE

In September 2000, the Company entered into a short-term financing arrangement ("Loan Agreement") with Technoinvest, a German entity, under which the Company could borrow a maximum of $2,500,000. At December 31, 2003 and 2002, $2,500,000 was outstanding. The outstanding balance accrues interest at 7% per annum. Accrued interest outstanding at December 31, 2003 and 2002 was $1,050,730 and $818,440, respectively.

According to the original Loan Agreement, the Company could repay the outstanding principal and interest at any time without penalty, but no later than September 11, 2001. Additionally, the lender reserved the right to convert the outstanding balance of the loan into common stock if the Company undertook an offering of securities during the term of the loan.

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DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

5. CONVERTIBLE NOTE PAYABLE (CONTINUED)

In September 2001, the Company began negotiations with the lender to amend the repayment provisions of the original Loan Agreement. An agreement was reached in December 2001, whereby the lender waived repayment of the outstanding balance of the loan subject to the improvement of the financial condition of the Company. At such time as the Company could repay the loan without endangering its financial existence, the outstanding balance of the loan becomes payable in full including interest earned up to the date of repayment. This agreement also provides for the lender, at its discretion, to convert the outstanding balance of the loan including interest into common stock at a conversion price of 14 Norwegian Crowns (NOK) per share. As a result of these provisions the Company excluded this loan and the accrued interest thereon from current liabilities.

In March 2004, the Company modified the terms of its existing agreement with Technoinvest whereby the outstanding convertible note payable in the amount of $2,500,000 and all current and accrued interest totaling approximately $3,602,500, was converted into 400,000 common shares of the Company, with a current value of approximately $57,000, and 400,000 NOK (approximately $55,000). The Company will recognize a gain of approximately $3,500,000 on this troubled debt restructuring.

6. SHORT-TERM BRIDGE LOANS

In August 2002, the Company entered into a short-term bridge loan arrangement under which the Company could borrow a maximum of $1,100,000. At December 31, 2002, principal of $795,384 was borrowed and outstanding. The outstanding balance accrued interest at 20% per annum. At December 31, 2002, accrued interest was $57,282.

According to the original arrangement, the Company could have repaid the outstanding principal and interest at any time without penalty, but no later than January 15, 2003. Additionally, the lender reserved the right to convert the outstanding balance of the loan and accrued interest into common stock, at a fixed rate of NOK 0.20 per share, if the Company undertook an offering of securities during the term of the loan. In August 2003, the short-term bridge loan and the related accrued interest, totaling approximately $859,000, were fully converted, in accordance with its existing terms, into 3,173,003 shares of common stock of the Company.

In June 2003, the Company entered into a secured short-term bridge loan arrangement, secured by the assets of the Company, under which the Company could borrow a maximum of $1,000,857. At December 31, 2003, $993,247 was borrowed and outstanding. The outstanding balance accrues interest at 20% per annum and matures in March 2004. At December 31, 2003, interest accrued was $100,086.

According to the original arrangement, the lender reserved the right to convert the outstanding balance plus accrued interest into common stock of the Company at a share price of NOK 0.30. Also, the arrangement had anti-dilution provisions to protect the lender if the Company subsequently sold shares at a price below the conversion price.

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6. SHORT-TERM BRIDGE LOANS (continued)

In January 2004, the outstanding secured short-term bridge loan was converted into 7,825,701 shares of common stock of the Company, pursuant to its existing terms. (See Note 9).

7. SHAREHOLDERS' DEFICIT

Private Placement/Exchange

In April and May of 2002, the Company completed an equity offering comprised of units consisting of one common share and two warrants. 602,785 shares were issued under this offering. All warrants were cancelled in September 2002 in conjunction with the convertible financing described below.

In September 2002, the Company commenced a financing of convertible notes, the conversion price of which was substantially less than the sale price of the units offered in the April and May 2002 offering discussed above. The Company created an anti-dilution amendment to the April and May offering, whereby the related investors, who also invested in the convertible notes, would receive anti-dilution shares. For investors who did not wish to invest in the convertible notes, a smaller amount of anti-dilution shares were issued. As such, 18,272,790 of anti-dilution shares were issued and the warrants from the April and May offering were cancelled.

During 2002, the Board of Directors approved a total of 475,000 common shares for issuance as compensation related to officers' compensation and capital raising efforts provided to the Company by consultants. In addition, 33,131 common shares were issued to investors as commission shares. The value of such shares is treated as a direct charge to equity as a cost of raising capital.

In connection with a November 2001 financing, the Company issued common stock upon conversion in May 2002 of the convertible notes component of securities sold. The convertible notes earned interest at a rate of 18% per annum and were convertible into common stock at NOK 5 per share. At the maturity date, interest was calculated and the entire amount of convertible notes and interest totaling $1,070,941, were converted into 198,444 common shares pursuant to the existing terms.

In January 2003, the Company completed a private placement of common shares. This offering was transacted in the form of a Rights Offering to all shareholders at a subscription price of NOK 0.20. A total of 1,763,177 shares were issued for proceeds of $506,015.

Also in January 2003, the Company issued 219,630 shares for compensation of $63,032 in lieu of cash compensation for certain consultants and in lieu of salary for certain employees, and also reached an agreement with a former officer, whereby 109,667 common shares of the Company, with a current value of approximately $47,000, were issued in settlement of certain consulting services.

In August 2003, the Company issued 3,173,003 shares of common stock upon conversion of its original short-term bridge loan. (See Note 6).

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

7. SHAREHOLDERS' DEFICIT (CONTINUED)

Stock Option Plans (Continued)

Effective January 27, 1999, the Board of Directors adopted the DynaPel Systems, Inc. 1998 Stock Option Plan (the "1998 Plan") and reserved 275,000 shares of common stock for issuance under the 1998 Plan. Aggregate grants to non-employee directors under the 1998 Plan cannot exceed 25,000 shares.

Effective March 23, 2000, the Board of Directors adopted the DynaPel Systems, Inc. 2000 Stock Option Plan (the "2000 Plan") and reserved 250,000 shares of common stock for issuance under the 2000 Plan. Aggregate grants to non-employee directors under the 2000 Plan cannot exceed 25,000 shares.

Effective December 27, 2002, the Board of Directors adopted the DynaPel Systems, Inc. 2001 Stock Option Plan (the "2001 Plan") and reserved 250,000 shares of common stock for issuance under the 2001 Plan. Aggregate grants to non-employee directors under the 2001 Plan cannot exceed 25,000 shares.

Options granted under the 1998 Plan, the 2000 Plan and the 2001 Plan may be incentive stock options or nonqualified stock options, as determined by a Committee of the Board of Directors (the "Committee") at the time of grant.

Incentive stock options are generally to be granted at a price not less than the fair market value of the stock on the date of grant, or at a price not less than 110% of the fair market value, if granted to a participant who is greater than a 10% owner of the Company. Furthermore, the aggregate fair market value of the common stock, determined as of the date of grant, for which options are granted to any participant, shall not exceed $100,000. Nonqualified stock options may be granted at a price to be determined by the Committee, which may be equal to, greater than, or less than the fair market value at the date of grant. Option vesting terms are established by the Committee at the time of grant. The expiration date of all options granted under the 1998 Plan, the 2000 Plan and the 2001 Plan is determined at the time of grant and may not exceed ten years from the date of the grant, or five years from the date of grant for participants who own greater than 10% of the Company. At December 31, 2003, there were 140,000 options available for grant under the 1998 Plan, 288,500 options available for grant under the 2000 Plan and no options available for grant under the 2001 Plan.

During the years ended December 31, 2003 and 2002, the Company recognized stock-based compensation expense of $131,250 and $112,500, respectively, in connection with stock options granted to employees and directors with exercise prices less than the market price of the stock on the date of grant. The compensation expense was calculated using the intrinsic value method.

The per share weighted average fair value of stock options granted in 2002 to employees and directors was $0.15 on the date of grant using the Black Scholes option-pricing model (excluding a volatility assumption) with the following weighted average assumptions: no expected dividend yield, risk-free interest rate of 2.89%, and an expected life of two years.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

7. SHAREHOLDERS' DEFICIT (CONTINUED)

Stock Option Plans (Continued)

With respect to the options granted in 2002, the fair values of the options equaled their intrinsic value. No options were granted in 2003.

The Company applies APB Opinion No. 25 in accounting for its stock options issued to employees and directors. Had the Company determined compensation cost based on the fair value at the grant date for its stock options granted prior to 2002, which vested in 2002 and 2003, the Company's net loss for the years ended December 31, 2003 and 2002 would have been changed to the pro forma amounts indicated below:

	2003	2002
Net loss:		
As reported	$ (2,393,325)	$ (2,556,847)
Pro forma	(2,395,979)	(2,573,872)

The following summarizes stock option activity under the 1998 Plan, the 2000 Plan and the 2001 Plan for the years ended December 31, 2002 and 2003:

	Number of Shares	Weighted Average Exercise Price
Options outstanding at January 1, 2002	394,000	$ 4.50
Granted	250,000	0.30
Exercised	-	-
Expired	(62,550)	4.50
Options outstanding at December 31, 2002	581,450	$ 2.60
Granted	-	-
Exercised	-	-
Expired	-	-
Options outstanding at December 31, 2003	581,450	$ 2.60

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

7. SHAREHOLDERS' DEFICIT (CONTINUED)

Stock Option Plans (Continued)

The following table summarizes information about stock options outstanding at December 31, 2003:

Range of exercise prices	Number outstanding at December 31, 2003	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at December 31, 2003	Weighted average exercise price
$ 0.30	250,000	8.99	$ 0.30	162,500	$ 0.30
3.50	184,450	5.55	3.50	184,450	3.50
5.50	147,000	6.16	5.50	147,000	5.50
$0.30-5.50	581,450	7.18	$ 2.60	493,950	$ 3.00

8. COMMITMENTS AND CONTINGENCIES

The Company leases an office facility in New York City from a shareholder under a month-to-month operating lease agreement. Rental expense under this agreement was approximately $45,000 and $65,000, respectively, for the years ended December 31, 2003 and 2002.

In addition, the Company is obligated under lease agreements in Ismaning and Munich, Germany for office spaces occupied by DynaPel Germany and its newly-formed subsidiary Holon Technology GmbH.

Minimum lease payments under these leases as of December 31, 2003 are approximately:

2004	$ 167,000
2005	207,000
2006	207,000
2007	13,000
	$ 594,000

9. SUBSEQUENT EVENTS

In January 2004, the management of DynaPel Germany declared itself insolvent to protect it from the demands of the tax authorities in Germany and other creditors. The management of DynaPel Germany has retained legal counsel with experience in corporate restructuring and tax issues to protect its interest in connection with the insolvency. In the opinion of the Board of Directors, based on the information available, the insolvency of DynaPel Germany should not affect DynaPel US and its current financial and marketing efforts in any material way. The Company expects the insolvency to be completed in the second quarter of 2004.

As a result of the insolvency in March 2004, the Company formed a new German subsidiary, Holon Technology GmbH. A majority of the engineering team from DynaPel Germany have agreed to work for Holon Technology GmbH.

DYNAPEL SYSTEMS, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

9. SUBSEQUENT EVENTS (CONTINUED)

In January 2004, in conjunction with the conversion of the short-term bridge loan, the Company raised 10,140,000 NOK ($1,357,000) with the sale of 10,140,000 common shares of the Company in a private placement to existing investors and certain new investors.

In February 2004, a Special Meeting of Shareholders was held in Oslo, Norway. At that meeting, the following points on the agenda were approved: (1) Approval of a Rights Issue and Listing on the Oslo Stock Exchange; (2) approval of the formation of an Underwriting Consortium in conjunction with the Listing described previously; (3) Approval of the 2004 Stock Option Plan; (4) Approval of an increase in the authorized common shares of the Company from 150 million to 700 million; and (5) Approval of a 1 for 10 reverse common stock split and an increase of the par value of common stock from $0.01 to $0.10. The 1 for 10 reverse common stock split was effected April 1, 2004. All changes to the Company's authorized capital has been given retroactive effect in the accompanying financial statements.

In March 2004, the Company did a follow-on equity placement to all existing shareholders (a Rights Offering) in the amount of 3,000,000 NOK ($428,000) before transaction expenses. The result of this transaction was the placement of an additional 3,000,000 common shares of the Company. After completing this offering, the Company had approximately 31,190,000 shares outstanding.

At the same time as the rights offering, the Company entered into a mandate agreement with DnB NOR Markets regarding a NOK 25 million rights issue to all existing shareholders at a subscription price of NOK 1.0 per share combined with an intention to apply for listing on the SMB list of Oslo Stock Exchange. An underwriting consortium has been assembled guaranteeing the NOK 25 million rights issue, conditional upon the listing of DynaPel on the Oslo Stock Exchange. The underwriting consortium will receive an underwriting fee of 5% of the guaranteed amount, and will be granted the right to subscribe for shares in the rights issue for an amount equivalent to 50% of their total underwriting obligation.

In March 2004, the Company signed a License Termination Agreement with the Cooperation Shareholder, which had the effect of terminating any and all ongoing agreements or amendments to agreements, including the Broadcast License, which they had entered into over the course of their relationship. Further, as a result of this agreement, neither the Cooperation Shareholder nor the Company (or any subsidiary of the Company) will be entitled to any additional royalty or revenue from the other party, whether currently due or accrued, notwithstanding anything to the contrary in any agreements between the two parties, as of December 31, 2003. In connection with the License Agreement, the Company will recognize all outstanding deferred royalties and deferred revenue in the first quarter of 2004 resulting in income of $3,784,508, which will be reported as other income in the accompanying consolidated statement of operations and comprehensive income.

Appendix 4 - Subscription Form

Share Issue DynaPel Systems Inc - Subscription form

For complete information on the Share Issue, see the attached Prospectus

GUIDANCE FOR SUBSCRIBERS OF SHARES
Subscription of shares in the Share Issue may take place during the period from and including 13 January, 2005 to 16.00 CET on 18 January, 2005 ("the Subscription Period"). Subscriptions may only be made by correctly completing and signing this form and sending it by mail or fax to the Subscription Office. **The subscription form MUST be received by the Subscription Office within the specified deadline in order to be valid.** The Subscription Office is:

DnB NOR Markets
Stranden 21
N-0021 Oslo, Norway
Telephone: 22 94 88 80 / Telefax: 22 83 20 00

Subscriptions received are legally binding on the subscriber. Those subscribing for shares bear the risk of any delay in the post or unavailability of fax lines. DynaPel Systems Inc will be free to accept or reject subscription forms that are unlawful, received late, incomplete or incorrect. In the event of over-subscription for shares, the number of shares allotted may be reduced in accordance with the allotment criteria described in the attached Prospectus which has been prepared in connection with the transaction.

SHARE ISSUE
Under the Share Issue DynaPel Systems Inc will issue a minimum of 5,714,286 and maximum of 6,000,000 new shares. The gross proceeds of the Share Issue amounts to between NOK 20 million and NOK 21 million. The Share Issue will be carried out as a public share offering towards the general public as well as institutional and professional investors, primarily in the Norwegian market and in reliance on Regulation S of the United States Securities Act of 1933, as amended (the "Securities Act"), as more fully described in the Prospectus (see "Transfer Restrictions" in section 2.10 in the attached Prospectus). The minimum subscription in the Share Issue will be 2,000 shares, which will constitute a stock exchange trading block. An Underwriting Syndicate has been established in order to underwrite NOK 20 million of the Share Issue. Participating in the guarantee consortium carries a right to allotment of shares corresponding to 50% of the underwritten amount. The Share Issue is conditioned that the Company in relation to the Share Issue receives proceeds of minimum NOK 20 million. In addition, the Share Issue is conditioned that the exchange rate between USD and NOK provide for a subscription price in NOK in the Share Issue of more than the par value of USD 0.50 per share. The Company has entered into a payment guarantee with one existing shareholder for an amount of up to NOK 5 mill. The payment guarantee shall secure an effective registration of the new shares resulting from the Share Issue. See section 2.16 for details on the payment guarantee.

SUBSCRIPTION PRICE
The subscription price has been set by the Company's Board of Directors at NOK 3.50 per share.

ALLOTMENT
Final allotment of shares will be made by the Company's Board of Directors in accordance with the allotment criteria described in section 2.8 of the attached Prospectus**.**

PAYMENT FOR SHARES ALLOTTED
On subscription of shares, each subscriber gives DnB NOR Markets a one-time irrevocable authorization to debit a specified Norwegian bank account for the amount allotted. Notice of allotment will be dispatched on or around 19 January, 2005. The account will be debited on or around 21 January, 2005. **There must be sufficient funds on the specified account to cover the full amount before it is debited.** If the specified account cannot be debited on the relevant date, DynaPel Systems Inc reserves the right to reduce or cancel the subscription or sell the shares allotted for the subscriber's account and risk. In the event of late payment, interest shall be charged on the amount overdue at 8.75% p.a. from the date due until payment is made. If the conditions described in the attached Prospectus are met, the shares are expected to be registered on the individual subscriber's VPS account on or around 27 January, 2005. The first day for trading of the company's shares on the Oslo Børs SMB list will at the latest be 27 January, 2005, unless otherwise decided by Oslo Børs.

DETAILS OF SUBSCRIPTION

Purchaser's VPS account* (12 digits)	Number of shares (minimum 2,000 shares)	For completion by subscription office
Price per share: **NOK 3.50**	Total to pay in NOK:	
I/we hereby give DnB NOR Markets a one-time authorisation to charge my/our Norwegian bank account for the shares allotted. (Number of shares allotted x subscription price)		--- **(Bank account – 11 digits MUST BE COMPLETED)**

In accordance with the terms set out in this form and the attached Prospectus, the number of shares specified above are hereby subscribed. At the same time, authorization is given to charge my/our specified account.

____
Subscription place and date
Must be dated in the subscription period.

____
Binding signature. The subscriber must have legal capacity.
If signed pursuant to an authorisation, documentation in the form of a company certificate or power of attorney must be attached

INFORMATION ON THE SUBSCRIBER

Name:	**Personal / organisation number:**
Address:	
Postcode/place:	
Daytime telephone:	**Telefax/e-mail:**
Account for dividend:	**Citizenship:**

*In order to subscribe for shares you must have established a securities account (VPS account). Under the regulations, a VPS account must be established in person and supported by evidence of identity with an account manager that can be a bank or an authorized stock broking firm.

DynaPel

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