

REEDS INC  
Form SB-2/A  
July 31, 2006

As filed with the Securities and Exchange Commission on July 31, 2006

Registration No. 333-135186

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

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PRE-EFFECTIVE AMENDMENT NO. 1 TO  
FORM SB-2/A  
REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933

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**Reed's, Inc.**

(Name of small business issuer in its charter)

**Delaware**  
(State or jurisdiction of  
incorporation or organization)

**2086**  
(Primary Standard Industrial  
Classification Code Number)

**95-4348325**  
(I.R.S. Employer  
Identification Number)

**13000 South Spring Street**  
**Los Angeles, California 90061**  
**(310) 217-9400**  
(Address and telephone number of  
principal executive offices and  
principal place of business)

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**Christopher J. Reed**  
**Chief Executive Officer**  
**13000 South Spring Street**  
**Los Angeles, California 90061**  
**(310) 217-9400**

(Name, address and telephone number of agent for service)

*With copies to:*

**Jeffrey P. Berg, Esq.**  
**Kenneth M.H. Hoff, Esq.**  
**Jenkins & Gilchrist, LLP**  
**12100 Wilshire Boulevard**  
**Suite 1500**

**Los Angeles, California 90025-7120**  
**(310) 820-8800**

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

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box.

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

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

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

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

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**THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATE OR DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT SHALL FILE A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THIS REGISTRATION STATEMENT SHALL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8(a) OF THE SECURITIES ACT OF 1933, AS AMENDED, OR UNTIL THE REGISTRATION STATEMENT SHALL BECOME EFFECTIVE ON SUCH DATE AS THE COMMISSION, ACTING PURSUANT TO SAID SECTION 8(a), MAY DETERMINE.**

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**The information in this prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities nor does it seek an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.**

**Subject to Completion, dated July 31, 2006**

**333,156 Shares of Common Stock**

**Reed's, Inc.**

### **RESCISSION OFFER**

We develop, manufacture, market and sell natural non-alcoholic beverages, candies and ice creams.

On May 13, 2005, a registration statement relating to our initial public offering of common stock was declared effective by the Securities and Exchange Commission. As a result, through the date of this prospectus, 333,156 shares of common stock were sold to the public for \$4.00 per share

There is no current public market for our shares and there is no assurance that a public market for our shares will ever develop. In the event a public market for our shares does not develop, our stockholders may be unable to sell the shares for an extended period of time. We intend to apply for listing of our common stock on the Nasdaq Capital Market or the American Stock Exchange following the completion of this rescission offer and our public offering, if we are able to qualify for such markets, and if not, we anticipate that US EURO Securities, Inc., one of our underwriters in the public offering, will apply for quotation of our common stock on the Over the Counter Bulletin Board ("OTCBB"). However, we cannot assure you when or if a market for our common stock will be established.

#### **The Rescission Offer**

- We are offering to repurchase 333,156 shares of our common stock from persons who are or were residents of California, Colorado, Connecticut, Hawaii, Illinois, Indiana, Louisiana, Massachusetts, Missouri, Montana, New York, Oregon, South Carolina, Utah, Vermont, Virginia and Washington and the country of Israel. These persons purchased shares of our common stock in our initial public offering. If our rescission offer is accepted by all offerees, we will be required to make an aggregate payment to the holders of these shares of up to approximately \$1,332,624, plus statutory interest.
- The repurchase price for the shares of our common stock subject to the rescission offer will be \$4.00 per share, which is equal to the price paid by those persons who purchased these shares. If you accept our rescission offer and surrender your shares, you will receive interest, based on the repurchase price noted above and calculated from the date you purchased the shares through the date that the rescission offer expires at the interest rate based on your state of residence.
- Federal law does not provide a specific interest rate to be used in the calculation of the consideration to be received in connection with the repurchases of securities by an issuer in a rescission offer. We intend to use the legal rates of interest for the repurchase of shares based on the state of residence of the stockholder.

**Investing in our common stock involves a high degree of risk. See "Risk Factors" beginning on page 8 to read about factors you should consider before accepting or rejecting the rescission offer.**

The rescission offer will expire on \_\_\_\_\_, 2006.

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.**

The date of this prospectus is \_\_\_\_\_, 2006

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You should rely only on the information contained in this prospectus. We have not authorized anyone to provide you with information that is different from that contained in this prospectus. We are offering to repurchase shares of our common stock only in jurisdictions where offers and sales are permitted. The information in this prospectus is complete and accurate only as of the date of the front cover regardless of the time of delivery of this prospectus or of any sale of shares. Except where the context requires otherwise, in this prospectus, the “Company,” “Reed’s,” “we,” “us” and “our” refer to Reed’s, Inc., a Delaware corporation.

## QUESTIONS AND ANSWERS ABOUT THE RESCISSION OFFER

### *General*

#### **Q: Why are we making the rescission offer?**

**A:** From August 3, 2005 through April 7, 2006, we issued 333,156 shares of our common stock in connection with our initial public offering pursuant to a Registration Statement on Form SB-2 (333-120451). The shares we issued in connection with the initial public offering were not issued pursuant to an effective registration statement and may not have been exempt from the registration or qualification requirements under the Securities Act of 1933, as amended, or the Securities Act, and under those state securities laws that provide an exemption from such requirements. We became aware that the shares may not have been issued pursuant to an effective registration statement. Because the shares were not issued pursuant to an effective registration statement and there was no available exemption from the registration requirements of the Securities Act or the registration or qualification requirements of the various states for such issuances, the shares issued in connection with the initial public offering may have been issued in violation of either federal or state securities laws, or both, and may be subject to rescission. In order to address this issue, we intend to make and complete this rescission offer prior to the effective date of the registration statement relating to the public offering to all holders of any outstanding shares who we believe may be entitled to argue for rescission. Pursuant to this rescission offer, we will offer to repurchase these shares then outstanding from the holders. We will be making this rescission offer to 167 persons who are or were residents of California, Colorado, Connecticut, Hawaii, Illinois, Indiana, Louisiana, Massachusetts, Missouri, Montana, New York, Oregon, South Carolina, Utah, Vermont, Virginia and Washington, and in the country of Israel. If our rescission offer is accepted by all offerees, we could be required to make an aggregate payment to the holders of these shares of up to approximately \$1,332,624, plus statutory interest.

The rescission offer is not an unanticipated development. Rather, our intent to make this rescission offer and the details of the rescission offer were disclosed in our Annual Report on Form 10-KSB for the year ended December 31, 2005. The rescission offer process is proceeding as disclosed in our public filings and as we expect. We intend to commence the rescission offer on \_\_\_\_\_, 2006. The filing of the registration statement relating to the rescission offer is a normal part of the rescission offer process.

#### **Q: Which shares of common stock are included in the rescission offer?**

**A:** We are offering, upon the terms and conditions described in this prospectus, to rescind the sale of 333,156 shares of common stock issued in connection with our initial public offering.

#### **Q: When does the rescission offer expire?**

**A:** Our rescission offer will expire on \_\_\_\_\_, 2006.

**Q: What will I receive if I accept the rescission offer?**

**A:** If you accept our rescission offer with respect to the common stock you purchased in the initial public offering, we will repurchase the shares you hold that are subject to the rescission offer at the price per share you paid, plus interest at the current statutory rate per year, from the date of purchase through the date the rescission offer expires.

The legal rates of interest for the repurchase of shares will be based on the state of residence of the stockholder. These interest rates are as follows:

State	Interest Rate	State	Interest Rate
California	7%	Montana	10%
Colorado	8%	New York *	7%
Connecticut	6%	Oregon	9%
Hawaii	10%	South Carolina	11.25%
Illinois	10%	Utah	12%
Indiana	8%	Vermont	12%
Louisiana	8%	Virginia	6%
Massachusetts	6%	Washington	8%
Missouri	8%	Israel *	7%

\* New York and Israeli law do not provide a specific interest rate. For purposes of the rescission offer, we are applying the rate of interest of California (our principal place of business) to calculate the consideration to be received by New York and Israeli residents who may be entitled to rescission rights.

**Q: Can you give me an example of what I will receive if I accept the rescission offer?**

**A:** We will repurchase outstanding shares of common stock subject to the rescission offer at the price per share you paid, plus interest at the current statutory rate per year, from the date of purchase of your shares through the date that the rescission offer expires. If you are a resident of California and hold 1,000 shares of our common stock that you purchased in connection with the public offering at a per share price of \$4.00 and you accept our rescission offer, you would receive:

- The original purchase price = 1,000 X \$4.00 = \$4,000.
- Plus simple interest at 7% per year for 10 months = \$233.33.
- For a total of \$4,233.33.

You will not have any right, title or interest to the shares of common stock you will be surrendering upon the closing of the rescission offer, and you will only be entitled to receive the proceeds from our repurchase of the common stock.

**Q: How will the rescission offer be funded?**

**A:** We have entered into an agreement with Mark Reed and Robert T. Reed, Jr. (the “designated purchasers”) that they would irrevocably commit to purchase up to all of the shares in the rescission offer that are tendered to us for rescission. We would assign to the designated purchasers the right to purchase any rescission shares at 100% of the amount required to pay the rescission price under applicable state law. As currently contemplated, the initial \$250,000 of rescission shares would be purchased by Mark Reed. If the number of rescission shares tendered for rescission exceeds \$250,000 of shares, Robert T. Reed, Jr. would purchase the balance of the rescission shares tendered for

rescission to us. Each of the designated purchasers is a brother of Christopher J. Reed, our Chief Executive Officer, Chief Financial Officer and the Chairman of the Board of Directors. Robert T. Reed, Jr. also is our Vice President and National Sales Manager - Mainstream and a beneficial owner of approximately 7.13% of our common stock.

**Q: Have any officers, directors or 5% stockholders advised us whether they will participate in the rescission offer?**

**A:** None of our officers, directors or 5% stockholders purchased shares in our initial public offering and are not eligible to participate in this rescission offer for purposes of tendering their shares for rescission. However, we have entered into an agreement with Mark Reed and Robert T. Reed, Jr. that they would irrevocably commit to purchase up to all of the shares in the rescission offer that are tendered to us for rescission. Robert T. Reed, Jr. is a beneficial owner of approximately 7.13% of our common stock. If Robert T. Reed, Jr. purchases shares in this rescission offer, he would increase his ownership interest in us.

**Q: Am I required to accept the rescission offer?**

**A:** The rescission offer is merely an offer to repurchase shares. No stockholder is required to accept our rescission offer.

**Q: If I do not accept the offer now, can I sell my shares?**

**A:** If you do not accept the rescission offer, you can sell the shares of common stock that were subject to the rescission offer without limitation as to the number or manner of sale. However, our common stock is not publicly traded, and there can be no assurances if or when such a market will develop.

**Q: What do I need to do now to accept or reject the rescission offer?**

**A:** To accept or reject the rescission offer, you must complete and sign the accompanying election form and return it in the enclosed return envelope to us, to the attention of Christopher J. Reed, 13000 South Spring Street, Los Angeles, California 90061, as soon as practical but in no event later than \_\_\_\_\_, 2006. If you are accepting the rescission offer, please also include in your return envelope, with respect to any shares of common stock that you want us to repurchase,

- a completed and signed election form (see [Appendix A](#)), and
- a stock power representing the shares you are surrendering for repurchase (see [Appendix B](#)).

**Q: Can I accept the rescission offer in part?**

**A:** If you accept the rescission offer, then you must accept the rescission offer with respect to all of the shares of common stock issued to you in connection with our initial public offering.

**Q: What happens if I do not return my rescission offer election form?**

**A:** If you do not return a properly completed election form before the expiration date of our rescission offer, you will be deemed to have rejected our offer.

**Q: What remedies or rights do I have now that I will not have after the rescission offer?**

**A:** It is unclear whether or not you will have a right of rescission under federal securities laws after the rescission offer. The staff of the Securities and Exchange Commission, or SEC, is of the opinion that a person's right of rescission created under the Securities Act may survive the rescission offer. Generally, the federal statute of limitations for noncompliance with the requirement to register securities under the Securities Act is one year from the date of the violation upon which the action to enforce liability is based.



The state remedies and statutes of limitations vary and depend upon the state in which you purchased the shares. For a more detailed description of the various state laws governing rescission rights in the respective states, see “Rescission Offer - Effect of Rescission Offer.”

We believe that your acceptance of the rescission offer will preclude you from later seeking similar relief. Regardless of whether you accept the rescission offer, we believe that any remedies you may have after the rescission offer expires would not be greater than an amount you would receive in the rescission offer.

**Q: Can I change my mind after I have mailed my signed election form?**

**A:** Yes. You can change your decision about accepting or rejecting our rescission offer at any time before the expiration date. You can do this by completing and submitting a new election form. Any new election forms must be received by us prior to the expiration date in order to be valid. We will not accept any election forms after the expiration date.

**Q: Who can help answer my questions?**

**A:** You can call Christopher J. Reed at Reed’s, at (310) 217-9400, with questions about the rescission offer.

**Q: Where can I get more information about Reed’s?**

**A:** You can obtain more information about Reed’s from the filings we make from time to time with the SEC. These filings are available on the SEC’s website at [www.sec.gov](http://www.sec.gov).

## SUMMARY

*This summary highlights selected information from this prospectus. It does not contain all of the information that is important to you. We encourage you to carefully read this entire prospectus and the documents to which we refer you. The following summary is qualified in its entirety by reference to the detailed information appearing elsewhere in this registration statement.*

### **Our Company**

We develop, manufacture, market and sell natural non-alcoholic and “New Age” beverages, candies and ice creams. “New Age Beverages” is a category that includes natural soda, fruit juices and fruit drinks, ready-to-drink teas, sports drinks and water. We currently offer 15 beverages, three candies and three ice creams. We sell most of our products in specialty gourmet and natural food stores, supermarket chains, retail stores and restaurants in the United States and, to a lesser degree, in Canada.

We primarily sell our products through a network of natural, gourmet and independent distributors. We also maintain an organization of in-house sales managers who work mainly in the stores serviced by our natural, gourmet and mainstream distributors and with our distributors. We also work with regional, independent sales representatives who maintain store and distributor relationships in a specified territory. In Southern California, we have our own direct distribution system.

Our current business strategy is to maintain our marketing focus in the natural food marketplace while expanding sales of our products in mainstream markets and distribution channels. We believe that the proceeds of our public offering may accelerate the success of this business strategy by providing working capital to finance an expanded in-house sales and distribution network.

We produce certain of our soda products for the western half of the United States at an 18,000 square foot warehouse facility owned by us in an unincorporated area of Los Angeles County near downtown Los Angeles, known as The Brewery.

We also contract with The Lion Brewery, Inc., a packing, or co-pack, facility in Pennsylvania, to supply us with soda products for the eastern half of the United States and nationally for soda products that we do not produce at The Brewery. Our Ginger Juice Brews are co-packed for us at a facility in Northern California. Our ice creams are co-packed for us at a dairy in upstate New York. We pack our candy products at the Brewery.

We have not been profitable during our last two fiscal years and there is no assurance that we will develop profitable operations in the future. Our net operating loss for the years ended December 31, 2005 and 2004 was \$825,955 and \$479,371, respectively. Our net operating loss for the quarters ended March 31, 2006 and 2005 was \$369,597 and \$241,386, respectively. We cannot assure you that we will have profitable operations in the future.

Our principal executive offices are located at 13000 South Spring Street, Los Angeles, California 90061. Our telephone number is (310) 217-9400. Our Internet address is [www.reedsgingerbrew.com](http://www.reedsgingerbrew.com). Information contained on our website or that is accessible through our website should not be considered to be part of this prospectus.

### **Rescission Offer**

From August 3, 2005 through April 7, 2006, we issued 333,156 shares of our common stock in connection with our initial public offering pursuant to a Registration Statement on Form SB-2. The shares issued in connection with the initial public offering may have been issued in violation of either federal or state securities laws, or both, and may be subject to rescission. In order to address this issue, we intend to make and complete the rescission offer to the holders

of these shares prior to the effective date of the registration statement relating to the public offering.

We have entered into an agreement with Mark Reed and Robert T. Reed, Jr. (the “designated purchasers”) that they would irrevocably commit to purchase up to all of the shares in the rescission offer that are tendered to us for rescission. We would assign to the designated purchasers the right to purchase any rescission shares at 100% of the amount required to pay the rescission price under applicable state law. As currently contemplated, the initial \$250,000 of rescission shares would be purchased by Mark Reed. If the number of rescission shares tendered for rescission exceeds \$250,000 of shares, Robert T. Reed, Jr. would purchase the balance of the rescission shares tendered for rescission to us. Each of the designated purchasers is a brother of Christopher J. Reed, our Chief Executive Officer, Chief Financial Officer and the Chairman of the Board of Directors. Robert T. Reed, Jr. also is our Vice President and National Sales Manager - Mainstream and a beneficial owner of approximately 7.13% of our common stock. Each of the designated purchasers may also participate in the purchase of shares of common stock to be distributed in the public offering. Since up to all of the rescission shares would be purchased by the designated purchasers, none of the rescission shares would be purchased directly by us and would not deplete proceeds from our public offering or other of our then current cash balances. The rescission shares, which may be purchased by the designated purchasers in the rescission offer, would be deemed to be registered shares for the benefit of the designated purchasers pursuant to a registration statement to be filed by us relating to the rescission offer under the Securities Act, effective as of the commencement date of the rescission offer without any further action on the part of the designated purchasers. If we are required to pay the obligation which may be created under the rescission offer, such a refund would materially and adversely effect our financial position.

Federal securities laws do not provide that a rescission offer terminates a purchaser's right to rescind a sale of stock that was not registered as required or was not otherwise exempt from such registration requirements. In connection with those offerees who rejected the rescission offer, we may continue to be liable under federal and state securities laws for up to an amount equal to the value of all shares of common stock issued in connection with the initial public offering plus any statutory interest. We also understand that the SEC and certain state regulators, including California, have requested additional information regarding the rescission offer. If it is determined that we offered securities without properly registering them under federal or state law, or securing an exemption from registration, regulators could impose monetary fines or other sanctions as provided under these laws. We believe our anticipated rescission offer could provide us with additional meritorious defenses against any future claims relating to these shares.

When the rescission offer expires, any person who did not accept the rescission offer will have freely tradable stock, subject to restrictions that may be placed on shares held by our affiliates.

There is no current market for our shares and there can be no assurance that a public market for our shares will ever develop. Further, there can be no assurance that in the event a public market for our shares were to develop that this market would be sustained over an extended period of time or that it would be of sufficient trading volume to allow ready liquidity to all investors in our shares. We intend to apply for listing of our common stock on the Nasdaq Capital Market or the American Stock Exchange following the completion of this rescission offer and our public offering, if we are able to qualify for such markets, and if not, we anticipate that US EURO Securities, Inc. will apply for quotation of our common stock on the Over the Counter Bulletin Board ("OTCBB"). However, we cannot assure you when or if a market for our common stock will be established.

We cannot give any assurances as to the number of stockholders who will accept the rescission offer. It is our intention that if any of the shares are tendered for rescission, the shares will be purchased by others and not from our funds. If we are required to pay the obligation which may be created under the rescission offer, such a refund would materially and adversely effect our financial position.

### **Our Public Offering**

We have filed a registration statement for our initial public offering and intend to continue the process of selling our shares in our public offering. We are offering to sell, on a best efforts basis, up to 2,000,000 newly issued shares of our common stock at a price of \$4.00 per share. As of the date of this prospectus, we have sold 333,156 shares resulting in gross proceeds to us of \$1,332,624, which are the subject of this rescission offer. However, whether or not these shares are repurchased under the rescission offer, the maximum number of shares which may be sold from the date of this prospectus will be reduced by the number of shares sold to the date of this prospectus.

The offering is a best efforts offering through our underwriters, US EURO Securities, Inc. and Brookstreet Securities Corporation and certain selected broker-dealers. We intend to complete this rescission offer before we recommence our public offering. We cannot give you assurances as to the number of shares which will be sold in the public offering or the price at which the common stock will trade in the future, if at all.

No minimum number of shares is required to be sold and as a result, we may only sell a nominal amount of additional shares under the offering. We will not escrow any of the proceeds received from the sale of shares before the offering terminates. Upon acceptance of a share purchase order, the proceeds from that order will be immediately available for our use.

### Summary Financial Data

The following historical financial information should be read in conjunction with the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our financial statements and the related notes included elsewhere in this prospectus. The historical results are not necessarily indicative of results to be expected for any future periods:

<b>Balance Sheet Data:</b>	<b>March 31, 2006(Unaudited )</b>		<b>December 31, 2005</b>	
Total assets	\$	5,138,925	\$	4,912,195
Current liabilities		3,769,282		3,450,269
Long-term liabilities, less current portion		1,284,732		1,312,931
Stockholders' equity		84,911		148,995

<b>Statements of Operations Data :</b>	<b>Three Months Ended March 31,</b>		<b>Years Ended December 31,</b>	
	<b>2006</b>	<b>2005</b>	<b>2005</b>	<b>2004</b>
	<b>(Unaudited)</b>	<b>(Unaudited)</b>		
Sales	\$ 1,979,272	\$ 1,817,336	\$ 9,470,285	\$ 8,978,365
Gross profit	290,396	331,049	1,724,786	1,875,328
Operating expenses	559,386	501,225	2,241,237	1,946,667
Loss from operations	(268,990)	(170,176)	(516,451)	(71,339)
Net Loss attributable to common stockholders	(369,597)	(241,386)	(855,425)	(479,371)
Net Loss per share, basic and diluted				
(1)	(0.07)	(0.05)	(0.18)	(0.10)
Weighted average shares used to compute net loss per share	5,157,077	4,726,091	4,885,151	4,726,091

(1) Does not include 39,500 shares issued following March 31, 2006 at \$4.00 per share in connection with the public offering.

## RISK FACTORS

An investment in our common stock is very risky. You should carefully consider the risk factors described below, together with all other information in this prospectus, before making an investment decision. If a market is ever established for our common stock, the trading price of our common stock could decline due to any of these risks, and you could lose all or part of your investment. You also should refer to the other information set forth in this prospectus, including our financial statements and the related notes.

### Risks Relating to Our Business

**We have a history of operating losses. If we continue to incur operating losses, we eventually may have insufficient working capital to maintain or expand operations according to our business plan.**

As of March 31, 2006, we had an accumulated deficit of \$3,628,660. For the three months ended March 31, 2006 and March 31, 2005, we had incurred losses from operations of \$268,990 and \$170,176, respectively. As of December 31, 2005, we had an accumulated deficit of \$3,259,063. For the years ended December 31, 2005 and 2004, we incurred losses from operations of \$516,451 and \$71,339, respectively. We may not generate sufficient revenues from product sales in the future to achieve profitable operations. If we are not able to achieve profitable operations at some point in the future, we eventually may have insufficient working capital to maintain our operations as we presently intend to conduct them or to fund our expansion and marketing and product development plans. In addition, our losses may increase in the future as we expand our manufacturing capabilities and fund our marketing plans and product development. These losses, among other things, have had and will continue to have an adverse effect on our working capital, total assets and stockholders' equity. If we are unable to achieve profitability, the market value of our common stock will decline and there would be a material adverse effect on our financial condition.

Our public offering is being made on a "best efforts" basis and there is no minimum number of shares we must sell beyond the number of shares that have been sold by us as of the date of this prospectus. We cannot assure you of the number of shares that we will sell in the public offering. We currently believe that our available cash resources and cash flow from operations, without any additional net proceeds from the public offering, will be sufficient to sustain our business operations for at least 13 months after the date of this prospectus. However, we would be required to reduce our level of operations, including reducing infrastructure, promotions, personnel and other operating expenses.

In addition, our ability to implement our full business expansion plan is largely dependent upon the outcome of the public offering. If we do not receive the maximum proceeds from the public offering, some or all of the elements of our expansion plan may have to be curtailed or delayed unless we are able to find alternative external sources of working capital. We would need to raise additional funds to respond to business contingencies, which may include the need to:

- fund more rapid expansion,
- fund additional marketing expenditures,
- enhance our operating infrastructure,
- respond to competitive pressures, and
- acquire other businesses.

We cannot assure you that additional financing will be available on terms favorable to us, or at all. If adequate funds are not available or if they are not available on acceptable terms, our ability to fund the growth of our operations, take

advantage of opportunities, develop products or services or otherwise respond to competitive pressures, could be significantly limited.

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**We may not be able to develop successful new beverage products which are important to our growth.**

An important part of our strategy is to increase our sales through the development of new beverage products. We cannot assure you that we will be able to continue to develop, market and distribute future beverage products that will enjoy market acceptance. The failure to continue to develop new beverage products that gain market acceptance could have an adverse impact on our growth and materially adversely affect our financial condition. We may have higher obsolescent product expense if new products fail to perform as expected due to the need to write off excess inventory of the new products.

Our results of operations may be impacted in various ways by the introduction of new products, even if they are successful, including the following:

- sales of new products could adversely impact sales of existing products,
- we may incur higher cost of goods sold and selling, general and administrative expenses in the periods when we introduce new products due to increased costs associated with the introduction and marketing of new products, most of which are expensed as incurred, and
- when we introduce new platforms and bottle sizes, we may experience increased freight and logistics costs as our co-packers adjust their facilities for the new products.

**The beverage business is highly competitive.**

The premium beverage and carbonated soft drink industries are highly competitive. Many of our competitors have substantially greater financial, marketing, personnel and other resources than we do. Competitors in the soft drink industry include bottlers and distributors of nationally advertised and marketed products, as well as chain store and private label soft drinks. The principal methods of competition include brand recognition, price and price promotion, retail space management, service to the retail trade, new product introductions, packaging changes, distribution methods, and advertising. We also compete for distributors, shelf space and customers primarily with other premium beverage companies. As additional competitors enter the field, our market share may fail to increase or may decrease.

**The loss of our largest customers would substantially reduce revenues.**

Our customers are material to our success. If we are unable to maintain good relationships with our existing customers, our business could suffer. Unilateral decisions could be taken by our distributors, and/or convenience chains, grocery chains, specialty chain stores, club stores and other customers to discontinue carrying all or any of our products that they are carrying at any time, which could cause our business to suffer.

Trader Joe's accounted for approximately 15% of our sales in 2005 and for approximately 14% of our sales in 2004. The loss of Trader Joe's as a retailer would substantially reduce our revenues unless and until we replaced that source of revenue.

**The loss of our third-party distributors could impair our operations and substantially reduce our financial results.**

We depend in large part on distributors to distribute our beverages and other products. Most of our outside distributors are not bound by written agreements with us and may discontinue their relationship with us on short notice. Most distributors handle a number of competitive products. In addition, our products are a small part of our distributors' businesses.

We continually seek to expand distribution of our products by entering into distribution arrangements with regional bottlers or other direct store delivery distributors having established sales, marketing and distribution organizations. Many of our distributors are affiliated with and manufacture and/or distribute other soda and non-carbonated brands and other beverage products. In many cases, such products compete directly with our products.

The marketing efforts of our distributors are important for our success. If our brands prove to be less attractive to our existing distributors and/or if we fail to attract additional distributors, and/or our distributors do not market and promote our products above the products of our competitors, our business, financial condition and results of operations could be adversely affected.

United Natural Foods, Inc. accounted for approximately 39% of our sales in 2005 and 2004. Management believes it could find alternative distribution channels in the event of the loss of this distributor. Such a loss may adversely affect sales in the short term.

The loss of our third-party beverage distributors could impair our operations and adversely affect our financial performance.

**Price fluctuations in, and unavailability of, raw materials that we use could adversely affect us.**

We do not enter into hedging arrangements for raw materials. Although the prices of raw materials that we use have not increased significantly in recent years, our results of operations would be adversely affected if the price of these raw materials were to rise and we were unable to pass these costs on to our customers.

We depend upon an uninterrupted supply of the ingredients for our products, a significant portion of which we obtain overseas, principally from China and Brazil. We obtain almost all of our crystallized ginger from Fiji and our Ginger Chews from Indonesia. Any decrease in the supply of these ingredients or increase in the prices of these ingredients as a result of any adverse weather conditions, pests, crop disease, interruptions of shipment or political considerations, among other reasons, could substantially increase our costs and adversely affect our financial performance.

**The loss of any of our co-packers could impair our operations and substantially reduce our financial results.**

We rely on third parties, called co-packers in our industry, to produce some of our beverages, to produce our glass bottles and to bottle some of our beverages. Our co-packing arrangements with our main co-packer are under a contract that expires in 2007. Our co-packing arrangements with other companies are on a short term basis and such co-packers may discontinue their relationship with us on short notice. While this arrangement permits us to avoid significant capital expenditures, it exposes us to various risks, including:

- our largest co-packer, Lion Brewery, accounted for approximately 63.5% of our total case production in 2005,
- if any of those co-packers were to terminate our co-packing arrangement or have difficulties in producing beverages for us, our ability to produce our beverages would be adversely affected until we were able to make alternative arrangements, and
- our business reputation would be adversely affected if any of the co-packers were to produce inferior quality products.

**We compete in an industry that is brand-conscious, so brand name recognition and acceptance of our products are critical to our success.**

Our business is substantially dependent upon awareness and market acceptance of our products and brands by our targeted consumers. In addition, our business depends on acceptance by our independent distributors of our brands as beverage brands that have the potential to provide incremental sales growth rather than reduce distributors' existing beverage sales. Although we believe that we have been relatively successful towards establishing our brands as recognizable brands in the New Age beverage industry, it may be too early in the product life cycle of these brands to determine whether our products and brands will achieve and maintain satisfactory levels of acceptance by independent

distributors and retail consumers. We believe that the success of our product name brands will also be substantially dependent upon acceptance of our product name brands. Accordingly, any failure of our brands to maintain or increase acceptance or market penetration would likely have a material adverse affect on our revenues and financial results.

**We compete in an industry characterized by rapid changes in consumer preferences and public perception, so our ability to continue to market our existing products and develop new products to satisfy our consumers' changing preferences will determine our long-term success.**

Consumers are seeking greater variety in their beverages. Our future success will depend, in part, upon our continued ability to develop and introduce different and innovative beverages. In order to retain and expand our market share, we must continue to develop and introduce different and innovative beverages and be competitive in the areas of quality and health, although there can be no assurance of our ability to do so. There is no assurance that consumers will continue to purchase our products in the future. Additionally, many of our products are considered premium products and to maintain market share during recessionary periods, we may have to reduce profit margins, which would adversely affect our results of operations. Product lifecycles for some beverage brands and/or products and/or packages may be limited to a few years before consumers' preferences change. The beverages we currently market are in varying stages of their lifecycles and there can be no assurance that such beverages will become or remain profitable for us. The beverage industry is subject to changing consumer preferences and shifts in consumer preferences may adversely affect us if we misjudge such preferences. We may be unable to achieve volume growth through product and packaging initiatives. We also may be unable to penetrate new markets. If our revenues decline, our business, financial condition and results of operations will be materially and adversely affected.

**Our quarterly operating results may fluctuate significantly because of the seasonality of our business.**

Our highest revenues occur during the spring and summer, the second and third quarters of each fiscal year. These seasonality issues may cause our financial performance to fluctuate. In addition, beverage sales can be adversely affected by sustained periods of bad weather.

**Our business is subject to many regulations and noncompliance is costly.**

The production, marketing and sale of our unique beverages, including contents, labels, caps and containers, are subject to the rules and regulations of various federal, provincial, state and local health agencies. If a regulatory authority finds that a current or future product or production run is not in compliance with any of these regulations, we may be fined, or production may be stopped, thus adversely affecting our financial conditions and operations. Similarly, any adverse publicity associated with any noncompliance may damage our reputation and our ability to successfully market our products. Furthermore, the rules and regulations are subject to change from time to time and while we closely monitor developments in this area, we have no way of anticipating whether changes in these rules and regulations will impact our business adversely. Additional or revised regulatory requirements, whether labeling, environmental, tax or otherwise, could have a material adverse effect on our financial condition and results of operations.

**Rising fuel and freight costs may have an adverse impact on our sales and earnings.**

The recent volatility in the global oil markets has resulted in rising fuel and freight prices, which many shipping companies are passing on to their customers. Our shipping costs, and particularly our fuel expenses, have been increasing and we expect these costs may continue to increase. Due to the price sensitivity of our products, we do not anticipate that we will be able to pass all of these increased costs on to our customers. The increase in fuel and freight costs could have a material adverse impact on our financial condition.

**Our manufacturing process is not patented.**

None of the manufacturing processes used in producing our products are subject to a patent or similar intellectual property protection. Our only protection against a third party using our recipes and processes is confidentiality agreements with the companies that produce our beverages and with our employees who have knowledge of such

processes. If our competitors develop substantially equivalent proprietary information or otherwise obtain access to our knowledge, we will have greater difficulty in competing with them for business, and our market share could decline.

We regard the protection of our trademarks, trade dress and trade secrets as critical to our future success. We have registered our trademarks in the United States. We also rely on a combination of laws and contractual restrictions, such as confidentiality agreements, to establish and protect our proprietary rights, trade dress and trade secrets. However, laws and contractual restrictions may not be sufficient to protect the exclusivity of our intellectual property rights, trade dress or trade secrets. Furthermore, enforcing our rights to our intellectual property could involve the expenditure of significant management and financial resources.

**We face risks associated with product liability claims and product recalls.**

Other companies in the beverage industry have experienced product liability litigation and product recalls arising primarily from defectively manufactured products or packaging. We maintain product liability insurance insuring our operations from any claims associated with product liability and we believe that the amount of this insurance is sufficient to protect us. We do not maintain product recall insurance. In the event we were to experience additional product liability or product recall claim, our business operations and financial condition could be materially and adversely affected.

On January 20, 2006, Consac Industries, Inc. (dba Long Life Teas and Long Life Beverages) filed a lawsuit in the United States District Court for the Central District of California against Reed's Inc. and Christopher Reed, Case No. CV06-0376. The complaint asserts claims for negligence, breach of contract, breach of warranty, and breach of express indemnity relating to Reed's, Inc.'s manufacture of approximately 13,000 cases of "Prism Green Tea Soda" for Consac. Consac contends that we negligently manufactured the soda resulting in at least one personal injury. Consac seeks \$2.6 million in damages, plus interest and attorneys fees. Although we believe that we have meritorious defenses to this proceeding, there can be no assurances as to its outcome. In the event we were to experience additional product liability or product recall claims, our business operations could be materially and adversely effected. An adverse outcome in this proceeding would have a material adverse effect on our business operations and financial condition.

**Our intellectual property rights are critical to our success, the loss of such rights could materially, adversely affect our business.**

We own numerous trademarks that are very important to our business. We also own the copyright in and to portions of the content on the packaging of our products. We regard our trademarks, copyrights and similar intellectual property as critical to our success and attempt to protect such property with registered and common law trademarks and copyrights, restrictions on disclosure and other actions to prevent infringement. Product packages, mechanical designs and artwork are important to our success and we would take action to protect against imitation of our packaging and trade dress and to protect our trademarks and copyrights, as necessary. However, there can be no assurance that other third parties will not infringe or misappropriate our trademarks and similar proprietary rights. If we lose some or all of our intellectual property rights, our business may be materially and adversely affected.

**If we are not able to retain the full-time services of Christopher J. Reed, it will be more difficult for us to manage our operations and our operating performance could suffer.**

Our business is dependent, to a large extent, upon the services of Christopher J. Reed, our founder, President, Chief Executive Officer, Chairman of the Board and Chief Financial Officer. We depend on Mr. Reed's creativity and leadership in running or supervising virtually all aspects of our day-to-day operations. We do not have a written employment agreement with Mr. Reed. In addition, we do not maintain key person life insurance on Mr. Reed. Therefore, in the event of the loss or unavailability of Mr. Reed to us, there can be no assurance that we would be able to locate in a timely manner or employ qualified personnel to replace him. The loss of the services of Mr. Reed or our failure to attract and retain other key personnel over time would jeopardize our ability to execute our business plan and could have a material adverse effect on our business, results of operations and financial condition.



**Our Chief Executive Officer may lack the experience and formal training to serve as our Chief Financial Officer.**

Our Chief Executive Officer, Christopher J. Reed, currently also serves as our Chief Financial Officer. However, Mr. Reed does not have any formal financial training as a Chief Financial Officer. Due to the increasing complexity of accountancy and cash management for reporting companies and the emphasis on internal controls over financial reporting, Mr. Reed's lack of experience in this area may adversely affect the future results of our operations and our ability to maintain an adequate system of internal controls over financial reporting.

**We need to manage our growth and implement and maintain procedures and controls during a time of rapid expansion in our business.**

The cost of manufacturing and packaging our products is approximately 80% of our aggregate revenues. This gross margin places pressure upon our cash flow and cash reserves when our sales increase. It is our intention to use the proceeds of our public offering to expand our business operations. If we are to expand our operations, such expansion would place a significant strain on our management, operational and financial resources. Such expansion would also require improvements in our operational, accounting and information systems, procedures and controls. If we fail to manage this anticipated expansion properly, it could divert our limited management, cash, personnel, and other resources from other responsibilities and could adversely affect our financial performance.

**We have operated without independent directors in the past.**

We have not had two independent directors through a large portion of our history. As a result, certain material agreements between related parties have not been negotiated with the oversight of independent directors and were entered into at the absolute discretion of the majority stockholder, Christopher J. Reed. Please see the "Certain Relationships and Related Transactions" section for specific details of these transactions.

**Risks Related to This Rescission Offer and Our Securities**

**We may continue to have potential liability even after this rescission offer is made.**

From August 3, 2005 through April 7, 2006, we issued 333,156 shares of our common stock in connection with our initial public offering pursuant to a Registration Statement on Form SB-2. The shares issued in connection with the initial public offering may have been issued in violation of either federal or state securities laws, or both, and may be subject to rescission. In order to address this issue, we are making this rescission offer to the holders of these shares sold in connection with our public offering.

If this rescission offer is accepted, we could be required to make aggregate payments to the holders of these shares up to \$1,332,624, plus statutory interest. This exposure is calculated by reference to the acquisition price of \$4.00 per share for the common stock in connection with the initial public offering, plus accrued interest at the applicable statutory rate. It is our intention that if any of the shares are tendered for rescission, the shares will be purchased by others and not from our funds. If we are required to pay the obligation which may be created under the rescission offer, such a refund would materially and adversely effect our financial position.

Federal securities laws do not provide that a rescission offer will terminate a purchaser's right to rescind a sale of stock that was not registered as required or was not otherwise exempt from such registration requirements. If any or all of the offerees reject the rescission offer, we may continue to be liable under federal and state securities laws for up to an amount equal to the value of all shares of common stock issued in connection with the initial public offering, plus any statutory interest we may be required to pay. We also understand that the SEC and certain state regulators, including California, have requested additional information regarding the rescission offer. If it is determined that we offered

securities without properly registering them under federal or state law, or securing an exemption from registration, regulators could impose monetary fines or other sanctions as provided under these laws.

**Your federal right of rescission may not survive if you affirmatively reject or fail to accept the rescission offer.**

If you affirmatively reject or fail to accept the rescission offer, it is unclear whether or not you will have a right of rescission under federal securities laws after the expiration of the rescission offer. The staff of the SEC is of the opinion that a person's right of rescission created under the Securities Act may survive the rescission offer.

**We cannot predict whether the amounts you would receive in the rescission offer would be greater than the fair market value of our securities.**

The amount you would receive in the rescission offer is fixed and is not tied to the fair market value of our common stock at the time the rescission offer closes. As a result, if you accept the rescission offer, you may receive less than the fair market value of the securities you would be tendering to us.

**If you do not accept the rescission offer, your shares and the shares you receive from the exercise of your options, although freely tradeable, may still remain subject to limitation on resales.**

If you affirmatively reject the rescission offer or fail to accept the rescission offer before the expiration of the rescission offer, your shares will be registered under the Securities Act and will be fully tradeable, subject to any applicable limitations set forth in Rule 144 under the Securities Act. However, you will also remain subject to any applicable terms and conditions of any agreement under which your shares were issued or otherwise relating to your shares. In addition, you will remain subject to any market standoff agreements, lockup arrangements and any other transfer restrictions entered into with respect to your shares.

**We have previously been unsuccessful in a prior public offering.**

We have previously tried to raise money in a public offering. This offering was declared effective on December 31, 2002 and was subsequently withdrawn on March 27, 2003 due to what we perceived as poor market conditions for a public offering in the economic climate at the time.

**There is not yet a public trading market for our securities and if a market develops for our securities, it could be limited, sporadic and highly volatile.**

There is currently no public market for our common stock and we cannot assure you when or if there will be a market for our common stock. We cannot assure you that an active market for our shares will be established or maintained in the future. We intend to apply for listing of our common stock on the Nasdaq Capital Market or the American Stock Exchange following the completion of this rescission offer and the public offering, if we are able to qualify for such markets, and if not, we anticipate that US EURO Securities, Inc., one of our underwriters in the public offering, will apply for quotation of our common stock on the Over the Counter Bulletin Board ("OTCBB"). However, the OTCBB is not a national securities exchange, and many companies have experienced limited liquidity when traded through this quotation system. Therefore, if you purchase shares of our common stock and later decide to sell the shares, you may have difficulty selling the shares. Even if a market for our common stock is established, stockholders may have to sell our stock at prices substantially lower than the price they paid for it or might otherwise receive than if a broad public market existed.

In addition, if a market develops for our common stock, the market price of our common stock may be volatile, which could cause the value of your investment to decline. Securities markets experience significant price and volume fluctuations. This market volatility, as well as general economic conditions, could cause the market price of our common stock to fluctuate substantially. Many factors that are beyond our control may significantly affect the market price of our shares. These factors include:

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- price and volume fluctuations in the stock markets generally,
- changes in our earnings or variations in operating results,

- any shortfall in revenue or increase in losses from levels expected by securities analysts,
- changes in regulatory policies or law,
- operating performance of companies comparable to us, and
- general economic trends and other external factors.

Such factors may cause the market price of our common stock to decrease significantly. You may be unable to sell your shares of common stock at or above the initial public offering price.

**Since there is no minimum number of shares in our public offering which must be subscribed for before we can use the proceeds from sales, our expansion plans will be affected by the number of shares actually sold.**

The speed with which we implement our expansion plans will depend, to a large degree, on the amount of funds available for expansion. Such funds may be provided by the sale of common stock in our public offering, our existing lines of credit, and revenues from sales, future loans or otherwise. If we sell less than all the shares in the public offering, our ability to implement our expansion plans described in this prospectus could be delayed, depending on the amount of other funds available to us for such purposes.

**Future financings could adversely affect your ownership interest and rights in comparison with those of other security holders.**

Our board of directors has the power to issue additional shares of common or preferred stock without stockholder approval. If additional funds are raised through the issuance of equity or convertible debt securities, the percentage ownership of our existing stockholders will be reduced, and these newly issued securities may have rights, preferences or privileges senior to those of existing stockholders, including, those persons acquiring shares in our public offering.

If we issue any additional common stock or securities convertible into common stock, such issuance will reduce the proportionate ownership and voting power of each other stockholder. In addition, such stock issuances might result in a reduction of the book value of our common stock.

**Because Christopher J. Reed controls a majority of our stock, he can control the outcome, or greatly influence the outcome, of all matters on which stockholders vote.**

Christopher J. Reed, our President, Chief Executive Officer, Chairman of the Board and Chief Financial Officer owns, before the commencement of our public offering, approximately 60% of our outstanding voting stock. If all the shares in our public offering are sold, Mr. Reed will own approximately 46% of our outstanding voting stock. If 1,000,000 shares in our public offering (50%) are sold, Mr. Reed will own approximately 54% of our outstanding voting stock. Therefore, Mr. Reed will be able to control the outcome, or greatly influence the outcome, on all matters requiring stockholder approval, including the election of directors, amendment of our certificate of incorporation, and any merger, consolidation or sale of all or substantially all of our assets or other transactions resulting in a change of control of our company. In addition, as our Chairman and Chief Executive Officer, Mr. Reed has and will continue to have significant influence over our strategy, technology and other matters. Mr. Reed's interests may not always coincide with the interests of other holders of our common stock.

**A substantial number of our shares will be available for sale in the public market after the offering and sales of those shares could adversely affect our stock price.**

Sales of a substantial number of shares of common stock into the public market after our public offering, or the perception that such sales could occur, could substantially reduce our stock price in any public market, and could impair our ability to obtain capital through a subsequent financing of our securities. After our public offering, we will have 6,994,953 shares of common stock outstanding if all 2,000,000 shares in the offering are sold and 5,994,953 shares of common stock outstanding if 1,000,000 shares in the offering (50%) are sold. All the shares of common stock sold in the public offering will be freely tradable without restriction or further registration required under federal securities laws.

In addition, we have issued and outstanding options and warrants that may be exercised into 904,241 shares of common stock, 136,158 shares of common stock issuable upon conversion of principal and accrued interest on certain debt at March 31, 2006 and 58,940 shares of Series A preferred stock that may be converted into 235,760 shares of common stock. In addition, our outstanding shares of Series A preferred stock bear a dividend of 5% per year, or approximately \$29,470 per year. We have the option to pay the dividend in shares of our common stock. In 2005, we paid the dividend in an aggregate of 7,362 shares of common stock, and anticipate that we will be obligated to issue at least this many shares annually to the holders of the Series A preferred stock so long as such shares are issued and outstanding. We also have 200,000 shares reserved for future issuance under the underwriters' warrant (including 33,316 shares underlying underwriters' warrants which we have agreed to issue to the underwriters relating to the sale of 333,156 shares sold as of the date of this prospectus).

Of the shares of our common stock currently outstanding, 4,240,500 shares are "restricted securities" under the Securities Act. Some of these "restricted securities" will be subject to restrictions on the timing, manner, and volume of sales of such shares.

**Our common stock may become subject to "penny stock" regulations that may affect the liquidity of our common stock.**

Our common stock may become subject to the rules adopted by the SEC, that regulates broker-dealer practices in connection with transactions in "penny stocks." Penny stocks are generally equity securities with a price of less than \$5.00 (other than securities registered on certain national securities exchanges or quoted on the NASDAQ Stock Market, provided that current price and volume information with respect to transactions in such securities is provided by the exchange or system).

The penny stock rules require that a broker-dealer, prior to a transaction in a penny stock not otherwise exempt from those rules, deliver a standardized risk disclosure document prepared by the SEC, which contains the following:

- a description of the nature and level of risk in the market for penny stocks in both public offerings and secondary trading,
- a description of the broker's or dealer's duties to the customer and of the rights and remedies available to the customer with respect to violation of such duties or other requirements of securities laws,
- a brief, clear, narrative description of a dealer market, including "bid" and "ask" prices for penny stocks and significance of the spread between the "bid" and "ask" price,
- a toll-free telephone number for inquiries on disciplinary actions; definitions of significant terms in the disclosure document or in the conduct of trading in penny stocks, and
- such other information and is in such form (including language, type, size and format), as the SEC shall require by rule or regulation.

Prior to effecting any transaction in penny stock, the broker-dealer also must provide the customer the following:

- the bid and offer quotations for the penny stock,
- the compensation of the broker-dealer and its salesperson in the transaction,

- the number of shares to which such bid and ask prices apply, or other comparable information relating to the depth and liquidity of the market for such stock,
- the liquidity of the market for such stock, and
- monthly account statements showing the market value of each penny stock held in the customer's account.

In addition, the penny stock rules require that prior to a transaction in a penny stock not otherwise exempt from those rules, the broker-dealer must make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser's written acknowledgment of the receipt of a risk disclosure statement, a written agreement to transactions involving penny stocks, and a signed and dated copy of a written suitability statement. These disclosure requirements may have the effect of reducing the trading activity in the secondary market for a stock such as our common stock if it is subject to the penny stock rules.

## RESCISSION OFFER

### Background

From August 3, 2005 through April 7, 2006, we issued 333,156 shares of our common stock in connection with our initial public offering pursuant to a Registration Statement on Form SB-2 (333-120451). The shares we issued in connection with the initial public offering were not issued pursuant to an effective registration statement and may not have been exempt from the registration or qualification requirements under the Securities Act of 1933 and under those state securities laws that provide an exemption from such requirements. We became aware that the shares may not have been issued pursuant to an effective registration statement. Because the shares were not issued pursuant to an effective registration statement and there was no available exemption from the registration requirements of the Securities Act or the registration or qualification requirements of the various states for such issuances, the shares issued in connection with the initial public offering may have been issued in violation of either federal or state securities laws, or both, and may be subject to rescission. In order to address this issue, we are making this rescission offer to all holders of any outstanding shares who we believe may be entitled to argue for rescission. Pursuant to this rescission offer, we will offer to repurchase these shares then outstanding from the holders. We will be making this rescission offer to 167 persons who are or were residents of California, Colorado, Connecticut, Hawaii, Illinois, Indiana, Louisiana, Massachusetts, Missouri, Montana, New York, Oregon, South Carolina, Utah, Vermont, Virginia and Washington, and the country of Israel. If our rescission offer is accepted by all offerees, we could be required to make an aggregate payment to the holders of these shares of up to approximately \$1,332,624, plus statutory interest.

Our anticipated rescission offer will cover an aggregate of 333,156 shares of common stock issued in connection with our initial public offering. These securities represent all of the shares issued in connection with the initial public offering. We intend to make and complete the rescission offer to the holders of these shares prior to the effective date of the registration statement relating to the public offering. The rescission offer will be kept open for at least 30 days and will be registered under the Securities Act and qualified in each state where such qualification is required under applicable state securities laws.

We will offer to rescind prior purchases of our common stock that are subject to the rescission offer for an amount equal to the price paid for the shares plus interest, calculated from the date of the purchase through the date on which the rescission offer expires, at the applicable statutory interest rate per year.

The rescission offer will be kept open for 30 days until \_\_\_\_\_, 2006 and will be registered under the Securities Act and qualified in each state where such qualification is required under applicable state securities laws.

If all holders of shares of our common stock subject to the rescission offer elected to accept our rescission offer, we would be required to make an aggregate payment of approximately \$1,332,624, plus statutory interest, to these holders. We believe this amount represents our aggregate exposure under federal and state securities laws for not seeking to register or qualify these shares or options under these laws. Our anticipated rescission offers to be made in the various states in which we may not have complied with applicable securities laws will cover an aggregate of 333,156 shares of common stock.

Our making this rescission offer may not terminate a purchaser's right to rescind a sale of securities that was not registered or qualified under the Securities Act or applicable state securities laws and was not otherwise exempt from registration or qualification. Accordingly, should the rescission offer be rejected by any or all offerees, we may continue to be contingently liable under the Securities Act and applicable state securities laws for the purchase price of these shares up to an aggregate amount of approximately \$1,332,624, plus statutory interest. If a court were to impose a greater remedy, our exposure as a result of the rescission offer could be higher. In addition, if it is determined that we offered securities without properly registering them under federal or state law, or securing an exemption from registration, regulators could impose monetary fines or other sanctions as provided under these laws. We understand that the SEC and certain state regulators, including California, have requested additional information relating to the rescission offer.

We have filed a registration statement for our initial public offering and intend to continue the process of selling our shares in our public offering at a purchase price of \$4.00 per share. The public offering is a best efforts offering through our underwriters, US EURO Securities, Inc. and Brookstreet Securities Corporation and certain selected broker-dealers. We intend to complete this rescission offer before we recommence our public offering. We cannot give you assurances as to the number of shares which will be sold in the public offering or the price at which the common stock will trade in the future, if at all.

There is no current public market for our shares and there is no assurance that a public market for our shares will ever develop. In the event a public market for our shares does not develop, holders of our common stock may be unable to sell the shares for an extended period of time. We intend to apply for listing of our common stock on the Nasdaq Capital Market or the American Stock Exchange following the completion of this rescission offer and our public offering, if we are able to qualify for such markets, and if not, we anticipate that US EURO Securities, Inc. will apply for quotation of our common stock on the Over the Counter Bulletin Board ("OTCBB"). However, we cannot assure you when or if a market for our common stock will be established.

### **Rescission Offer and Price**

We are offering to rescind the issuance of 333,156 shares of common stock which we issued in our initial public offering. By making this rescission offer, we are not waiving any applicable statutes of limitations.

We will be making this rescission offer to 167 persons who are or were residents of California, Colorado, Connecticut, Hawaii, Illinois, Indiana, Louisiana, Massachusetts, Missouri, Montana, New York, Oregon, South Carolina, Utah, Vermont, Virginia and Washington, and the country of Israel.

If you accept our rescission offer and you hold shares of our common stock, we will repurchase the shares you hold that are subject to the rescission offer at the price per share paid (\$4.00), plus interest at the current statutory rate per year mandated by your state of residence, from the date of purchase through the date that the rescission offer expires.

If you accept our rescission offer, you will be entitled to receive interest at the applicable statutory interest rate per year in accordance with your state of residence. You will not, however, be entitled to any payments for interest or otherwise unless you affirmatively elect to participate in the offer. We intend to use the legal rates of interest for the repurchase of the shares and options based on the state of residence of the stockholder. These interest rates are as follows:

State	Interest Rate	State	Interest Rate
California	7%	Montana	10%
Colorado	8%	New York *	7%
Connecticut	6%	Oregon	9%
Hawaii	10%	South Carolina	11.25%
Illinois	10%	Utah	12%
Indiana	8%	Vermont	12%
Louisiana	8%	Virginia	6%
Massachusetts	6%	Washington	8%
Missouri	8%	Israel *	7%

\* New York and Israeli law do not provide a specific interest rate. For purposes of the rescission offer, we are applying the rate of interest of California (our principal place of business) to calculate the consideration to be received by New York and Israeli residents who may be entitled to rescission rights.

### Acceptance

You may accept the rescission offer by completing and signing the enclosed election form indicating the shares and options to be repurchased and delivering a stock power representing the shares you are surrendering for repurchase, on or before the close of business on \_\_\_\_\_, 2006, which date and time we refer to in this document as the expiration date. All acceptances of the rescission offer will be deemed to be effective on the expiration date and the right to accept the rescission offer will terminate on the expiration date. Acceptances or rejections may be revoked in a written notice to us, to the attention of Christopher J. Reed, 13000 South Spring Street, Los Angeles, California 90061, which is received prior to the expiration date. Within 15 business days after the expiration date, we will pay for any securities as to which the rescission offer has been validly accepted.

The rescission offer will expire at 5:00 p.m., Pacific Time, on \_\_\_\_\_, 2006. If you submit an election form after the expiration time, regardless of whether your form is otherwise complete, your election will not be accepted, and you will be deemed to have rejected our rescission offer.

Neither we nor our officers and directors make any recommendations to you with respect to the rescission offer contained herein. You are urged to read the rescission offer carefully and to make an independent evaluation with respect to its terms.

IF PERSONS DESIRING TO ACCEPT THE RESCISSION OFFER INTEND TO MAKE USE OF THE MAIL TO RETURN THEIR STOCK POWERS, INSURED REGISTERED MAIL, RETURN RECEIPT REQUESTED, IS RECOMMENDED.

### Rejection or Failure to Affirmatively Accept

If you fail to accept, or if you affirmatively reject the rescission offer by so indicating on the enclosed election form, you will retain ownership of the shares which you purchased in connection with our initial public offering and you will not receive any cash for those securities in connection with the rescission offer. Your shares will be registered and fully tradeable under the Securities Act, unless you are one of our affiliates within the meaning of Rule 144. Your shares will remain subject to any applicable terms and conditions of the original agreement under which they were issued and any subsequent agreement relating to such shares and any other transfer restrictions entered into with respect to your shares.

### Solicitation

We have not retained, nor do we intend to retain, any person to make solicitations or recommendations to you in connection with the rescission offer.

## Effect of Rescission Offer

It is unclear whether the rescission offer will terminate our liability, if any, for failure to register or qualify the issuance of the securities under either federal or state securities laws. Accordingly, should the rescission offer be rejected by any or all offerees, we may continue to be contingently liable under the Securities Act of 1933 and applicable state securities laws for the purchase price of these shares and the value of the options up to an aggregate amount of approximately \$1,332,624, plus statutory interest. If you are a stockholder who acquired shares of our common stock in connection with our initial public offering that are subject to the rescission offer, it is possible that you may continue to have rights under common law or fraud in the state in which the potential securities violation with respect to your shares occurred. If a court were to impose a greater remedy, our liability as a result of the potential securities violations would be higher.

Regardless of whether you accept the rescission offer, we believe that any remedies you may have after the rescission offer expires would not be greater than an amount you would receive in the rescission offer.

Below is a discussion of our contingent liability in those states where we may have potential securities laws violations resulting from our issuance of the shares, which are covered by the rescission offer. Each state has different laws with respect to rights under common law and fraud and the following discussion of state law does not relate to the antifraud provisions of applicable securities laws or rights under common law or equity:

### California

None of the shares sold in the state of California may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Corporate Securities Law of 1968 of California.

Under California law, an issuer is civilly liable to a purchaser of its securities sold in violation of the registration or qualification requirements of the California Corporate Securities Law of 1968. The purchaser may sue to recover the consideration paid for such securities with interest at 7% per year, less the amount of any income received from ownership of the securities, upon the tender of such securities at any time prior to the earlier of the two year anniversary of the noncompliance with the registration or qualification requirements or the one year anniversary of the discovery by the purchaser of the facts constituting such noncompliance.

However, we may terminate the rights of the purchasers to seek additional remedies under the California Corporate Securities Law of 1968 by making a written rescission offer before suit is commenced by the purchaser, approved as to form by the California Commissioner of Corporations where the offer:

- states the respect in which liability under the registration or qualification requirements may have arisen,
- offers to repurchase the securities for a cash price payable upon delivery of the securities, or offers to pay the purchaser an amount in cash equal in either case to the amount recoverable by the purchaser, or offers to rescind the transaction by putting the parties back in the same position as before the transaction,
- provides that such offer may be accepted by the purchaser at any time within a specified period of not less than 30 days after the date of receipt of the offer unless rejected earlier during such periods by the purchaser,
- sets forth the provisions of the rescission offer requirements under the California Corporate Securities Law of 1968, and
- contains such other information as the California Commissioner of Corporations may require by rule or order.



If the purchaser fails to accept such offer in writing within the specified time period of not less than 30 days after the date of receipt of the offer, that purchaser will no longer have any right of rescission under California law.

We must also file with the California Commissioner of Corporations, in such form as the California Commissioner of Corporations prescribes by rule, an irrevocable consent appointing the Commissioner of Corporations or its successor in office to be our attorney to receive services for any lawful process in any noncriminal suit, action or proceeding against us or our successor, which arises under California law after the consent has been filed with all the same force and validity as if served personally on us.

We believe this rescission offer complies in all material respects with the rescission offer requirements of the California Corporate Securities Law of 1968.

### **Colorado**

None of the shares sold in the state of Colorado may have been issued pursuant to an effective registration statement or an applicable exemption from the registration requirements set forth in the Colorado Securities Act.

Under Colorado law, an issuer is civilly liable to a purchaser who buys securities sold by the issuer in violation of the registration requirements of the Colorado Securities Act. The issuer is liable to the purchaser for the consideration paid for the security, plus interest at 8% per year, costs and reasonable attorney fees, less the amount of any income received on the security, upon tender of the security. If the purchaser no longer owns the security, the issuer is liable to such purchaser for damages. The purchaser must bring the action within two years after the contract of sale.

However, we may terminate the rights of the purchasers to seek additional remedies under the Colorado Securities Act by making a written rescission offer, before suit, to repurchase the security for cash, payable on delivery of the security, in an amount equal to the consideration paid plus interest at 8% per year, less the amount of any income received on the security, or for damages, if the purchaser no longer owns the security. The offer must be accepted by the purchaser within 30 days after the offer is mailed by the issuer. The purchaser will no longer have a right of rescission under Colorado law if the purchaser fails to accept such offer within the period of time specified.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Colorado Securities Act.

### **Connecticut**

None of the shares sold in the state of Connecticut may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Securities and Business Investments Law of Connecticut.

Under the Securities and Business Investments Law of Connecticut, a person that offers or sells securities in violation of the registration requirements of the Securities and Business Investments Law of Connecticut is civilly liable to the purchaser of the security. The purchaser may sue to recover the consideration paid for the security, together with interest at 8% per year, costs and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security. If the purchaser no longer owns the security, the purchaser may sue for damages. The purchaser must bring the action for violation of the registration requirements within two years after the date of the contract of sale.

However, we may terminate the rights of the purchasers to seek additional remedies under the Securities and Business Investments Law of Connecticut by making a written rescission offer, before suit and at a time when the purchaser still owned the security, to refund the consideration, paid together with interest at 6% per year, less the amount of any income received on the security, and he failed to accept the offer within thirty days of its receipt. The purchaser also

may not bring such an action if the purchaser received such an offer before bringing a cause of action and at a time when the purchaser did not own the security, unless the purchaser rejected the offer in writing within thirty days of its receipt.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Securities and Business Investments Law of Connecticut.

### **Hawaii**

None of the shares sold in the state of Hawaii may have been issued pursuant to an effective registration statement or an applicable exemption from the registration requirements set forth in the Hawaii Uniform Securities Act.

Under Hawaii law, an issuer is civilly liable to purchasers of securities sold by the issuer in violation of the Hawaii Uniform Securities Act upon tender of the securities sold or of the contract made. The issuer is liable for the full amount paid by the purchaser, with interest at 10% per year, plus all taxable court costs and reasonable attorney's fees. The purchaser must bring an action to recover the purchase price within five years from the date of the sale or within two years from the discovery of facts constituting the violation, but in any event no later than seven years from the date of sale.

However, we may terminate the rights of the purchasers to seek additional remedies under the Hawaii Uniform Securities Act by making a written rescission offer, before suit, to take back the security in question and refund the full amount paid by the purchaser, plus interest at 10% per year, less the amount of any income received by the purchaser from the securities, and the purchaser refuses or fails to accept such offer within 30 days. The purchaser will no longer have a right of rescission under Hawaii law if the purchaser fails to accept such offer within the period of time specified.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Hawaii Uniform Securities Act.

### **Illinois**

None of the shares sold in the state of Illinois may have been issued pursuant to an effective registration statement or an applicable exemption from the registration requirements set forth in the Illinois Securities Law of 1953.

Under the Illinois Securities Law, an issuer who sells securities in violation of the Illinois Securities Law of 1953 is civilly liable to purchasers of such securities for the full amount paid, plus interest at 10% per year, less any income or other amounts received by the purchaser on the securities, upon offer to tender the securities sold. If the purchaser no longer owns the securities, the issuer is liable for the above amount less any amounts received by the purchaser for or on account of the disposition of the securities. The purchaser must bring an action for relief within three years from the date of sale.

However, we may terminate the rights of the purchasers to seek additional remedies under the Illinois Securities Law of 1953 by making a written rescission offer, before suit, to repurchase the securities, and the purchaser fails to accept the offer within 15 days from the date the offer is received. The offer must be an offer to repurchase the securities for a price equal to the full amount paid, plus interest at 10% per year, less any income thereon. The offer must advise the purchaser of his or her rights, state the period of time in which the offer may be accepted, and contain such further information, if any, as the Secretary of State may prescribe. The purchaser will no longer have a right of rescission under Illinois law if the purchaser fails to accept such offer within the period of time specified.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Illinois Securities Law of 1953.



## Indiana

None of the shares sold in the state of Indiana may have been issued pursuant to an effective registration statement or an applicable exemption from the registration requirements of the Indiana Securities Act.

A person who offers or sells a security in violation of the registration requirements of the Indiana Securities Act is civilly liable to the purchaser of the security. The purchaser may sue to recover the consideration paid, together with interest at 8% per year, plus costs, and reasonable attorneys' fees. If the purchaser no longer owns the security, the amount of cash or other property received on the security upon the sale of the security should be deducted, or the purchaser may bring an action for damages. The purchaser must bring the action for violation of the registration requirements within three years after discovery of the violation by the person bringing the action.

However, we may terminate the rights of the purchasers to seek additional remedies under the Indiana Securities Act by making a written rescission offer, before suit, and at a time when the purchaser owned the security, to refund the consideration paid together with interest at 8% per year, less the amount of any income received on the security, and the purchaser failed to accept the offer within 30 days of its receipt. If the purchaser did not own the security, the purchaser may not commence such an action unless the purchaser rejected the offer within 30 days of receipt.

In order to conduct a rescission offer, unless otherwise ordered by the Securities Commissioner of Indiana in a particular case the issuer of the security must adhere to the following:

- The offer must be in writing and the exact text must be submitted to and approved by the Securities Commissioner in advance.
- The offer must be worded so that the subscriber must answer affirmatively that the subscriber either accepts or rejects the rescission offer.
  - The offer must be mailed to the address of the subscriber which appears on the books of the transfer agent.
- The subscriber shall have 30 days from the date of receipt to accept the offer (acceptance period). Acceptance or rejection shall be effective upon mailing by the subscriber.
  - If a subscriber fails to respond, the investment will be deemed rescinded.
- During the acceptance period no other communications other than reminders that the rescission letter be returned may be initiated by the issuer or its agents with any subscribers to whom the rescission offer is being made.
- At the close of the acceptance period, the issuer shall file with the Securities Commissioner a report indicating the date the acceptance period ended, the number of subscribers to whom the offer was made, and the number of subscribers who accepted the rescission offer and number of shares rescinded.
  - Resumption of offers and/or sales shall not take place until the Securities Commissioner so orders.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Indiana Securities Act.

## Louisiana

None of the shares sold in the state of Louisiana may have been issued pursuant to an effective registration statement or an applicable exemption from the registration requirements set forth in the Louisiana Securities Law.

Under Louisiana law, an issuer is civilly liable to a purchaser of securities sold in violation of the registration requirements of the Louisiana Securities Law. The purchaser may sue to recover the consideration paid in cash, plus interest at 8% per year, less the amount of any income received thereon, together with all taxable court costs and reasonable attorney's fees, upon the tender of the security at any time before the entry of judgment, or for damages, if the purchaser no longer owns the security. The purchaser must bring suit within two years from the date of the sale.

However, we may terminate the rights of the purchasers to seek additional remedies under the Louisiana Securities Law by making a written rescission offer, before suit and at a time when the purchaser owned the security, to repay in cash or by certified or official bank check, within 30 days from the date of acceptance of such offer in exchange for the securities, the fair value of the consideration paid, plus interest at 8% per year, less the amount of any income received on the security, and the purchaser fails to accept the offer within 30 days of receiving it. If the written offer is provided to the purchaser at a time when the purchaser no longer owns the security, then the repayment amount is equal to the difference between the fair value of the consideration the purchaser gave for the security and the fair value of the security at the time the purchaser disposed of it, plus interest at 8% per year, less the amount of any income received on the security. No such written offer will be effective unless, if it were an offer to sell securities, it would be exempt under Section 51:709 of the Louisiana Securities Law, or, if registration would have been required, such rescission offer has been registered and effected under the Louisiana Securities Law. The purchaser will no longer have a right of rescission under the Louisiana law if the purchaser fails to accept such offer within the period of time specified.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Louisiana Securities Law.

### **Massachusetts**

None of the shares sold in the state of Massachusetts may have been issued pursuant to an effective registration statement or an applicable exemption from the registration requirements set forth in the Massachusetts Uniform Securities Act.

Under Massachusetts law, an issuer is civilly liable to a purchaser of its securities sold in violation of the registration requirements. The purchaser may sue to recover the consideration paid, plus interest at 6% per year, costs and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages if the purchaser no longer owns the security. The purchaser must bring suit within four years after the purchaser discovers the violation in question.

However, we may terminate the rights of the purchasers to seek additional remedies under the Massachusetts Uniform Securities Act by making a written rescission offer, before suit and at a time when the purchaser owned the security, to refund the consideration paid with interest at 6% per year, less the amount of any income received on the security, and the purchaser fails to accept the offer within 30 days of receiving it, or if the purchaser receives such an offer before suit and at a time when the purchaser did not own the security, unless the purchaser rejects the offer in writing within 30 days of receiving it. The purchaser will no longer have a right of rescission under Massachusetts law if the purchaser fails to accept such offer within the period of time specified.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Massachusetts Uniform Securities Act.

### **Missouri**

None of the shares sold in the state of Missouri may have been issued pursuant to an effective registration statement or an applicable exemption from the registration requirements set forth in the Missouri Securities Act of 2003.

Under Missouri law, an issuer is civilly liable to persons who purchase securities sold by the issuer in violation of the registration requirements. The purchaser may sue to recover the consideration paid for the security, less the amount of any income received on the security, and interest at 8% per year, costs and reasonable attorneys' fees, upon the tender of the security, or for actual damages. The purchaser must bring the action within one year after the violation occurs.

However, we may terminate the rights of the purchasers to seek additional remedies under the Missouri Securities Act of 2003 by making a written rescission offer, before suit, which states the respect in which liability may have arisen, fairly advises the purchaser of the purchaser's rights in connection with the offer and provides any financial or other information necessary to correct all material misrepresentations or omissions in the information that was required to be furnished to the purchaser at the time of the purchase. The offer must present an offer to repurchase the security for cash, payable on delivery of the security, equal to the consideration paid, plus interest at 8% per year, less the amount of any income received on the security, or for damages if the purchaser no longer owns the security. The offer must be accepted by the purchaser within 30 days after the date it is received. The purchaser will no longer have a right of rescission under Missouri law if the purchaser fails to accept such offer within the period of time specified.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Missouri Securities Act of 2003.

### **Montana**

None of the shares sold in the state of Montana may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Securities Act of Montana.

Under Montana law, a person who offers or sells securities in violation of the registration requirements is civilly liable to the person buying the security. The purchaser may sue to recover the consideration paid for the security, together with interest at 10% per year, costs, and reasonable attorneys' fees less the amount of any income received on the security, upon the tender of the security. The purchaser may also sue for damages if he no longer owns the security. The purchaser must bring the action for violation of the registration requirements within two years after the violation occurs.

However, we may terminate the rights of the purchasers to seek additional remedies under the Securities Act of Montana by making a written rescission offer, before suit and at a time when he owned the security, to refund the consideration paid, together with interest at 10% per year, less the amount of any income received on the security and the purchaser failed to accept the offer within 30 days of its receipt. If the purchaser no longer owns the security, the purchaser may not commence such an action if he received a written offer in the amount that would be recoverable if the purchaser did own the security upon a tender, less the value of the security when the purchaser disposed of it, plus interest at 10% per year.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Securities Act of Montana.

### **New York**

Under New York law, there is no requirement to register or qualify securities, and there is no provision for rescission offers. We applied for an exemption under New York law from the broker-dealer registration and securities issuance requirements with the State of New York to issue the shares to you in the public offering without registration or qualification. Because we applied for such an exemption, we believe that the shares of common stock issued by us in the state of New York were issued pursuant to an exemption from registration or qualification under New York law.

If shares were issued to you in New York, you do not have a right of rescission under New York law. Accordingly, the rescission offer is being made with respect to individuals who purchased shares of our common stock in New York, pursuant only to federal rights of rescission. The acceptance or non-acceptance of the rescission offer by these individuals will have no effect under New York law.



## **Oregon**

None of the shares sold in the state of Oregon may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Oregon Securities Law.

Under Oregon law, a person who offers or sells securities in violation of the registration requirements is civilly liable to the person buying the security. If the purchaser still owns the security, the purchaser may sue to recover, upon tender of the security, the consideration paid for the security, plus interest at 9% per year, less any amount received on the security. If the purchaser no longer owns the security, the purchaser may sue to recover damages in the amount that would be recoverable upon a tender, less the value of the security when the purchaser disposed of it, and less interest on such value from the date of disposition. The purchaser must bring the action for violation of the registration requirements within three years after the sale of the security.

However, we may terminate the rights of the purchasers to seek additional remedies under the Oregon Securities Law by making a written rescission offer, before suit, containing both (i) an offer to pay the purchaser the consideration paid for the security, interest at 9% per year, less any amount received on the security, and (ii) a statement of the effect on the purchaser's rights of failure to respond. An action for violation of the registration requirements may be commenced after receipt of a notice, if the purchaser owned the security when the notice was received, accepted the payment offer within 30 days after its receipt, and has not been paid the full amount offered; or if the purchaser did not own the security when the notice was received, and within 30 days after receipt, gave written notice of inability to tender back the security.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Oregon Securities Law.

## **South Carolina**

None of the shares sold in the state of South Carolina may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements of the South Carolina Uniform Securities Act of 2005.

Under South Carolina law, a person who offers or sells securities in violation of the registration requirements is civilly liable to the person buying the security. The purchaser may sue to recover the consideration paid for the security, less the amount of any income received on the security, and interest at 11.25% per year, costs and reasonable attorneys' fees determined by the court, upon the tender of the security. If the purchaser no longer owns the security, the purchaser may sue for actual damages that would be recoverable upon a tender less the value of the security when the purchaser disposed of it, plus interest at 11.25% per year, costs and reasonable attorneys' fees determined by the court. Tender may be made at any time before entry of judgment. Tender requires only notice in a record of ownership of the security and willingness to exchange the security for the amount specified. The legal rate of interest payable under South Carolina law is based on the prime rate as listed in the first edition of the Wall Street Journal published for each calendar year for which the damages are awarded, plus four percentage points, compounded annually. For purposes of the rescission offer, the rate of interest applicable to the rescission offer will be based on the prime interest rate (7.25%) listed in the first edition of the Wall Street Journal published in calendar year 2006. A person must bring an action for violation of the registration requirements within three years after the violation occurred.

However, we may terminate the rights of the purchasers to seek additional remedies under South Carolina Uniform Securities Act of 2005 by making a written rescission offer, before suit stating the respect in which liability may have arisen, and fairly advising the purchaser their rights in connection with the offer, and any financial or other information that was required to be furnished to that person at the time of the purchase of the securities. The rescission

must include an offer to repurchase the security for cash, payable upon delivery of the security, equal to the consideration paid, including all commissions and fees, plus interest at 11.25% per year, less the amount of any income received on the security. If the purchaser no longer owns the security, the offer may be to pay the purchaser upon acceptance of the offer, damages in an amount that would be recoverable upon a tender, less the value of the security when the purchaser disposed of it, plus interest at 11.25% per year. The offer must be accepted by the purchaser within 30 days after the date of its receipt by the purchaser. The offeror must have the present ability to pay the amount offered or to tender the security. Finally, the offer must be delivered to the purchaser, or sent in a manner that ensures receipt by the purchaser, and the purchaser must accept the offer and be paid in accordance with the terms of the offer.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the South Carolina Uniform Securities Act of 2005.

### **Utah**

None of the shares sold in the state of Utah may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Utah Uniform Securities Act.

Under Utah law, a person who offers or sells securities in violation of the registration requirements is civilly liable to the person buying the security. The purchaser may sue to recover the consideration paid for the security, together with interest at 12% per year, costs and reasonable attorney's fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he no longer owns the security. Damages are the amount that would be recoverable upon a tender less the value of the security when the buyer disposed of it, and interest at 12% per year. If the purchaser can show that the violation was reckless or intentional, the purchaser may bring suit for three times the consideration paid for the security, together with interest, costs and attorney's fees. The purchaser must bring the action for violation of the registration requirements within four years after the act or transaction constituting the violation, or within two years after the discovery by the purchaser of the facts constituting the violation, whichever expires first.

However, we may terminate the rights of the purchasers to seek additional remedies under the Utah Uniform Securities Act by making a written rescission offer, before suit and at a time when he owned the security, to refund the consideration paid together with interest at 12% per year, less the amount of any income received on the security, and he failed to accept the offer within 30 days of receipt. If the purchaser no longer owns the security, he may not commence such an action if he received a written offer before suit, unless he rejected the offer in writing within 30 days of its receipt.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Utah Uniform Securities Act.

### **Vermont**

None of the shares sold in the state of Vermont may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Vermont Uniform Securities Act.

Under Vermont law, a person who offers or sells securities in violation of the registration requirements is civilly liable to the person buying the security. The purchaser of the security may sue to recover the consideration paid for the security, together with interest at 12% per year, costs and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages plus costs and reasonable attorneys' fees if the purchaser no longer owns the securities. Damages are the amount that would be recoverable upon a tender, less the value of the security when the purchaser disposed of it, and interest at 12% per year. Tender shall require only notice of willingness to exchange the security for the amount specified. The purchaser must bring the action for violation of the registration requirements within three years after the act, omission or transaction constituting the violation, or within two years after the violation is or reasonably should have been discovered, whichever occurs later, but not later than six years after the act, omission or transaction constituting the violation.

Under Vermont law, effective as of July 1, 2006, an action may not be maintained if before the action is instituted, the purchaser receives an offer stating the respect in which the civil liability may have arisen and fairly advising the purchaser of that person's rights in connection with the offer, and any financial or other information necessary to correct all material misrepresentations or omissions in the information that was required by this chapter to be

furnished to that person at the time of the purchase. The offer must be to repurchase the security for cash, payable on delivery of the security, equal to the consideration paid, together with interest at the rate of 12% per year, less the amount of any income received on the security, or, if the purchaser no longer owns the security, an offer to pay the purchaser upon acceptance of the offer damages in an amount that would be recoverable upon a tender, less the value of the security when the purchaser disposed of it, together with interest at the rate of 12% per year. The offer must be accepted by the purchaser within 30 days of its receipt, the offeror must have the present ability to pay the amount offered or to tender the security, the offer must be delivered to the purchaser in a manner that ensures receipt by the purchaser and the purchaser must be paid in accordance with the terms of the offer.

## **Virginia**

None of the shares sold in the state of Virginia may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Virginia Securities Act.

Under Virginia law, a person who offers or sells securities in violation of the registration requirements is civilly liable to the person buying the security. The purchaser may sue to recover the consideration paid for the security, together with interest at 6% per year, costs, and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of such security, or for the substantial equivalent in damages if he no longer owns the security. Any tender may be made at any time before entry of judgment. The purchaser must bring the action for violation of the registration requirements within two years after the transaction upon which the action is based.

However, we may terminate the rights of the purchasers to seek additional remedies under the Virginia Securities Act by making a written rescission offer, before suit, to refund the consideration paid, together with interest at 6% per year, less the amount of any income received on the security, or to pay damages if the purchaser no longer owns the security, and the purchaser refuses or fails to accept such offer within 30 days of its receipt.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Virginia Securities Act.

## **Washington**

None of the shares sold in the state of Washington may have been issued pursuant to an effective registration statement or an applicable exemption from the qualification requirements set forth in the Securities Act of Washington.

Under Washington law, a person who offers or sells securities in violation of the registration requirements is civilly liable to the person buying the security. The purchaser may sue to recover the consideration paid for the security, together with interest at 8% per year, costs and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages if the purchaser no longer owns the security. Damages are the amount that would be recoverable upon a tender less (i) the value of the security when the purchaser disposed of it, and (ii) interest at 8% per year from the date. The purchaser must bring the action for violation of the registration requirements within three years after the contract of sale.

However, we may terminate the rights of the purchasers to seek additional remedies under the Securities Act of Washington by making a written rescission offer, before suit, which has been passed upon by the director before suit, and at a time when the purchaser owned the security, to refund the consideration paid together with interest at 8% per year, less the amount of any income received on the security.

We believe that this rescission offer complies in all material respects with the rescission offer requirements of the Securities Act of Washington.

## **Israel**

Israel's securities law, known as The Securities Law, 5728-1968, prohibits the offering of securities to the public, other than under a prospectus, the publication of which has been permitted by the Israel Securities Authority. The regulations promulgated under The Securities Law provide for an exemption to this general prohibition when the number of investors in Israel to whom the offeror sells the offered securities in an offering, combined with the number of investors in Israel to whom the offeror sold securities during the twelve month preceding the offer, is less than 35 investors. Because we have sold our securities to fewer than 35 investors in Israel at any time, we believe that the shares of common stock issued by us in Israel in the public offering were issued pursuant to an exemption from the prospectus publication requirements under Israeli law.

If shares were issued to you in Israel, you do not have a right of rescission under Israeli law. Accordingly, the rescission offer is being made with respect to individuals who purchased shares of our common stock in Israel, pursuant only to United States federal rights of rescission. The acceptance or non-acceptance of the rescission offer by these individuals will have no effect under Israeli law.

## **Funding the Rescission Offer**

We have entered into an agreement with Mark Reed and Robert T. Reed, Jr. (the "designated purchasers") that they would irrevocably commit to purchase up to all of the shares in the rescission offer that are tendered to us for rescission. We would assign to the designated purchasers the right to purchase any rescission shares at 100% of the amount required to pay the rescission price under applicable state law. As currently contemplated, the initial \$250,000 of rescission shares would be purchased by Mark Reed. If the number of rescission shares tendered for rescission exceeds \$250,000 of shares, Robert T. Reed, Jr. would purchase the balance of the rescission shares tendered for rescission to us. Each of the designated purchasers is a brother of Christopher J. Reed, our Chief Executive Officer, Chief Financial Officer and the Chairman of the Board of Directors. Robert T. Reed, Jr. also is our Vice President and National Sales Manager - Mainstream and a beneficial owner of approximately 7.13% of our common stock. Each of the designated purchasers may also participate in the purchase of shares of common stock to be distributed in the public offering. Since up to all of the rescission shares would be purchased by the designated purchasers, none of the rescission shares would be purchased directly by us and would not deplete proceeds from our public offering or other of our then current cash balances. The rescission shares, which may be purchased by the designated purchasers in the rescission offer, would be deemed to be registered shares for the benefit of the designated purchasers pursuant to a registration statement to be filed by us relating to the rescission offer under the Securities Act, effective as of the commencement date of the rescission offer without any further action on the part of the designated purchasers. If we are required to pay the obligation which may be created under the rescission offer, such a refund would materially and adversely effect our financial position.

## **Directors, Officers and Major Stockholders**

None of our officers, directors or 5% stockholders purchased shares in our initial public offering and are not eligible to participate in this rescission offer for purposes of tendering their shares for rescission. However, we have entered into an agreement with Mark Reed and Robert T. Reed, Jr. (the "designated purchasers") that they would irrevocably commit to purchase up to all of the shares in the rescission offer that are tendered to us for rescission. Robert T. Reed, Jr. is a beneficial owner of approximately 7.13% of our common stock. If Robert T. Reed, Jr. purchases shares in this rescission offer, he would increase his ownership interest in us.

## **MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES**

### **Tax Consequences of the Rescission Offer**

The following discussion summarizes the material federal income tax considerations relevant to our stockholders who hold shares that are subject to the rescission offer. We do not discuss all income tax considerations that may be relevant to particular stockholders in light of their individual circumstances, such as stockholders who are non-U.S. persons, stockholders who are not individuals, or stockholders subject to the alternative minimum tax provisions of the Internal Revenue Code of 1986, as amended, or the Code. In addition, we do not address the tax consequences of the rescission offer to persons who hold shares that are subject to hedging, conversion, or constructive sale transactions, or whose tax year is other than a calendar year. Finally, we do not address any foreign, state or local tax considerations. **ACCORDINGLY, STOCKHOLDERS ARE URGED TO CONSULT THEIR OWN TAX ADVISORS AS TO THE SPECIFIC TAX CONSEQUENCES OF THE RESCISSION OFFER, INCLUDING THE APPLICABLE FEDERAL, STATE, LOCAL AND FOREIGN TAX CONSEQUENCES TO THEM OF THE RESCISSION OFFER.**

## General

The repurchase of shares from our stockholders may be treated by the Internal Revenue Service, or the Service, as, among other things, (i) a redemption of equity securities by us, or (ii) a purchase of securities by a third party. Because we cannot determine in advance how the Service may characterize these transactions, we have described below the treatment under the two most likely characterizations.

We have entered into an agreement with Mark Reed and Robert T. Reed, Jr. (the “designated purchasers”) that they would irrevocably commit to purchase up to all of the shares in the rescission offer that are tendered to us for rescission. We would assign to the designated purchasers the right to purchase any rescission shares at 100% of the amount required to pay the rescission price under applicable state law. Each designated person will buy the rescission shares for his own account and with his own funds. There is no plan or intention by us to redeem the shares to be acquired by the designated purchaser.

### Treatment as Repurchase of Shares

We intend to treat the rescission transaction as one strictly between the stockholder and the designated purchaser. A sale to the designated purchaser for an amount of cash equal to the original purchase price, plus applicable accrued interest, would be treated as a sale or exchange, and assuming that such stockholder holds the rescission shares as a capital asset, the sale would be treated as a capital gain or loss (within the meaning of Section 1221 of the Code and administrative and case law thereunder). The amount of the gain would be the amount received by the stockholder (including the accrued interest amount) less the amount originally paid for the rescission shares. In this analysis, we have assumed that the Service will not assert that the designated purchasers are in any way acting as our agent in making the purchase of the rescission shares. If the Service were to assert that the designated purchasers are acting as our agent in making the purchase of the rescission shares, then the tax treatment would more likely be similar to that described in the subparagraph below entitled “Treatment as Redemption of Shares.”

### Treatment as Redemption of Shares

The Service may take the position that the rescission will constitute a taxable redemption of the rescission shares for cash, with the redemption price equal to the amount paid for such shares (and include in the redemption price the interest on the original purchase price of such rescission shares). A redemption for an amount of cash equal to the original purchase price (plus accrued interest) could be treated as a redemption governed by the rules of Section 302 and related sections of the Code. However, the federal tax law governing this proposed transaction is unclear, at best, and we have not received a ruling from the Service regarding such tax consequences. For example, the Service could characterize the rescission offer as the return of the original purchase price, which would ordinarily be nontaxable, plus the payment of interest, which would be taxable as ordinary income.

If this tax position as a redemption is sustained, any rescission transaction would be treated as a sale or exchange, and, assuming that such stockholder holds his shares as a capital asset (within the meaning of Section 1221 of the Code and administrative and case law thereunder), the character of any gain or loss to the stockholder would be treated as a capital gain or loss, if:

- It results in a “complete redemption” of the stockholder's interest in us under Section 302(b)(3) of the Code, which would be the case if either (i) all of the shares actually and constructively owned by the stockholder are sold pursuant to the rescission offer, or (ii) all of the shares actually owned by the stockholder are sold pursuant to the rescission offer and the stockholder is eligible to waive, and effectively waives, constructive ownership of the shares under procedures described in Section 302(c) of the Code;



- It is “substantially disproportionate” with respect to the stockholder under Section 302(b)(2) of the Code, which would occur if (i) the percentage of our voting stock owned by the stockholder immediately after the repurchase, taking into account all shares purchased from the stockholder pursuant to the rescission offer, equals less than 80% of the percentage of our voting stock owned by the stockholder immediately before the repurchase, and (ii) the stockholder, after the repurchase, owns less than 50% of the total combined voting power of all classes of our stock entitled to vote; or
- It is not “essentially equivalent to a dividend” with respect to the stockholder, under Section 302(b)(1) of the Code, which would occur if, in light of the stockholder’s individual circumstances, including his relative interest in us, his sale of shares pursuant to the rescission offer results in a “meaningful reduction” of his interest in us.

In determining whether any of the above redemption tests are satisfied, a stockholder must take into account not only shares that are actually owned by him, but also shares that are constructively owned by him within the meaning of Section 318 of the Code. Section 318 of the Code provides that a stockholder may constructively own shares actually owned, and in some cases, constructively owned by certain related individuals and shares that he has the right to acquire by the exercise of an option, warrant, or a conversion right. Contemporaneous or related transactions in our capital stock or capital stock rights also may affect the redemption tests.

If the rules of Section 302 were to apply and the rescission fails to qualify as a redemption, then the gross proceeds of such transaction would be characterized as a dividend distribution, taxable at ordinary income tax rates to the extent of our accumulated and current earnings and profits (if any), and any excess would be treated as a return of capital, to the extent of the stockholder’s basis in the rescission shares, and any amount in excess of the basis would be treated as a gain from a sale or exchange of a capital asset.

THE LAW APPLICABLE TO THE RESCISSION OFFER IS UNCLEAR AND WE HAVE NOT RECEIVED AN OPINION OF COUNSEL OR A RULING FROM THE SERVICE TO THAT EFFECT. THUS, THE SERVICE COULD SUCCESSFULLY ASSERT A CONTRARY POSITION, OR OTHERWISE, RECHARACTERIZE THE TRANSACTION IN WHOLE OR IN PART.

THE PRECEDING DISCUSSION IS INTENDED ONLY AS A SUMMARY OF CERTAIN UNITED STATES INCOME TAX CONSEQUENCES OF THE RESCISSION OFFER AND DOES NOT PURPORT TO BE A COMPLETE ANALYSIS OR DISCUSSION OF ALL POTENTIAL TAX EFFECTS RELEVANT THERETO. STOCKHOLDERS ARE URGED TO CONSULT THEIR OWN TAX ADVISORS AS TO THE SPECIFIC TAX CONSEQUENCES TO THEM OF THE RESCISSION OFFER, INCLUDING TAX RETURN REPORTING REQUIREMENTS, THE APPLICABILITY AND EFFECT OF FOREIGN, FEDERAL, STATE, LOCAL, AND OTHER APPLICABLE TAX LAWS AND THE EFFECT OF ANY PROPOSED CHANGES IN THE TAX LAWS.

#### **SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This prospectus contains forward-looking statements. The forward-looking statements are contained principally in, but not limited to, the sections entitled “Risk Factors,” “Management’s Discussion and Analysis or Plan of Operation” and “Business.” Forward-looking statements provide our current expectations or forecasts of future events. Forward-looking statements include statements about our expectations, beliefs, plans, objectives, intentions, assumptions and other statements that are not historical facts. Words or phrases such as “anticipate,” “believe,” “continue,” “ongoing,” “estimate,” “expect,” “intend,” “may,” “plan,” “potential,” “predict,” “project” or similar words or phrases, or the negatives of those words or phrases, may identify forward-looking statements, but the absence of these words does not necessarily mean that a statement is not forward-looking.



Forward-looking statements are subject to known and unknown risks and uncertainties and are based on potentially inaccurate assumptions that could cause actual results to differ materially from those expected or implied by the forward-looking statements. Our actual results could differ materially from those anticipated in forward-looking statements for many reasons, including the factors described in the section entitled “Risk Factors” in this prospectus. Accordingly, you should not unduly rely on these forward-looking statements, which speak only as of the date of this prospectus.

Unless required by law, we undertake no obligation to publicly revise any forward-looking statement to reflect circumstances or events after the date of this prospectus or to reflect the occurrence of unanticipated events. You should, however, review the factors and risks we describe in the reports we will file from time to time with the SEC, after the date of this prospectus.

Management cautions that these statements are qualified by their terms and/or important factors, many of which are outside of our control, involve a number of risks, uncertainties and other factors that could cause actual results and events to differ materially from the statements made, including, but not limited to, the following:

- The effectiveness of our rescission offer to preclude certain holders of our stock from seeking relief for alleged violations of securities laws in connection with securities issuances in connection with our initial public offering,
- Our ability to generate sufficient cash flow to support capital expansion plans and general operating activities,
  - Decreased demand for our products resulting from changes in consumer preferences,
- Competitive products and pricing pressures and our ability to gain or maintain its share of sales in the marketplace,
  - The introduction of new products,
- Our being subject to a broad range of evolving federal, state and local laws and regulations including those regarding the labeling and safety of food products, establishing ingredient designations and standards of identity for certain foods, environmental protections, as well as worker health and safety. Changes in these laws and regulations could have a material effect on the way in which we produce and market our products and could result in increased costs,
- Changes in the cost and availability of raw materials and the ability to maintain our supply arrangements and relationships and procure timely and/or adequate production of all or any of our products,
  - Our ability to penetrate new markets and maintain or expand existing markets,
  - Maintaining existing relationships and expanding the distributor network of our products,
- The marketing efforts of distributors of our products, most of whom also distribute products that are competitive with our products,
- Decisions by distributors, grocery chains, specialty chain stores, club stores and other customers to discontinue carrying all or any of our products that they are carrying at any time,
  - The availability and cost of capital to finance our working capital needs and growth plans,
  - The effectiveness of our advertising, marketing and promotional programs,



- Changes in product category consumption,
  - Economic and political changes,
- Consumer acceptance of new products, including taste test comparisons,
  - Possible recalls of our products, and
- Our ability to make suitable arrangements for the co-packing of any of our products.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements.

### **DIVIDEND POLICY**

We have never declared or paid dividends on our common stock. We currently intend to retain future earnings, if any, for use in our business, and, therefore, we do not anticipate declaring or paying any dividends in the foreseeable future. Payments of future dividends, if any, will be at the discretion of our board of directors after taking into account various factors, including the terms of our credit facility and our financial condition, operating results, current and anticipated cash needs and plans for expansion.

We are obligated to pay a non-cumulative 5% dividend from lawfully available assets to the holders of our Series A preferred stock in either cash or additional shares of common stock at our discretion. In 2005, we paid the dividend in an aggregate of 7,362 shares of common stock, and anticipate that we will be obligated to issue at least this many shares annually to the holders of the Series A preferred stock so long as such shares are issued and outstanding. See “Description of Our Securities - Preferred Stock.”

### **MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our financial statements and the related notes appearing elsewhere in this prospectus. This discussion and analysis may contain forward-looking statements based on assumptions about our future business. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including but not limited to those set forth under “Risk Factors” and elsewhere in this prospectus.*

#### **Overview**

We develop, manufacture, market and sell natural non-alcoholic and “New Age” beverages, candies and ice creams. “New Age Beverages” is a category that includes natural soda, fruit juices and fruit drinks, ready-to-drink teas, sports drinks and water. We currently manufacture, market and sell six unique product lines:

- Reed’s Ginger Brews,
- Virgil’s Root Beer and Cream Sodas,
- China Colas,
- Reed’s Ginger Juice Brews,

- Reed's Ginger Candies, and
- Reed's Ginger Ice Creams

We sell most of our products in specialty gourmet and natural food stores, supermarket chains, retail stores and restaurants in the United States and, to a lesser degree, in Canada. We primarily sell our products through a network of natural, gourmet and independent distributors. We also maintain an organization of in-house sales managers who work mainly in the stores serviced by our natural, gourmet and mainstream distributors and with our distributors. We also work with regional, independent sales representatives who maintain store and distributor relationships in a specified territory. In Southern California, we have our own direct distribution system.

The following table shows a breakdown of net sales with respect to our distribution channels for the periods set forth in the table:

	<b>Direct sales to large retailer accounts</b>	<b>% of total sales</b>	<b>Local direct distribution</b>	<b>% of total sales</b>	<b>Natural, gourmet and mainstream distributors</b>	<b>% of total</b>	<b>Total sales</b>
2005	\$ 1,536,896	16	\$ 751,999	8	\$ 7,181,390	76	\$ 9,470,285
2004	1,983,598	22	395,601	4	6,599,166	74	8,978,365
2003	1,286,365	19	90,121	1	5,405,290	80	6,781,776

Historically, we have focused our marketing efforts on natural and gourmet food stores. In 2003, we expanded our marketing efforts to include more mainstream markets. These efforts included selling our products directly to:

- large retail accounts, such as Costco, BJ Wholesale, and Cost Plus World Markets, and
- the natural food section of mainstream national supermarket chains, such as Safeway, Kroger's, Ralph's and Bristol Farms.

In addition, since 2003, we have introduced new products and offer specialty beverage packaging options not typically available in the marketplace into the marketplace that have contributed to our growth in sales. These products include a 5-liter "party keg" version of our Virgil's Root Beer and Cream Soda, 12-ounce long neck bottles of our Virgil's Cream Soda and 750 ml. size bottles of our Reed's Original Ginger Brew, Extra Ginger Brew and Spiced Apple Brew.

We gauge the financial success of our company by a number of different parameters. Because our industry typically values companies on a top-line basis, one of our main company goals is to increase net sales. Our net sales have increased each year during the period from 2001 to 2005, as follows:

	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
<b>Net sales</b>	\$ 6,200,000	\$ 6,400,000	\$ 6,800,000	\$ 9,000,000	\$ 9,500,000

We believe that the increase in net sales over this period comes from three factors:

- successes in our Southern California direct distribution strategy,
- increases in our core of national distribution to natural and gourmet food stores and mainstream supermarket chains, and
- increases in our direct sales to large retailers.

Almost as important as increasing our net sales are increasing our gross margins. We continue to work to reduce costs related to production of our products. However, we have encountered difficulties in increasing our gross margins due to certain factors, including:

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- inefficiencies commensurate with a start-up period for the Brewery that we purchased in 2002 as our West Coast production facility, and
- higher freight, glass and production expenses due to the increase in the cost of fuel and increases in the price of ingredients in our products.

In 2002, we purchased and outfitted the Brewery, in part to help reduce both production costs and freight costs associated with our west coast sales. Gross margins decreased from 24.8% in 2002 to 19.5% in 2003 as a principal result of the start-up of the Brewery. Gross margins increased to 20.9% in 2004 as a principal result of attaining greater functionality and efficiencies in our operation of the Brewery by our own personnel and being able to produce and ship products in the western half of the United States from a west coast facility. However, in 2005, gross margins decreased to 18.2% as a principal result of increases in fuel prices, which put downward pressure on our margins due to increased freight expenses and increased glass and production costs, both of which are sensitive to fuel costs.

In addition, our west coast Brewery facility is running at 40% of capacity. We have had difficulties with the underutilization of the Brewery at 40% of capacity as a result of working out problems associated with the flavor of our ginger brew products produced at the Brewery, causing us to increase freight and other associated expenses with producing and shipping such products nationally from our east coast co-packing facility. Management is committed to selling a high quality, great tasting product. Since the east coast co-packer is producing such a product, management has elected to continue to sell that product on the west coast, even though it negatively impacts our gross margins. As we are able to make the Brewery become more fully utilized, we believe that we will experience improvements in gross margins due to freight and production savings.

### **Trends, Risks, Challenges, Opportunities That May or Are Currently Affecting Our Business**

Our main challenges, trends, risks and opportunities that could affect or are affecting our financial results include but are not limited to:

**Fuel Prices** - Our freight rates were approximately 9.7% of net sales during 2005. We expect freight rates to increase by an additional 5% to 10% in 2006 as a result of the continuing increase in fuel prices. However, as we increase production at the Brewery, for delivery of products in the western half of the United States, we expect to offset this trend, at least in part, by reducing our need for cross-country freight services from our eastern co-packing facility.

**Low Carbohydrate Diets and Obesity** - Our products are not geared for the low carbohydrate market. Consumer trends have reflected higher demand for lower carbohydrate products. Despite this trend, we achieved an increase in our sales growth in 2005. We monitor these trends closely and have started developing low-carbohydrate versions of some of our beverages, although we do not have any currently marketable low-carbohydrate products.

**Distribution Consolidation** - There has been a recent trend towards continued consolidation of the beverage distribution industry through mergers and acquisitions. This consolidation results in a smaller number of distributors to market our products and potentially leaves us subject to the potential of our products either being dropped by these distributors or being marketed less aggressively by these distributors. As a result, we have initiated our own direct distribution to mainstream supermarkets and natural and gourmet foods stores in Southern California and to large national retailers. Consolidation among natural foods industry distributors has not had an adverse affect on our sales.

**Consumer Demanding More Natural Foods** - The rapid growth of the natural foods industry has been fueled by the growing consumer awareness of the potential health problems due to the consumption of chemicals in the diet. Consumers are reading ingredient labels and choosing products based on them. We design products with these consumer concerns in mind. We feel this trend toward more natural products is one of the main trends behind our

growth. Recently, this trend in drinks has not only shifted to products using natural ingredients, but also to products with added ingredients possessing a perceived positive function like vitamins, herbs and other nutrients. Our ginger-based products are designed with this consumer demand in mind.

**Supermarket and Natural Food Stores** - More and more supermarkets, in order to compete with the growing natural food industry, have started including natural food sections. As a result of this trend, our products are now available in mainstream supermarkets throughout the United States in natural food sections. Supermarkets can require that we spend more advertising money and they sometimes require slotting fees. We continue to work to keep these fees reasonable. Slotting fees in the natural food section of the supermarket are generally not as expensive as in other areas of the store.

**Beverage Packaging Changes** - Beverage packaging has continued to innovate, particularly for premium products. There is an increase in the sophistication with respect to beverage packaging design. While we feel that our current core brands still compete on the level of packaging, we continue to experiment with new and novel packaging designs such as the 5-liter party keg and 750 ml. champagne style bottles. We have further plans for other innovative packaging designs.

**Packaging or Raw Material Price Increases** - An increase in packaging or raw materials has caused our margins to suffer and has negatively impacted our cash flow and profitability. We continue to search for packaging and production alternatives to reduce our cost of goods.

**Cash Flow Requirements** - Our growth will depend on the availability of additional capital infusions. We have a financial history of losses and are dependent on non-banking sources of capital, which tend to be more expensive and charge higher interest rates. Any increase in costs of goods will further increase losses and will further tighten cash reserves. We intend to use the proceeds from our public offering to increase our liquidity to be able to make cash expenditures, as needed.

**Interest Rates** - We use lines of credit as a source of capital and are negatively impacted as interest rates rise. Management believes our public offering will provide capital sufficient for us to reduce our debt level and allow us to lower our incremental borrowing costs.

### **Critical Accounting Policies**

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, or GAAP. GAAP requires us to make estimates and assumptions that affect the reported amounts in our financial statements including various allowances and reserves for accounts receivable and inventories, the estimated lives of long-lived assets and trademarks and trademark licenses, as well as claims and contingencies arising out of litigation or other transactions that occur in the normal course of business. The following summarize our most significant accounting and reporting policies and practices:

**Revenue Recognition.** Revenue is recognized on the sale of a product when the product is shipped, which is when the risk of loss transfers to our customers, and collection of the receivable is reasonably assured. A product is not shipped without an order from the customer and credit acceptance procedures performed. The allowance for returns is regularly reviewed and adjusted by management based on historical trends of returned items. Amounts paid by customers for shipping and handling costs are included in sales.

**Trademark License and Trademarks.** Trademark license and trademarks primarily represent the costs we pay for exclusive ownership of the Reed's® trademark in connection with the manufacture, sale and distribution of beverages and water and non-beverage products. We also own the China Cola® trademark and have applied for a trademark on the Virgil's name. In addition, we own a number of other trademarks in the United States as well as in a number of countries around the world. We account for these items in accordance with SFAS No. 142, "Goodwill and Other Intangible Assets." Under the provisions of SFAS No. 142, we do not amortize indefinite-lived trademark licenses and trademarks.

In accordance with SFAS No. 142, we evaluate our non-amortizing trademark license and trademarks quarterly for impairment. We measure impairment by the amount that the carrying value exceeds the estimated fair value of the trademark license and trademarks. The fair value is calculated by reviewing net sales of the various beverages and applying industry multiples. Based on our quarterly impairment analysis the estimated fair values of trademark license and trademarks exceeded the carrying value and no impairments were identified during the years ended December 31, 2005 or 2004 or during the three months ended March 31, 2006.

**Long-Lived Assets.** Our management regularly reviews property, equipment and other long-lived assets, including identifiable amortizing intangibles, for possible impairment. This review occurs quarterly or more frequently if events or changes in circumstances indicate the carrying amount of the asset may not be recoverable. If there is indication of impairment of property and equipment or amortizable intangible assets, then management prepares an estimate of future cash flows (undiscounted and without interest charges) expected to result from the use of the asset and its eventual disposition. If these cash flows are less than the carrying amount of the asset, an impairment loss is recognized to write down the asset to its estimated fair value. The fair value is estimated at the present value of the future cash flows discounted at a rate commensurate with management's estimates of the business risks. Quarterly, or earlier if there is indication of impairment of identified intangible assets not subject to amortization, management compares the estimated fair value with the carrying amount of the asset. An impairment loss is recognized to write down the intangible asset to its fair value if it is less than the carrying amount. Preparation of estimated expected future cash flows is inherently subjective and is based on management's best estimate of assumptions concerning expected future conditions. No impairments were identified during the years ended December 31, 2005 or 2004 or during the three months ended March 31, 2006.

Management believes that the accounting estimate related to impairment of our long lived assets, including our trademark license and trademarks, is a "critical accounting estimate" because: (1) it is highly susceptible to change from period to period because it requires management to estimate fair value, which is based on assumptions about cash flows and discount rates; and (2) the impact that recognizing an impairment would have on the assets reported on our balance sheet, as well as net income, could be material. Management's assumptions about cash flows and discount rates require significant judgment because actual revenues and expenses have fluctuated in the past and we expect they will continue to do so.

In estimating future revenues, we use internal budgets. Internal budgets are developed based on recent revenue data for existing product lines and planned timing of future introductions of new products and their impact on our future cash flows.

**Advertising.** We account for advertising production costs by expensing such production costs the first time the related advertising is run.

**Accounts Receivable.** We evaluate the collectibility of our trade accounts receivable based on a number of factors. In circumstances where we become aware of a specific customer's inability to meet its financial obligations to us, a specific reserve for bad debts is estimated and recorded which reduces the recognized receivable to the estimated amount our management believes will ultimately be collected. In addition to specific customer identification of potential bad debts, bad debt charges are recorded based on our historical losses and an overall assessment of past due trade accounts receivable outstanding.

**Inventories.** Inventories are stated at the lower of cost to purchase and/or manufacture the inventory or the current estimated market value of the inventory. We regularly review our inventory quantities on hand and record a provision for excess and obsolete inventory based primarily on our estimated forecast of product demand and/or our ability to sell the product(s) concerned and production requirements. Demand for our products can fluctuate significantly. Factors that could affect demand for our products include unanticipated changes in consumer preferences, general market conditions or other factors, which may result in cancellations of advance orders or a reduction in the rate of reorders placed by customers. Additionally, our management's estimates of future product demand may be inaccurate, which could result in an understated or overstated provision required for excess and obsolete inventory.

**Income Taxes.** Current income tax expense is the amount of income taxes expected to be payable for the current year. A deferred income tax asset or liability is established for the expected future consequences of temporary differences in the financial reporting and tax bases of assets and liabilities. We consider future taxable income and ongoing, prudent,

and feasible tax planning strategies, in assessing the value of our deferred tax assets. If our management determines that it is more likely than not that these assets will not be realized, we will reduce the value of these assets to their expected realizable value, thereby decreasing net income. Evaluating the value of these assets is necessarily based on our management's judgment. If our management subsequently determined that the deferred tax assets, which had been written down, would be realized in the future, the value of the deferred tax assets would be increased, thereby increasing net income in the period when that determination was made.

## Results of Operations

### *Three Months Ended March 31, 2006 Compared to Three Months Ended March 31, 2005*

Net sales increased by \$161,936, or 8.9%, from \$1,817,336 in the first three months ended March 31, 2005 to \$1,979,272 in the first three months ended March 31, 2006. Sales of our core Reed's Ginger Brew items increased from \$916,000 in the first three months ended March 31, 2005 to \$1,073,000 in the first three months ended March 31, 2006. Sales of our Virgil's Root Beer 12 ounce bottles and our new Virgil's Cream soda increased by \$76,000 from \$390,000 and \$101,000, respectively, in the first three months ended March 31, 2005 to \$467,000 and \$100,000, respectively, in the first three months ended March 31, 2006. Candy sales increased by \$76,000 from \$129,000 in the first three months ended March 31, 2005 to \$205,000 in the first three months ended March 31, 2006. These increases were offset by decreases in sales in certain of our other products. Sales of our new Virgil's 5-liter party keg labels decreased from \$148,000 in the first three months ended March 31, 2005 to \$50,000 in the first three months ended March 31, 2006 due to non-recurring sales to certain large retailers. Ice cream sales increased from \$34,000 in the first three months ended March 31, 2005 to \$36,000 in the first three months ended March 31, 2006.

Cost of sales increased by \$202,589, or 13.6%, from \$1,486,287 in the first three months ended March 31, 2005 to \$1,688,876 in the first three months ended March 31, 2006. As a percentage of net sales, cost of sales increased from 81.8% in the first three months ended March 31, 2005 to 85.3% in the first three months ended March 31, 2006. Costs of sales increased primarily as a result of increased depreciation (0.6%), increased production expenses due to fuel costs (2.5%) and increased packaging costs (0.4%).

Gross profit decreased from \$331,049 in the first three months ended March 31, 2005 to \$290,396 in the first three months ended March 31, 2006. As a percentage of net sales, gross profit decreased from 18.2% in the first three months ended March 31, 2005 to 14.7% in the first three months ended March 31, 2006. Effective February 1, 2006, we approved a price increase in a number of our product lines at an average of approximately 7% in order to attempt to increase our gross profit. The full implementation of the price increase is expected to be completed by the middle of the third quarter of 2006. We expect margins to increase by the end of 2006 due to this price increase, provided that these price increases do not adversely affect our volume of sales.

General and administrative and selling expenses increased by \$50,719, or 10.2%, from \$499,099 in the first three months ended March 31, 2005 to \$549,818 in the first three months ended March 31, 2006 and increased as a percentage of net sales from 27.5% in the first three months ended March 31, 2005 to 27.8% in the first three months ended March 31, 2006. The increase in expenses was due to increased salaries due to a larger sales force (0.8%), increased sales expenses from increased fuel costs and increased telephone charges (3.8%), increased utility expenses (1.1%) and increased legal and accounting costs due to the costs associated with being a public reporting company (0.8%). Health insurance costs increased due to more people being covered by our health plan (2.3%). Payroll increased due to temporary employee services incurred as a result of an employee departure during the quarter ended March 31, 2006 (2.0%). We reduced our promotional expenses due to fewer club store demos (-1.9%).

Legal defense costs for the three months ended March 31, 2006 and 2005 were \$9,568 and \$2,216, respectively. These expenses were incurred for a lawsuit brought against us by a consultant alleging funds due him. We mounted a successful defense in this action and were successful on an appeal of this matter.

Interest expense increased by \$29,397, or 41.3%, from \$71,210 in the first three months ended March 31, 2005 to \$100,607 in the first three months ended March 31, 2006. The increase in interest expense was due to increasing short term interest rates, increased borrowings on our available lines of credit and increasing our long term debt, which was used to purchase brewing equipment, vehicles and office equipment.



As a result of the foregoing, we experienced a net loss of \$241,386 in the first three months ended March 31, 2005 and \$369,597 in the first three months ended March 31, 2006. Accordingly, we experienced a net loss of \$0.05 per share in the first three months ended March 31, 2005 and \$0.07 per share in the first three months ended March 31, 2006.

*Twelve Months Ended December 31, 2005 Compared to Twelve Months Ended December 31, 2004*

Net sales increased by \$491,920, or 5.5%, from \$8,978,365 in 2004 to \$9,470,285 in 2005. Sales of our core Reed's Ginger Brew items increased from \$3,681,000 in 2004 to \$4,103,000 in 2005. Sales of our Virgil's Root Beer 12 ounce bottles and our new Virgil's Cream soda increased from \$1,591,000 and \$139,000, respectively, in 2004 to \$2,091,000 and \$667,000, respectively, in 2005. Candy sales increased from \$699,000 in 2004 to \$822,000 in 2005. These increases were offset by decreases in sales in certain of our other products. Sales of our new Virgil's 5 liter party keg labels decreased from \$1,002,000 in 2004 to \$575,000 in 2005 due to non-recurring sales in 2004 to certain large retailers. Ice cream sales dropped from \$196,000 in 2004 to \$145,000 in 2005. Our co-packing sales of private labels from the Brewery dropped from \$450,048 in 2004 to \$239,835 in 2005.

Cost of sales increased by \$642,462, or 9.0%, from \$7,103,037 in 2004 to \$7,745,499 in 2005. Costs of sales as a percentage of sales increased from 79.1% in 2004 to 81.8% in 2005. Costs of sales as a percentage of sales increased primarily as a result of increases in higher freight costs (0.5%), packaging costs (0.8%) and production expenses (4.4%) due to increased fuel costs and increased depreciation (0.3%), offset by decreases in ingredient costs (-3.3%).

We calculate gross profit as total revenues less cost of sales. Gross profit decreased from \$1,875,328 in 2004 to \$1,724,786 in 2005. As a percentage of net sales, gross profit decreased from 20.9% in 2004 to 18.2% in 2005. Effective February 1, 2006 we increased prices in a number of our product lines at an average of approximately 7% in order to attempt to increase our gross profit. We expect margins to increase by the end of 2006 due to this price increase, provided that these price increases do not adversely affect our volume of sales.

General and administrative and selling expenses increased by \$213,958, or 11.5%, from \$1,866,511 in 2004 to \$2,080,469 in 2005 and increased as a percentage of net sales from 20.8% in 2004 to 22.0% in 2005. The increase in expenses was primarily due to increased salaries due to a larger sales force, more commissions due to increased number of outside sales brokers, increased sales fuel costs, increased fuel expenses for plant heating requirements and increased legal and accounting costs due to the costs associated with the public offering and becoming a reporting company under the Exchange Act. In addition, if we are able to receive a significant portion of the proceeds from the public offering, we intend to increase our in-house sales force, which we anticipate will permit us to increase sales of our product lines in the future. We anticipate a lead time until these new sales people generate enough additional revenue to support their additional cost.

Beginning in January 2000, we extended an interest-free line of credit to one of our consultants, Peter Sharma, III who was a member of our board until January 27, 2006. In July 2005, a repayment schedule began at \$1,000 per month and ends with a balloon payment for the remaining balance, due on December 31, 2007. As of December 31, 2005, management has chosen to reserve the entire amount of the outstanding balance of \$124,210. Management is pursuing collection efforts. Mr. Sharma was a registered representative of Brookstreet Securities Corporation until May 4, 2006. Brookstreet is one of our underwriters in the public offering. Mr. Sharma received compensation of approximately \$28,000 through his former relationship with Brookstreet. We are advised by Brookstreet that Mr. Sharma will not participate in any future sales through Brookstreet in connection with the public offering.

Legal defense costs for the years ended December 31, 2005 and 2004 were \$36,558 and \$80,156, respectively. These expenses were incurred for a lawsuit brought against us by a consultant alleging funds due him. We mounted a successful defense in this action and were successful on an appeal of this matter.

Interest expense increased by \$54,472, or 21.4%, from \$255,032 in 2004 to \$309,504 in 2005. The increase in interest expense was primarily due to increased borrowing on our receivable line of credit with our principal lender. We anticipate using a portion of the proceeds from the public offering to pay down existing lines of credit, and expect that such proceeds will reduce our need for debt financing and allow us to obtain more favorable borrowing rates, thus offsetting the rise in the prime rate, and therefore interest expense should decrease.

Loss on extinguishment of debt decreased from \$153,000 in 2004 to none in 2005. This loss related to the discount on the conversion of approximately \$255,000 of our debt into 25,500 shares of our Series A preferred stock. Upon conversion, the excess of the fair market price of the underlying common stock over the conversion price of \$1.50 per share resulted in the loss on extinguishment of debt.

As a result of the foregoing, we experienced a net loss of \$479,371 and \$855,425 in 2004 and 2005, respectively. In addition, we accrued a \$29,470 dividend payable to the holders of our Series A preferred stock in 2005, which we elected to pay in the form of 7,362 shares of common stock. Accordingly, we experienced a net loss of \$0.10 and \$0.18 per share in 2004 and 2005, respectively.

Management recognizes the operating losses and costs incurred have negatively impacted liquidity. We anticipate using a portion of the proceeds from the public offering to pay down existing lines of credit, and expect that such proceeds will reduce our need for debt financing and allow us to obtain more favorable borrowing rates, thus offsetting the rise in the prime rate, and therefore interest expense should decrease. In addition, we anticipate that the price increases management instituted will lead to increased gross margins and decreases in loss from operations, thus improving our profitability.

### **Liquidity and Capital Resources**

Historically, we have financed our operations primarily through private sales of common stock, preferred stock, convertible debt, a line of credit from a financial institution, and cash generated from operations.

As of March 31, 2006, we had a working capital deficit of \$1,315,156, compared to a working capital deficit of \$1,594,758 as of December 31, 2005. This decrease in our working capital deficit should not be viewed as a change in trend. The primary factor contributing to a reduction in our working capital deficit was the cash received from our initial public offering. As of December 31, 2005, we had a working capital deficit of \$1,594,758, compared to a working capital deficit of \$684,647 as of December 31, 2004. This increase in our working capital deficit was primarily attributable to increases in accounts payable and our line of credit. These increases were required due to the loss we incurred in 2005 and costs incurred for the public offering. Cash and cash equivalents were \$195,457 as of March 31, 2006, as compared to \$27,744 as December 31, 2005 and \$42,488 as of December 31, 2004.

As of March 31, 2006, we had outstanding borrowings of \$1,539,946 under the following line of credit agreements:

- We have an unsecured \$50,000 line of credit with US Bank which expires in December 2009. Interest is payable monthly at the prime rate, as published in the Wall Street Journal, plus 12% per annum. Our outstanding balance was \$26,646 at March 31, 2006 and there was \$23,354 available under the line of credit. The interest rate in effect at March 31, 2006 was 19.75%.
- We have a line of credit with Merrill Lynch. Robert T. Reed, Jr., our Vice President and National Sales Manager - Mainstream and a brother of our Chief Executive Officer, Christopher J. Reed has pledged certain securities (which do not include any of our securities which are owned by Mr. Reed) in his personal securities account on deposit with Merrill Lynch as collateral for repayment of the line of credit. The amount of the line of credit is based on a percentage value of such securities. At March 31, 2006, the outstanding balance on the line of credit was \$642,209, and there was \$47,140 available under the line of credit. The line of credit bears interest at a rate of 3.785% per annum plus LIBOR (8.695% as of March 31, 2006). In consideration for Mr. Reed's pledging his stock account at Merrill Lynch as collateral, we have agreed to pay Mr. Reed 5% per annum of the amount we borrow from Merrill Lynch, as a loan fee. During the years ended December 31, 2005 and 2004, we paid Mr. Reed \$15,250 and \$3,125, respectively, under this agreement. In addition, Christopher J. Reed has pledged all of his shares of common stock to Robert T. Reed, Jr. as collateral for the shares pledged by Robert T. Reed, Jr.



We have a line of credit with Business Alliance Capital Corporation. This line of credit allows us to borrow a maximum amount of \$1,400,000, based on a borrowing base of accounts receivables and inventory. The borrowing base on the accounts receivable is 80% of all eligible receivables, which are primarily accounts receivables under 90 days. The inventory borrowing base is 50% of eligible inventory. As of March 31, 2006, the outstanding balance on the line of credit was \$871,091. The interest rate on this line of credit is prime plus 4.0%, and the interest rate at March 31, 2006 was 10.5%. The line of credit expires on June 30, 2007 and is guaranteed by Christopher J. Reed and his wife, Judy Reed, who are directors and our principal stockholders. This revolving line of credit is secured by all of our assets, including accounts receivable, inventory, trademarks and other intellectual property, building and equipment. As of March 31, 2006, we had approximately \$257,000 of availability on this line of credit.

At March 31, 2006, we did not have any material commitments for capital expenditures.

Net cash used in operating activities was \$491,428 in the quarter ended March 31, 2006, as compared to net cash provided by operating activities of \$135,465 in the quarter ended March 31, 2005. This increase in net cash used in operating activities was primarily due to the increase in net loss to \$369,587 in the quarter ended March 31, 2006, as compared to \$241,368 in the quarter ended March 31, 2005, increases in inventory and accounts receivable in the quarter ended March 31, 2006 from the prior corresponding period, offset by decreases in prepaid expenses in the quarter ended March 31, 2006 from the prior corresponding period.

Net cash used in operating activities decreased to \$42,610 in the year ended December 31, 2005 from \$176,020 in the year ended December 31, 2004. This decrease primarily was due to the increase in net loss to \$825,955 in 2005, as compared to \$479,371 in 2004, decreases in accrued interest and increases in prepaid expenses in 2005 from 2004 and a non-recurring write off in deferred offering costs of \$153,000 in 2004, offset by a provision for amounts due from a former director in 2005 and the decrease of accounts receivable and inventory in 2005 from 2004.

We used \$19,271 in investing activities in the quarter ended March 31, 2006, as compared to \$37,001 in the quarter ended March 31, 2005. Net cash used in investing activities in each of these quarters primarily consisted of the purchase of equipment for the Brewery. In the quarter ended March 31, 2005, we made a loan to a director in the amount of \$12,813 before we commenced our public offering.

We used \$214,667 in investing activities in the year ended December 31, 2005, as compared to \$248,187 in the year ended December 31, 2004. Net cash used in investing activities in each of these years primarily consisted of the purchase of equipment for the Brewery and loans made to a director before we commenced our public offering. In the years ended December 31, 2005 and 2004, we purchased equipment for the Brewery in the amounts of \$181,654 and \$204,147, respectively, and made loans to a former director in the amounts of \$33,013 and \$44,040, respectively.

Cash flow provided from financing activities in the quarter ended March 31, 2006 was \$678,412, as compared to cash flow used in financing activities of \$107,792 in the quarter ended March 31, 2005. We received cash from the sale of common stock of \$811,955 in the public offering in the quarter ended March 31, 2006. We increased borrowings on our line of credit in the amount of \$93,993 in the quarter ended March 31, 2006, as compared to our making payments on our line of credit in the amount of \$194 in the quarter ended March 31, 2005. Deferred offering costs increased to \$198,833 in the quarter ended March 31, 2006 as compared to \$63,062 in the quarter ended March 31, 2005. The increase in deferred offering costs primarily related to offering costs, such as accounting fees, legal fees, and selling expenses, that we incurred in connection with the public offering. We made principal payments on our long-term debt of \$28,703 and \$44,536 in the quarters ended March 31, 2006 and 2005, respectively.

Cash flow provided from financing activities was \$242,533 in the year ended December 31, 2005, as compared to \$453,765 in the year ended December 31, 2004. We increased borrowings on our line of credit in 2005 and long term debt in the aggregate amount of approximately \$115,000 primarily to purchase manufacturing equipment to improve the Brewery and vehicles for our Southern California direct distribution program. In addition, we received cash from the sale of common stock of approximately \$197,000 in the public offering in 2005 and approximately \$334,000 from the issuance of preferred stock in 2004. The slight increase in cash provided by financing activities from 2004 to 2005 was offset by larger increases in cash used in financing activities from 2004 to 2005. Increases in deferred offering costs increased to \$332,858 in 2005 from \$219,955 in 2004. The increase in deferred offering costs primarily related to offering costs, such as accounting fees, legal fees, and selling expenses, that we incurred in connection with the public offering. We made principal payments on our long-term debt of \$263,815 and \$208,852 in the years ended December 31, 2005 and 2004, respectively. We also paid to Judy Reed the amount of \$21,000 in 2005 as repayment of debt.

During the quarter ended March 31, 2006, we had a net loss of \$369,597. At March 31, 2006, we had a working capital deficiency of \$1,315,156 and an accumulated deficit of approximately \$3,630,000. During the year ended December 31, 2005, we had a net loss of \$825,955. At December 31, 2005, we had a working capital deficiency of \$1,594,758 and an accumulated deficit of approximately \$3,260,000.

We have a “best efforts” commitment from an underwriter to assist us in continuing the process of raising capital through a public offering of our common stock which we commenced in 2005. We believe that we will be successful in raising additional funds from the public offering. However, we cannot predict the exact amount which will be raised. We intend to resume the offering upon completion of this rescission offer to persons who have purchased shares in the offering to date. We expect the public offering to commence during the summer of 2006. Until the commencement of the public offering, we will continue to experience challenges with managing cash flow, but we believe that we have enough liquidity to operate the business in the short term. The addition of cash from the public offering, if successful, would provide us the ability to improve our liquidity position and provide capital to continue to expand the business. The remaining amount of common stock that we can sell in connection with the offering is 1,666,844 shares at an anticipated offering price of \$4.00 per share. If the remainder of the shares were sold, we would receive approximately \$6,445,000, net of offering expenses.

We have entered into an agreement with Mark Reed and Robert T. Reed, Jr. (the “designated purchasers”) that they would irrevocably commit to purchase up to all of the shares in the rescission offer that are tendered to us for rescission. We would assign to the designated purchasers the right to purchase any rescission shares at 100% of the amount required to pay the rescission price under applicable state law. As currently contemplated, the initial \$250,000 of rescission shares would be purchased by Mark Reed. If the number of rescission shares tendered for rescission exceeds \$250,000 of shares, Robert T. Reed, Jr. would purchase the balance of the rescission shares tendered for rescission to us. Each of the designated purchasers is a brother of Christopher J. Reed, our Chief Executive Officer, Chief Financial Officer and the Chairman of the Board of Directors. Robert T. Reed, Jr. also is our Vice President and National Sales Manager - Mainstream and a beneficial owner of approximately 7.13% of our common stock. Each of the designated purchasers may also participate in the purchase of shares of common stock to be distributed in the public offering. Since up to all of the rescission shares would be purchased by the designated purchasers, none of the rescission shares would be purchased directly by us and would not deplete proceeds from our public offering or other of our then current cash balances. The rescission shares, which may be purchased by the designated purchasers in the rescission offer, would be deemed to be registered shares for the benefit of the designated purchasers pursuant to a registration statement to be filed by us relating to the rescission offer under the Securities Act, effective as of the commencement date of the rescission offer without any further action on the part of the designated purchasers. If we are required to pay the obligation which may be created under the rescission offer, such a refund would materially and adversely effect our financial position.

We may not generate sufficient revenues from product sales in the future to achieve profitable operations. If we are not able to achieve profitable operations at some point in the future, we eventually may have insufficient working capital to maintain our operations as we presently intend to conduct them or to fund our expansion and marketing and product development plans. In addition, our losses may increase in the future as we expand our manufacturing capabilities and fund our marketing plans and product development. These losses, among other things, have had and will continue to have an adverse effect on our working capital, total assets and stockholders' equity. If we are unable to achieve profitability, the market value of our common stock will decline and there would be a material adverse effect on our financial condition.

We are conducting the public offering to raise an additional approximate \$6,445,000 of net proceeds from the sale of our common stock. We intend to use the proceeds from the public offering for working capital, the expansion and development of our sales and marketing activities and to invest in infrastructure to increase our operational and manufacturing efficiencies. However, the public offering is being conducted on a “best efforts” basis, and we cannot assure you that we will sell the maximum amount of securities being offered thereby. Accordingly, if we cannot receive adequate proceeds from the public offering, we may be limited in our ability to expand our business operations as rapidly as we would deem necessary at any time, unless we are able to obtain additional financing. There can be no assurance that we will be able to obtain such financing on acceptable terms, or at all. If adequate funds are not available or are not available on acceptable terms, we may not be able to pursue our business objectives. This inability could adversely affect our business, results of operations and financial condition.

As we are not required to use our capital sources to pay for the repurchase of shares in the rescission offer, we currently believe that our available cash resources and cash flow from operations, without any additional net proceeds from the public offering, will be sufficient to sustain our business operations for at least 13 months after the date of this prospectus. However, we would be required to reduce our level of operations, including reducing infrastructure, promotions, personnel and other operating expenses.

In addition, our ability to implement our full business expansion plan is largely dependent upon the outcome of the public offering. If we do not receive the maximum proceeds from the public offering, some or all of the elements of our expansion plan may have to be curtailed or delayed unless we are able to find alternative external sources of working capital. We would need to raise additional funds to respond to business contingencies, which may include the need to:

- fund more rapid expansion,
- fund additional marketing expenditures,
- enhance our operating infrastructure,
- respond to competitive pressures, and
- acquire other businesses.

We cannot assure you that additional financing will be available on terms favorable to us, or at all. If adequate funds are not available or if they are not available on acceptable terms, our ability to fund the growth of our operations, take advantage of opportunities, develop products or services or otherwise respond to competitive pressures, could be significantly limited.

### **Recent Accounting Pronouncements**

In November 2004, the Financial Accounting Standards Board, or FASB, issued SFAS No. 151, “Inventory Costs, an amendment of ARB No. 43, Chapter 4.” The amendments made by Statement 151 clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current period charges and require the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The guidance is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 23, 2004. We have evaluated the impact of the adoption of SFAS 151, and do not believe the impact will be significant to our overall results of operations or financial position.



In December 2004, the FASB issued SFAS No. 153, "Exchanges of Non-monetary Assets, an amendment of APB Opinion No. 29, Accounting for Non-monetary Transactions." The amendments made by Statement 153 are based on the principle that exchanges of non-monetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for non-monetary exchanges of similar productive assets and replace it with a broader exception for exchanges of non-monetary assets that do not have commercial substance. Previously, Opinion 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. Opinion 29 provided an exception to its basic measurement principle (fair value) for exchanges of similar productive assets. The FASB believes that exception required that some non-monetary exchanges, although commercially substantive, be recorded on a carryover basis. By focusing the exception on exchanges that lack commercial substance, the FASB believes this Statement produces financial reporting that more faithfully represents the economics of the transactions. The Statement is effective for non-monetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for non-monetary asset exchanges occurring in fiscal periods beginning after the date of issuance. The provisions of this Statement shall be applied prospectively. We have evaluated the impact of the adoption of SFAS 153, and do not believe the impact will be significant to our overall results of operations or financial position.

In December 2004, the FASB issued SFAS No. 123 (revised 2004), "Share-Based Payment." Statement 123(R) will provide investors and other users of financial statements with more complete and neutral financial information by requiring that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. Statement 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. Statement 123(R) replaces FASB Statement No. 123, "Accounting for Stock-Based Compensation," and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees." Statement 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, that Statement permitted entities the option of continuing to apply the guidance in Opinion 25, as long as the footnotes to financial statements disclosed what net income would have been had the preferable fair-value-based method been used. Public entities (other than those filing as small business issuers) will be required to apply Statement 123(R) as of the first interim or annual reporting period that begins after June 15, 2005. We have evaluated the impact of the adoption of SFAS 123(R), and do not believe the impact will be significant to our overall results of operations or financial position. All options issued prior to December 31, 2005 vested immediately, and therefore, there is no associated unamortized compensation that will be recorded in future periods relating to these options.

In May 2005 the FASB issued SFAS Number 154, "Accounting Changes and Error Corrections." This SFAS provides guidance on accounting for and reporting of accounting changes and error corrections. We have evaluated the impact of SFAS 154 and do not believe the impact will be significant to our overall results of operations or financial position.

We do not believe that the adoption of the above recent pronouncements will have a material effect on our financial position or results of operations.

On September 22, 2005, the SEC issued rules to delay by one-year the required reporting by management on internal controls over financial reporting for non-accelerated filers. The new SEC rule extends the compliance date for such registrants to fiscal years ending on or after July 15, 2007. Accordingly, we qualify for the deferral until the year ending December 31, 2007 in order to comply with the internal control reporting requirements.

## **Inflation**

Although management expects that our operations will be influenced by general economic conditions, we do not believe that inflation has a material effect on our results of operations.



## BUSINESS

### Background

We develop, manufacture, market, and sell natural non-alcoholic and “New Age” beverages, candies and ice creams. “New Age Beverages” is a category that includes natural soda, fruit juices and fruit drinks, ready-to-drink teas, sports drinks and water. We currently manufacture, market and sell six unique product lines:

- Reed’s Ginger Brews,
- Virgil’s Root Beer and Cream Sodas,
- China Colas,
- Reed’s Ginger Juice Brews,
- Reed’s Ginger Candies, and
- Reed’s Ginger Ice Creams

We sell most of our products in specialty gourmet and natural food stores, supermarket chains, retail stores and restaurants in the United States and, to a lesser degree, in Canada. We primarily sell our products through a network of natural, gourmet and independent distributors. We also maintain an organization of in-house sales managers who work mainly in the stores serviced by our natural, gourmet and mainstream distributors and with our distributors. We also work with regional, independent sales representatives who maintain store and distributor relationships in a specified territory. In Southern California, we have our own direct distribution system.

We produce and co-pack our products principally at our company-owned facility in Los Angeles, California, known as the Brewery, and at a contracted co-packing facility in Pennsylvania. We also co-pack certain of our products at smaller co-packing facilities in the United States and in Europe.

Key elements of our business strategy include:

- increased national direct sales and distribution,
- increased store placement with mainstream stores and retailers,
- strong national distributorships,
- stimulate strong consumer demand for our existing brands and products,
- develop additional unique alternative beverage brands and other products, and
- specialty packaging like our 5-liter party kegs, our ceramic swing-lid bottle and our 750 ml. champagne bottle.

Our current sales efforts are focused in three areas:

- sales to mainstream, natural and specialty food stores in the United States and, to a lesser degree, Canada, through our regional distributors and sales representatives,
- direct sales effort to large national retailers, and

- direct distribution by our trucks and drivers to retailers in Southern California.

We believe that these marketing efforts have contributed to our growth. We intend to continue to expand our sales personnel in each of these marketing areas with the proceeds from the public offering.

In addition, since 2003, we have introduced new products and offer specialty beverage packaging options not typically available in the marketplace into the marketplace that have contributed to our growth in sales. These products include a 5-liter “party keg” version of our Virgil’s Root Beer and Cream Soda, 12-ounce long neck bottles of our Virgil’s Cream Soda, 750 ml. size bottles of our Reed’s Original Ginger Brew, Extra Ginger Brew and Spiced Apple Brew and a one pint version of our Virgil’s Root Beer with a swing-lid. In addition, we have recently introduced a new flavor, our Black Cherry Cream soda in a 12-ounce bottle. These new packaging options are being utilized in our marketing efforts.

We create consumer demand for our products by

- supporting in-store sampling programs of our products,
- generating free press through public relations,
- advertising in national magazines targeting our customers,
- maintaining a company website (*www.reedsgingerbrew.com*), and
- participating in large public events as sponsors.

Our business expansion plans are contingent to a great extent on the success of the public offering. If all or most of the shares being offered in our public offering are sold, we expect to be able to increase our marketing, advertising and distribution campaigns, and the number of products we offer. The failure to raise the maximum proceeds offered in our public offering will limit our ability to expand our operations.

Our principal executive offices are located at 13000 South Spring Street, Los Angeles, California 90061. Our telephone number is (310) 217-9400. Our Internet address is *www.reedsgingerbrew.com*. Information contained on our website or that is accessible through our website should not be considered to be part of this prospectus.

## **Historical Development**

In June 1987, Christopher J. Reed, our founder and Chief Executive Officer, began development of Reed’s Original Ginger Brew, his first beverage creation. After two years of development, the product was introduced to the market in Southern California stores in 1989. By 1990, we began marketing our products through natural food distributors and moved our production to a larger facility in Boulder, Colorado.

In 1991, we incorporated our business operations in the state of Florida under the name of Original Beverage Corporation and moved all of our production to a co-pack facility in Pennsylvania. We began exhibiting at national natural and specialty food trade shows, which brought national distribution in natural, gourmet and specialty foods and the signing of our first mainstream supermarket distributor. Our products began to receive trade industry recognition as an outstanding new product. The United States National Association of the Specialty Food Trade, or NASFT, named Original Ginger Brew as an “Outstanding Beverage Finalist” in the United States, and the Canadian Fancy Food Association, or CFFA, awarded us “Best Imported Food Product.”

Throughout the 1990’s, we continued to develop and launch new ginger brew varieties. Reed’s Ginger Brews reached broad placement in natural and gourmet foods stores nationwide through major specialty, natural/gourmet and mainstream food and beverage distributors.

In 1997, we began licensing the products of China Cola and eventually acquired the rights to that product in December 2000. In addition, we launched Reed's Crystallized Ginger Candy, a product which we manufacture in Fiji under a proprietary, natural, non-sulfured process. In 1999, we purchased the Virgil's Root Beer brand from the Crowley Beverage Company. The brand has won numerous gourmet awards. In 2000, we began to market three new products: Reed's Original Ginger Ice Cream, Reed's Cherry Ginger Brew and a beautiful designer 10-ounce gift tin of our Reed's Crystallized Ginger Candy. In December 2000, we purchased an 18,000 square foot warehouse property, the Brewery, in Los Angeles, California, to house our west coast production and warehouse facility. The Brewery now also serves as our principal executive offices. In 2001, we changed our state of incorporation to Delaware and also changed our name to Reed's, Inc. We also introduced our Reed's Chocolate Ginger Ice Cream and Reed's Green Tea Ginger Ice Cream products and expanded our confectionary line with two new candy products: Reed's Crystallized Ginger Baking Bits and Reed's Ginger Candy Chews. In 2002, we launched our Reed's Ginger Juice Brew line, with four flavors of organic juice blends. In November 2002, we completed our first test runs of Reed's and Virgil's products at the Brewery and in January 2003, our first commercially available products came off the Los Angeles line. In 2003, we commenced our own direct distribution in Southern California and introduced sales of our 5-liter Virgil's party keg. In 2004, we expanded our product line to include Virgil's Cream Soda (including in a 5-liter keg), Reed's Spiced Apple Brew in a 750 ml. champagne bottle and draught Virgil's Root Beer and Cream Soda. In 2006, we expanded our product line to include Virgil's Black Cherry Cream Soda.

## Industry Overview

Our beverages are classified as New Age beverages, a category that includes natural soda, fruit juices and fruit drinks, ready-to-drink teas, sports drinks and water. According to Beverage Marketing Corporation, in 2004, total wholesale dollar sales in the New Age segment were approximately \$16.5 billion in wholesale dollar sales, an increase of 11.3% from 2003. (Source: Beverage World Magazine, April 15, 2006.)

Annual confectionary sales (including chocolate, non-chocolate and gum sales) in the United States were approximately \$27.9 billion in 2005, of which approximately \$8.7 billion was non-chocolate candy. (Source: National Confectioners Association, 2006 Year in Review.)

According to the International Dairy Foods Association (IDFA), total U.S. sales of ice cream and frozen desserts were estimated at approximately \$21 billion. The packaged ice cream industry includes economy, regular, premium and super-premium products. Super-premium ice cream, such as Reed's Ginger Ice Creams, is generally characterized by a greater richness and density than other kinds of ice cream. This higher quality ice cream generally costs more than other kinds and is usually marketed by emphasizing quality, flavor selection, texture and brand image. The International Ice Cream Association attributes almost all of the market growth over the past 10 years to sales of super-premium and premium ice creams, particularly the innovative products. Sales of premium and super-premium styles account for approximately 42% of the total industry revenues, versus approximately 15% for all the "light" formulations combined. (Source: CNN/Money, July 29, 2005.)

## Our Products

We currently manufacture and sell 15 beverages, three candies and three ice creams. We make all of our products using premium all-natural ingredients.

We produce carbonated and non-carbonated products. Most sales of our beverage products are of our sodas. According to Spence Information Services (SPINS), which is the only sales information service catering to the natural food trade, for the year 2003,

- Reed's Ginger Brews and Virgil's Root Beer held three of the top ten items based on dollar and unit sales among all sugar/fructose sweetened sodas in the natural foods industry in the United States, with Reed's Extra Ginger Brew holding the number one position, and
- Reed's Original Ginger Brew and Virgil's were two of the top ten brands based on dollar and unit sales among all sugar/fructose sweetened sodas in the natural foods industry in the United States, with Reed's Original Brew holding the number one position.

Our carbonated products include six varieties of Reed's Ginger Brews, Virgil's Root Beer and Cream Sodas, China Cola and Cherry China Cola. We also sell four varieties of a new line of non-carbonated ginger brews called Reed's Ginger Juice Brews.

Our candy products include Reed's Crystallized Ginger Candy, Reed's Crystallized Ginger Baking Bits and Reed's Ginger Candy Chews.

Our ice cream products include Reed's Original Ginger Ice Cream, Reed's Chocolate Ginger Ice Cream and Reed's Green Tea Ginger Ice Cream.

### *Beverages*

#### *Reed's Ginger Brews*

Ginger ale is the oldest known soft drink. Before modern soft drink technology existed, non-alcoholic beverages were brewed at home directly from herbs, roots, spices, and fruits. These handcrafted brews were then aged like wine and highly prized for their taste and their tonic, health-giving properties. Reed's Ginger Brews are a revival of this home brewing art and we make them with care and attention to wholesomeness and quality, using the finest fresh herbs, roots, spices, and fruits. Our expert brew masters brew each batch and age it with great pride.

We believe that Reed's Ginger Brews are unique in their kettle brewed origin among all mass-marketed soft drinks. Reed's Ginger Brews contain between 8 and 26 grams of fresh ginger in every 12-ounce bottle. We use no refined sugars as sweeteners. Our products differ from commercial soft drinks in three particular characteristics: sweetening, carbonation and coloring for greater adult appeal. Instead of using injected-based carbonation, we produce our carbonation naturally, through slower, beer-oriented techniques. This process produces smaller, longer lasting bubbles that do not dissipate rapidly when the bottle is opened. We do not add coloring. The color of our products comes naturally from herbs, fruits, spices, roots and juices.

In addition, since Reed's Ginger Brews are pasteurized, they do not require or contain any preservatives. In contrast, modern commercial soft drinks generally are produced using natural and artificial flavor concentrates prepared by flavor laboratories, tap water, and highly refined sweeteners. Typically, manufacturers make a centrally processed concentrate that will lend itself to a wide variety of situations, waters, and filling systems. The final product is generally cold-filled and requires preservatives for stability. Colors are added that are either natural, although highly processed, or artificial.

In addition, while we make no claim as to any medical or therapeutic benefits of our products, we have found friends and advocates among alternative, holistic, naturopathic, and homeopathic medical practitioners, dieticians and medical doctors, who tell us that they recommend Reed's Extra Ginger Brew for their patients as a simple way to ingest a known level of ginger. The United States Food and Drugs Administration (FDA) include ginger on their GRAS (generally recognized as safe) list. However, neither the FDA nor any other government agency officially endorses or recommends the use of ginger as a dietary supplement.

We currently manufacture and sell six varieties of Reed's Ginger Brews:

- *Reed's Original Ginger Brew* was our first creation, and is a Jamaican recipe for homemade ginger ale using 17 grams of fresh ginger root, lemon, lime, honey, fructose, pineapple, herbs and spices. Reed's Original Ginger Brew is 20% fruit juice.
- *Reed's Extra Ginger Brew* is the same approximate recipe, with 26 grams of fresh ginger root for a stronger bite. Reed's Extra Ginger Brew is 20% fruit juice.

- *Reed's Premium Ginger Brew* is the no-fructose version of Reed's Original Ginger Brew, and is sweetened only with honey and pineapple juice. Reed's Premium Ginger Brew is 20% fruit juice.

- *Reed's Raspberry Ginger Brew* is brewed from 17 grams of fresh ginger root, raspberry juice and lime. Reed's Raspberry Ginger Brew is 20% raspberry juice and is sweetened with fruit juice and fructose.
- *Reed's Spiced Apple Brew* uses 8 grams of fresh ginger root, the finest tart German apple juice and such apple pie spices as cinnamon, cloves and allspice. Reed's Spiced Apple Brew is 50% apple juice and sweetened with fruit juice and fructose.
- *Reed's Cherry Ginger Brew* is the newest addition to our Ginger Brew family, and is naturally brewed from: filtered water, fructose, fresh ginger root, cherry juice from concentrate and spices. Reed's Cherry Ginger Brew is 22% cherry juice.

All six of Reed's Ginger Brews are offered in 12-ounce bottles and are sold in stores as singles, in four-packs and in 24-bottle cases. Reed's Original Ginger Brew is sold by select retailers in a special 12-pack. Reed's Spiced Apple Brew is now available in a 750 ml. champagne bottle.

### *Virgil's Root Beer*

Over the years, Virgil's Root Beer has won numerous awards and has a reputation among many as one of the best root beers made anywhere. Virgil's Root Beer won the "Outstanding Beverage" award at the NASFT's International Fancy Food and Confection Show in 1997.

Virgil's is a premium root beer. We use all-natural ingredients, including filtered water, unbleached cane sugar, anise from Spain, licorice from France, bourbon vanilla from Madagascar, cinnamon from Sri Lanka, clove from Indonesia, wintergreen from China, sweet birch and molasses from the southern United States, nutmeg from Indonesia, pimento berry oil from Jamaica, balsam oil from Peru and cassia oil from China.

We collect these ingredients worldwide and gather them together at the brewing and bottling facilities we use in the United States and Germany. We combine and brew these ingredients under strict specifications and finally heat-pasteurize Virgil's Root Beer, to ensure quality.

We sell Virgil's Root Beer in four packaging styles: 12-ounce bottles in a four-pack, a special ceramic-swing-lid style pint bottle, a 5-liter self-tapping party keg and a draught "pony keg."

### *Virgil's Cream Soda*

We launched Virgil's Cream Soda in January 2004. We make this product with the same attention to quality that makes Virgil's Root Beer so popular.

Virgil's Cream Soda is a gourmet cream soda. We brew Virgil's Cream Soda the same way we brew Virgil's Root Beer. We use all-natural ingredients, including filtered water, unbleached cane sugar and bourbon vanilla from Madagascar.

Virgil's Cream Soda is currently sold in 12-ounce long neck bottles in colorful 4-packs, a 5-liter party keg version and in our draught format.

In 2006, we expanded our product line to include Virgil's Black Cherry Cream Soda in a 12-ounce bottle.

### *China Cola*

We consider China Cola to be the best tasting and most natural cola in the world. We restored China Cola to its original delicious blend of raw cane sugar, imported Chinese herbs, essential oils and natural spices. China Cola

contains no caffeine. It comes in two varieties, Original China Cola and Cherry China Cola.

Original China Cola is made from filtered water, raw cane sugar, szechwan poeny root, cassia bark, Malaysian vanilla, oils of lemon, oil of lime, oil of orange, nutmeg, clove licorice, cardamom, caramel color, citric acid and phosphoric acid.

Cherry China Cola is made from the same ingredients as Original China Cola, with the addition of natural cherry flavor.

China Cola and Cherry China Cola sell as singles, in four-packs and in 24-bottle cases.

#### *Reed's Ginger Juice Brews*

In May 2002, we launched a new line of ginger brews called Reed's Ginger Juice Brews. They are 100% juice products that are non-carbonated and brewed from organic fresh ginger root and sweetened with organic juices. We created this product, in part, in response to a strong trend we have seen toward organic ingredients and non-carbonated beverages in the marketplace. We wanted to extend our ginger brew line and believe that these new flavors will cater to the growing market for organic non-carbonated beverages.

All four of our Reed's Ginger Juice Brews contain: filtered water, organic fresh ginger root, and organic white grape juice from concentrate. Specifically,

- Reed's Lemon Guava Ginger Juice Brew adds guava juice from concentrate and lemon juice from concentrate.
- Reed's Strawberry Kiwi Ginger Juice Brew adds organic strawberry juice from concentrate and organic kiwi juice from concentrate.
- Pineapple Orange Ginger Juice Brew adds organic pineapple juice from concentrate, organic orange juice from concentrate, and organic limejuice from concentrate.
- Reed's Cranberry Raspberry Ginger Juice Brew adds cranberry juice from concentrate, and organic raspberry juice from concentrate.

Reed's Ginger Juice Brews drinks come in a 16-ounce juice bottle as singles or in cases of 12 and 24 bottles.

#### *Reed's Ginger Candies*

##### *Reed's Crystallized Ginger Candy*

Reed's Crystallized Ginger was the first crystallized ginger on the market in the United States to be sweetened with raw cane instead of refined white sugar. Reed's Crystallized Ginger is custom-made for us in Fiji.

The production process is an ancient one that has not changed much over time. After harvesting baby ginger (the most tender kind), the root is diced and then steeped for several days in large vats filled with simmering raw cane syrup. The ginger is then removed and allowed to crystallize into soft, delicious nuggets. Many peoples of the islands have long enjoyed these treats for health and pleasure.

We sell this product in 3.5-ounce bags, 10-ounce enameled, rolled steel gift tins, 16-ounce re-sealable Mylar bags, and in bulk. We also sell Reed's Crystallized Ginger Baking Bits in bulk.

##### *Reed's Ginger Candy Chews*

For many years, residents of Southeast Asia from Indonesia to Thailand have enjoyed soft, gummy ginger candy chews. We sell Reed's Ginger Candy Chews individually wrapped in soft-packs of ten candies and as individually wrapped loose pieces in bulk. Reed's has taken them a step further, adding more ginger, using no gelatin (vegan-friendly) and making them slightly easier to unwrap than their Asian counterparts.



2007 and renews automatically for successive two-year terms unless terminated by either party. The Lion Brewery assembles our products and charges us a fee, generally by the case, for the products they produce.



Competition.”

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distributors in the Southern California area. A DSD system allows us to have greater control over our marketing efforts, as we become less dependent on distributors who have relationships with our competitors. We hope to expand our DSD network to areas outside of Southern California as our resources will allow.



Our Virgil's and China Cola lines compete with a number of other natural soda companies, including Stewarts, IBC, Henry Weinhard, Blue Sky, A&W and Natural Brews.

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CV06-0376. The complaint asserts claims for negligence, breach of contract, breach of warranty, and breach of express indemnity relating to Reed's, Inc.'s manufacture of approximately 13,000 cases of "Prism Green Tea Soda" for Consac. Consac contends that we negligently manufactured the soda resulting in at least one personal injury. Consac seeks \$2.6 million in damages, plus interest and attorneys fees. Some of the allegations made against the company are covered by insurance and some allegations are not covered by insurance. Although we believe that we have meritorious defenses to this proceeding, there can be no assurances as to its outcome.

From August 3, 2005 through April 7, 2006, we issued 333,156 shares of our common stock in connection with our initial public offering pursuant to a Registration Statement on Form SB-2. The shares issued in connection with the initial public offering may have been issued in violation of either federal or state securities laws, or both, and may be subject to rescission. In order to address this issue, we intend to make this rescission offer to the holders of these shares prior to the effective date of the registration statement relating to the public offering.

If this rescission offer is accepted, we could be required to make aggregate payments to the holders of these shares up to \$1,332,624, plus statutory interest. This exposure is calculated by reference to the acquisition price of \$4.00 per share for the common stock in connection with the initial public offering, plus accrued interest at the applicable statutory rate. It is our intention that if any of the shares are tendered for rescission, the shares will be purchased by others and not from our funds. If we are required to pay the obligation which may be created under the rescission offer, such a refund would materially and adversely effect our financial position.

Federal securities laws do not provide that a rescission offer will terminate a purchaser's right to rescind a sale of stock that was not registered as required or was not otherwise exempt from such registration requirements. If any or all of the offerees reject the rescission offer, we may continue to be liable under federal and state securities laws for up to an amount equal to the value of all shares of common stock issued in connection with the initial public offering plus any statutory interest we may be required to pay. We also understand that the SEC and certain state regulators, including California, have requested additional information regarding the rescission offer. If it is determined that we offered securities without properly registering them under federal or state law, or securing an exemption from registration, regulators could impose monetary fines or other sanctions as provided under these laws.

Except as set forth above, we believe that there are no material litigation matters at the current time. Although the results of such litigation matters and claims cannot be predicted with certainty, we believe that the final outcome of such claims and proceedings will not have a material adverse impact on our financial position, liquidity, or results of operations.



*Robert Lyon* has been our Vice President Sales - Special Projects since June 2002. In that capacity, Mr. Lyon directs our Southern California direct sales and distribution program in mainstream markets. Over the past five years, Mr. Lyon also has operated an organic rosemary farm in Malibu, California, selling bulk to re-packagers. In the 1980s and 1990s, Mr. Lyon operated a successful water taxi service with 20 employees and eight vessels of his own design. He also built the national sales team for a jewelry company, Iberia from 1982 through 1987. Mr. Lyon holds several U.S. patents. He earned a Business Degree from Northwestern Michigan University in 1969.



We believe that our directors should have the highest professional and personal ethics and values, consistent with our longstanding values and standards. They should have broad experience at the policy-making level in business or banking. They should be committed to enhancing stockholder value and should have sufficient time to carry out their duties and to provide insight and practical wisdom based on experience. Their service on other boards of public companies should be limited to a number that permits them, given their individual circumstances, to perform responsibly all director duties for us. Each director must represent the interests of all stockholders. When considering potential director candidates, the Board also considers the candidate's character, judgment, diversity, age and skills, including financial literacy and experience in the context of our needs and the needs of the board of directors.



































































































































maximum indemnity allowed to directors and executive officers by Section 145 of the DGCL and which allow for certain additional procedural protections.

II-1

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In September 2005, we declared a dividend of 7,362 shares of our common stock as a dividend to the holders of our Series A preferred stock based on a \$29,470 accrued annual dividend payable. We issued the stock dividend in May 2006. The Series A preferred stock bears a 5% annual, non-cumulative dividend that may be in cash or in shares of our common stock based on its then fair market value. We believe the securities were issued in reliance from exemptions from registration pursuant to Section 4(2) or Regulation D under the Securities Act.

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- 10.9 Sirius/Pureprophet, Ltd. Vendor's Credit Line Agreement with Original Beverage Corp. \*
- 10.10 Terms Of Amortization for Peter Sharma III for Sirius/Pureprophet, Ltd. -  
Vendor's Credit Line Agreement with Original Beverage Corp. \*
- 10.11 Co-Sign Agreement \*

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securities of the undersigned small business issuer pursuant to this registration statement, regardless of the underwriting method used to sell the securities to the purchaser, if the securities are offered or sold to such purchaser by means of any of the following communications, the undersigned small business issuer will be a seller to the purchaser and will be considered to offer or sell such securities to such purchaser:

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Each prospectus filed pursuant to Rule 424(b) as part of a registration statement relating to an offering, other than registration statements relying on Rule 430B or other than prospectus filed in reliance on Rule 430, shall be deemed to be part of and included in the registration statement as of the date it is first used after effectiveness. *Provided, however,* that no statement made in a registration statement or prospectus that is part of the registration statement or made in a document incorporated or deemed incorporated by reference into the registration statement or prospectus that is part of the registration statement will, as to a purchaser with a time of contract of sale prior to such first use, supersede or modify any statement that was made in the registration statement or prospectus that was part of the registration statement or made in any such document immediately prior to such date of first use.

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\* Previously filed as part of the registrant's Registration Statement on Form SB-2 (File No. 333-120451) and incorporated herein by this reference.

# Previously filed as part of this Registration Statement on Form SB-2 (File No. 333-135186).

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**FORM OF NOTICE OF ELECTION**

Reed's, Inc.  
 13000 South Spring Street  
 Los Angeles, California 90061  
 Attn: Christopher J. Reed

Dear Mr. Reed:

I have received the prospectus of Reed's, Inc. ("Reed's") relating to its rescission offer, dated \_\_\_\_\_, 2006, pursuant to which Reed's has offered to repurchase certain shares of its common stock that may have been issued in violation of federal or state securities laws, or both. I advise Reed's as follows by placing an "X" in the proper spaces provided below (and filling in the appropriate table(s), if applicable):

**Shares of Common Stock**

- .. 1. I hereby elect to reject the rescission offer and desire to retain the shares.  
 I hereby elect to accept the rescission offer and rescind the sale of \_\_\_\_\_ (fill in number) shares and to receive a full refund for all sums paid therefore together with interest at the applicable statutory rate per year. My Stock Power(s) is/are also enclosed with this Notice of Election

<b>Date of Purchase</b> (The date you were issued stock. If you do not know, leave blank.)	<b>Number of Shares Purchased</b>	<b>Certificate Number</b> (If you do not know, leave blank.)
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IF PERSONS DESIRING TO ACCEPT THIS RESCISSION OFFER INTEND TO MAKE USE OF THE MAILS TO RETURN THEIR STOCK POWER(S), INSURED REGISTERED MAIL, RETURN RECEIPT REQUESTED, IS RECOMMENDED AND SHOULD ALSO PROVIDE THEIR DOCUMENTATION, INCLUDING THIS NOTICE OF ELECTION, BY FACSIMILE TO CHRISTOPHER J. REED AT THE FOLLOWING FACSIMILE NUMBER: (310) 217-9411.

TO THE EXTENT I HAVE ACCEPTED THE OFFER, I AGREE I WILL NOT HAVE ANY FURTHER RIGHT, TITLE OR INTEREST IN THOSE SHARES OF COMMON STOCK AND ANY SUBSEQUENT APPRECIATION IN THE VALUE OF THE SHARES UNDERLYING THE SHARES OF COMMON STOCK.

For California residents:

THIS OFFER OF REPURCHASE HAS BEEN APPROVED BY THE CALIFORNIA COMMISSIONER OF CORPORATIONS IN ACCORDANCE WITH SECTION 25507(b) OF THE CALIFORNIA CORPORATE SECURITIES LAW OF 1968 ONLY AS TO ITS FORM. SUCH APPROVAL DOES NOT IMPLY A FINDING BY THE COMMISSIONER THAT ANY STATEMENTS MADE HEREIN OR IN ACCOMPANYING DOCUMENTS ARE TRUE OR COMPLETE; NOR DOES IT IMPLY A FINDING THAT THE AMOUNT OFFERED BY REED'S, INC. IS EQUAL TO THE AMOUNT RECOVERABLE BY THE BUYER OF THE SECURITY IN ACCORDANCE WITH SECTION 25503 IN A SUIT AGAINST REED'S, INC., AND THE COMMISSIONER DOES NOT ENDORSE THE OFFER AND MAKES NO RECOMMENDATION AS TO ITS ACCEPTANCE OR REJECTION.

Dated: \_\_\_\_\_, 2006

Print name of stockholder:

Name of stockholder:

Authorized signature:

Authorized signature (if shares held in more than one name):

Title of authorized signatory (if applicable):

Title of authorized signatory (if applicable):

Address of stockholder:

Phone number of stockholder:

Fax number of stockholder:

Email of stockholder:

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**REED'S, INC.  
STOCK POWER**

**FOR VALUE RECEIVED**, the undersigned hereby sells, assigns and transfers unto Reed's, Inc., a Delaware corporation or its designee, \_\_\_\_\_ shares of Common Stock of Reed's, Inc., and does hereby irrevocably constitute and appoint Christopher J. Reed and Judy Holloway Reed, and any of them, the undersigned's Attorney to transfer said shares on the books of said corporation with full power of substitution in the premises.

Dated: \_\_\_\_\_, 2006

**SELLING STOCKHOLDER**

*Print Name(s) of Selling Stockholder(s)*

*Authorized Signature*

*Title of Authorized Signatory (if applicable)<sup>1</sup>*

*Authorized Signature (if shares held in more than one name)*

*Title of Authorized Signatory (if applicable)*

*Address of Selling Stockholder (Line 1)*

*Address of Selling Stockholder (Line 2)*

*Phone*

*Email*

*Fax*

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<sup>1</sup> Trustees, officers and other fiduciaries or agents should indicate their title or capacity and print their names under their signatures.