

CREATIVE COMPUTER APPLICATIONS INC
Form 10QSB
August 15, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-QSB

(Mark One)

**QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2005.

**TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF
THE EXCHANGE ACT**

For the transition period from _____ to _____

Commission file number 0-12551

CREATIVE COMPUTER APPLICATIONS, INC.

(Exact name of small business issuer as specified in its charter)

California
(State or other jurisdiction of
incorporation or organization)

95-3353465
(I.R.S. Employer
Identification No.)

26115-A Mureau Road, Calabasas, California 91302
(Address of principal executive offices)

(818) 880-6700
(Issuer's telephone number, including area code):

Check whether the Issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the Issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 3,483,900 common shares as of August 10, 2005.

Transitional Small Business Disclosure Format (check one):

Yes No

CREATIVE COMPUTER APPLICATIONS, INC.

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CREATIVE COMPUTER APPLICATIONS, INC.

PART 1 - FINANCIAL INFORMATION

Item 1. Financial Statements

CONDENSED CONSOLIDATED BALANCE SHEETS

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	June 30, 2005 (Unaudited)	December 31, 2004 (Unaudited)
<u>ASSETS</u>		
CURRENT ASSETS:		
Cash	\$ 1,354,505	\$ 1,655,063
Receivables, net	710,560	1,736,768
Inventory	104,101	86,298
Prepaid expenses and other assets	314,806	256,289
Deferred tax asset	539,420	539,420
TOTAL CURRENT ASSETS	3,023,392	4,273,838
PROPERTY AND EQUIPMENT, net	447,503	345,004
INVENTORY OF COMPONENT PARTS	209,135	186,599
CAPITALIZED SOFTWARE COSTS, net of accumulated amortization of \$1,056,657 and \$878,021	1,693,358	1,531,573
DEFERRED MERGER COSTS	199,790	
DEFERRED TAX ASSET	254,457	254,457
	\$ 5,827,635	\$ 6,591,471
LIABILITIES AND SHAREHOLDERS EQUITY		
CURRENT LIABILITIES:		
Notes payable to bank (Note 4)	200,000	300,000
Accounts payable	309,419	377,768
Accrued liabilities:		
Vacation pay	247,371	243,060
Accrued payroll	104,491	128,227
Other	183,748	173,808
Deferred service contract income	838,747	1,235,032
Deferred revenue on system sales	369,896	226,111
TOTAL CURRENT LIABILITIES	2,253,672	2,684,006
SHAREHOLDERS EQUITY:		
Common shares, no par value; 20,000,000 shares authorized; 3,409,900 and 3,321,900 shares issued and outstanding	6,287,692	6,195,692
Accumulated deficit	(2,713,729)	(2,288,227)
TOTAL SHAREHOLDERS EQUITY	3,573,963	3,907,465
	\$ 5,827,635	\$ 6,591,471

See Notes to Condensed Consolidated Financial Statements.

CREATIVE COMPUTER APPLICATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended June 30,	
	2005	2004
	(Unaudited)	
NET SYSTEM SALES AND SERVICE REVENUE:		
System sales	\$ 296,600	\$ 723,087
Service revenue	1,259,407	1,071,907
	1,556,007	1,794,994
COSTS OF PRODUCTS AND SERVICES SOLD:		
System sales	371,218	530,905
Service revenue	409,831	398,777
	781,049	929,682
Gross profit	774,958	865,312
OPERATING EXPENSES		
Selling, general and administrative	771,245	596,678
Research and development	244,097	258,534
Total operating expenses	1,015,342	855,212
Operating income (loss)	(240,384)	10,100
INTEREST AND OTHER INCOME	4,415	584
INTEREST EXPENSE	(2,569)	(570)
Income (Loss) before provision for income taxes	(238,538)	10,114
PROVISION FOR INCOME TAXES		
NET INCOME (LOSS)	\$ (238,538)	\$ 10,114
EARNINGS (LOSS) PER SHARE (Note 3):		
Basic	\$ (.07)	\$.00
Diluted	(.07)	.00
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING:		
Basic	3,383,233	3,318,900
Diluted	3,383,233	3,418,109

See Notes to Condensed Consolidated Financial Statements.

CREATIVE COMPUTER APPLICATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Six Months Ended June 30,	
	2005	2004
	(Unaudited)	
NET SYSTEM SALES AND SERVICE REVENUE:		
System sales	\$ 883,707	\$ 1,617,851
Service revenue	2,497,588	2,135,843
	3,381,295	3,753,694
COSTS OF PRODUCTS AND SERVICES SOLD:		
System sales	824,568	976,539
Service revenue	824,693	806,563
	1,649,261	1,783,102
Gross profit	1,732,034	1,970,592
OPERATING EXPENSES		
Selling, general and administrative	1,599,977	1,319,074
Research and development	558,940	514,880
Total operating expenses	2,158,917	1,833,954
Operating income (loss)	(426,883)	136,638
INTEREST AND OTHER INCOME	9,142	1,858
INTEREST EXPENSE	(7,761)	(1,685)
Income (Loss) before provision for income taxes	(425,502)	136,811
PROVISION FOR INCOME TAXES		
NET INCOME (LOSS)	\$ (425,502)	\$ 136,811
EARNINGS (LOSS) PER SHARE (Note 3):		
Basic	\$ (.13)	\$.04
Diluted	(.13)	.04
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING:		
Basic	3,368,567	3,318,900
Diluted	3,368,567	3,423,240

See Notes to Condensed Consolidated Financial Statements.

CREATIVE COMPUTER APPLICATIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Increase (Decrease) in Cash

	Six Months Ended June 30,	
	2005	2004
	(Unaudited)	
OPERATING ACTIVITIES		
Net Income (loss)	\$ (425,502)	\$ 136,811
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	67,260	54,959
Provision for doubtful accounts	21,528	
Amortization of capitalized software costs	178,636	220,080
Increase (decrease) from changes in:		
Receivables	1,004,680	(253,517)
Inventories	(40,339)	4,692
Prepaid expenses and other assets	(58,517)	(47,210)
Accounts payable	(68,349)	75,044
Accrued liabilities	(9,485)	59,816
Deferred service contract income	(396,285)	80,581
Deferred revenue on system sales	143,785	487,909
Net cash provided by operating activities	417,412	819,165
INVESTING ACTIVITIES		
Additions to property and equipment	(169,759)	(46,701)
Additions to capitalized acquisition costs	(199,790)	
Additions to capitalized software costs	(340,421)	(280,624)
Net cash used in investing activities	(709,970)	(327,325)
FINANCING ACTIVITIES		
Payments on notes payable	(100,000)	
Exercise of stock options	92,000	
Net cash used in financing activities	(8,000)	
NET INCREASE (DECREASE) IN CASH	(300,558)	491,840
CASH, beginning of period	1,655,063	889,521
CASH, end of period	\$ 1,354,505	\$ 1,381,361

See notes to Condensed Consolidated Financial Statements.

CREATIVE COMPUTER APPLICATIONS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1-Presentation of Financial Statements

In the opinion of management of Creative Computer Applications, Inc. (the Company or CCA), the accompanying unaudited condensed consolidated financial statements reflect all adjustments (which include only normal recurring accruals) necessary to present fairly the Company's financial position as of June 30, 2005, the results of its operations for the three and six month periods ended June 30, 2005 and 2004, and cash flows for the six months ended June 30, 2005 and 2004. These results have been determined on the basis of accounting principles generally accepted in the United States of America and practices applied consistently with those used in preparation of the Company's Annual Report on Form 10-KSB for the fiscal year ended August 31, 2004 and the Transitional Report on Form 10-QSBT for the period ended December 31, 2004.

The results of operations for the three and six months ended June 30, 2005 are not necessarily indicative of the results expected for any other period or for the entire year.

Note 2- Inventories

Inventories consist primarily of computer hardware held for resale and are stated at the lower of cost or market (net realizable value). Cost is determined using the first-in, first-out method. Supplies are charged to expense as incurred.

The Company also maintains an inventory pool of component parts to service systems previously sold, which is classified as non-current in the accompanying balance sheets. Such inventory is carried at the lower of cost or market and is charged to cost of sales based on usage. Allowances are made for quantities on hand in excess of estimated future usage. At June 30, 2005 and 2004 the inventory allowance was \$180,073 and \$126,273.

Note 3-Earnings per Share

The Company accounts for its earnings per share in accordance with SFAS No.128, which requires presentation of basic and diluted earnings per share. Basic earnings per share is computed by dividing income or loss available to common shareholders by the weighted average number of common shares outstanding for the reporting period. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts, such as stock options, to issue common stock were exercised or converted into common stock.

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Earnings per share has been computed as follows:

	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005	Three Months Ended June 30, 2004	Six Months Ended June 30, 2004
NET INCOME (LOSS)	\$ (238,538)	\$ (425,502)	\$ 10,114	\$ 136,811
Basic weighted average number of common shares outstanding	3,383,233	3,368,567	3,318,900	3,318,900
Dilutive effect of stock options			99,209	104,340
Diluted weighted average number of common shares outstanding	3,383,233	3,368,567	3,418,109	3,423,240
Basic earnings (loss) per share	\$ (.07)	\$ (.13)	\$.00	\$.04
Diluted earnings (loss) per share	\$ (.07)	\$ (.13)	\$.00	\$.04

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For the three and six months ended June 30, 2005 and 2004, options to purchase 314,000 and 100,000 shares of common stock at per share prices ranging from \$.72 to \$1.76 were not included in the computation of diluted earnings (loss) per share because inclusion would have been anti-dilutive.

Note 4-Debt Obligations

The Company's line of credit with its bank provides for \$1,000,000 on a revolving basis through February 1, 2006. On June 30, 2005, the total amount due to the bank was \$200,000.

Note 5-Stock-Based Compensation

As allowed by Statement of Financial Accounting Standards No. 123 (SFAS 123), the Company has adopted the intrinsic value method of accounting for employee stock options under the principles of APB Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and discloses the pro forma effect on net income (loss) and income (loss) per share as if the fair value based method had been applied. For equity instruments, including stock options, issued to non-employees, the fair value of the equity instruments or the fair value of the consideration received, whichever is more readily determinable, is used to determine the value of services or goods received and the corresponding charge to operations.

The following table illustrates the effect on net income (loss) and income (loss) per share as if the Company had applied the fair value recognition provision of SFAS No. 123 to stock-based employee compensation:

	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005	Three Months Ended June 30, 2004	Six Months Ended June 30, 2004
Net income (loss), as reported	\$ (238,538)	\$ (425,502)	\$ 10,114	\$ 136,811
Add: Stock-based compensation expense included in reported net income, net of related tax effects				
Less: total stock based employee compensation expense determined under fair value based method for all awards	(11,011)	(22,021)	(19,513)	(39,027)
Net loss, pro forma	\$ (249,549)	\$ (447,523)	\$ (9,399)	\$ 97,784
Basic net earnings (loss) per share, as reported	\$ (.07)	\$ (.13)	\$.00	\$.04
Basic net earnings (loss) per share, pro forma	\$ (.07)	\$ (.13)	\$.00	\$.03
Diluted net earnings (loss) per share, as reported	\$ (.07)	\$ (.13)	\$.00	\$.04

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Diluted net earnings (loss) per share, pro forma	\$	(.07)	\$	(.13)	\$.00	\$.03
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The Company issues all of its options at fair market value at the time of grant; therefore, no expense has been recorded under the intrinsic value method for the three and six months ended June 30, 2005 and 2004. As required by SFAS 123, the Company provides the following disclosure of estimated values for these awards: The fair value of each option was estimated on the date of grant using a Black-Scholes option-pricing model with the

following weighted average assumptions for 2004: risk free interest rates ranging from 3.4% to 6.1%, expected lives of 5 years; volatility ranging from 67% to 126% and no assumed dividends. The weighted-average grant-date fair value of options granted during 2004 was estimated to be \$.93. There were no options granted in the six months ended June 30, 2005.

Note 6-Commitments and Contingencies

In accordance with the bylaws of the Company, officers and directors are indemnified for certain events or occurrences arising as a result of the officer or director's serving in such capacity. The term of the indemnification period is for the lifetime of the officer or director. The maximum potential amount of future payments the Company could be required to make under the indemnification provisions of its bylaws is unlimited. However, the Company has a director and officer liability insurance policy that reduces its exposure and enables it to recover a portion of any future amounts paid. As a result of its insurance policy coverage, the Company believes the estimated exposure for the indemnification provisions of its bylaws is minimal and, therefore, the Company has not recorded any related liabilities.

The Company enters into indemnification provisions under agreements with various parties in the normal course of business, typically with customers and landlords. Under these provisions, the Company generally indemnifies and holds harmless the indemnified party for losses suffered or incurred by the indemnified party as a result of the Company's activities or, in some cases, as a result of the indemnified party's activities under the agreement. These indemnification provisions often include indemnifications relating to representations made by the Company with regard to intellectual property rights. These indemnification provisions generally survive termination of the underlying agreement. The maximum potential amount of future payments the Company could be required to make under these indemnification provisions cannot be estimated. The Company maintains general liability, errors and omissions, and professional liability insurance in order to mitigate such risks. The Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification agreements. As a result, the Company believes the estimated exposure under these agreements is minimal. Accordingly, the Company has not recorded any related liabilities.

Note 7-New Accounting Pronouncements

In December 2004 the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment (SFAS No. 123(R))*. SFAS No. 123(R) requires compensation cost relating to unvested share-based payment transactions that are outstanding as of the effective date and newly issued transactions to be recognized in the financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. SFAS No. 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. SFAS No. 123(R) replaces SFAS No. 123 and supersedes APB 25. SFAS No. 123, as originally issued in 1995, established fair-value-based method of accounting for share-based payment transactions with employees. However, SFAS No. 123 permitted entities the option of continuing to apply the guidance in APB 25, as long as the footnotes to financial statements disclosed what net income would have been had the fair-value-based method been used. As disclosed in footnote 5, the Company elected the option of disclosure only under SFAS No. 123. Public companies will be required to apply SFAS No. 123(R) as of the first annual reporting period that begins after June 15, 2005, or December 15, 2005 for small business issuers. In April 2005, the SEC issued a Final Rule Release, Amendment to Rule 4-01(a) of Regulation S-X regarding the compliance date for Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment. This rule extends the date for compliance with SFAS No. 123R until the beginning of the public companies' next fiscal year, instead of the next reporting period, that begins after June 15, 2005, or December 15, 2005 for small business issuers. The Company is currently evaluating the impact of this statement.

In March 2005, the SEC staff issued a Staff Accounting Bulletin (SAB 107) which expressed views of the staff regarding the interaction between SFAS No. 123R and certain SEC rules and regulations and provide the staff's views regarding the valuation of share-based payment

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arrangements for public companies. In particular, SAB 107 provides guidance related to share-based payment transactions with non-employees, the transition from nonpublic to public entity status, valuation methods (including assumptions such as expected volatility and expected term), the accounting for certain redeemable financial instruments issued under share-based payment

arrangements, the classification of compensation expense, non-GAAP financial measures, first-time adoption of SFAS No. 123R in an interim period, capitalization of compensation cost related to share-based payment arrangements, the accounting for income tax effects of share-based payment arrangements upon adoption of SFAS No. 123R, the modification of employee share options prior to adoption of SFAS No. 123R and disclosures in Management's Discussion and Analysis subsequent to adoption of SFAS No. 123R.

In December 2004, the FASB issued SFAS No. 151, Inventory Costs, an amendment of ARB No. 43, Chapter 4, which requires that abnormal amounts of idle facility expense, freight, handling costs and wasted material (spoilage) be recognized as current-period charges. In addition, the statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS No. 151 is effective for fiscal years beginning after June 15, 2005. The Company will adopt this statement as required, and the Company does not believe the adoption will have a material effect on the Company's results of operations or financial condition.

In December 2004, the FASB issued SFAS No. 153, Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29, which eliminates the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The statement defines a nonmonetary exchange with commercial substance as one in which the future cash flows of an entity are expected to change significantly as a result of the exchange. SFAS No. 153 is effective for fiscal years beginning after June 15, 2005. The Company will adopt this statement as required, and it does not believe the adoption will have a material effect on the Company's results of operation or financial condition.

In May 2005, the Financial Accounting Standards Board issued Statement No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20, Accounting Changes, and Statement No. 3, Reporting Accounting Changes in Interim Financial Statements, or SFAS No. 154. SFAS No. 154 changes the requirements for the accounting for, and reporting of, a change in accounting principle. Previously, most voluntary changes in accounting principles were required to be recognized by way of a cumulative effect adjustment within net income during the period of the change. SFAS No. 154 generally requires retrospective application to prior periods' financial statements of voluntary changes in accounting principles. SFAS No. 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005; however, SFAS No. 154 does not change the transition provisions of any existing accounting pronouncements. We do not believe adoption of SFAS No. 154 will have a material effect on our consolidated results of operations or financial position.

Note 8-Merger

On January 10, 2005, the Company entered into a letter of intent to merge with StorCOMM, Inc. of Jacksonville, Florida, a private company providing Picture Archive Communication Systems (PACS) and Clinical Image Management Systems for the medical imaging market (the StorCOMM Merger). CCA will be the surviving entity and StorCOMM shareholders will own one-half of the merged entity. The transaction is subject to the completion and execution of a definitive merger agreement and shareholder approval. It is expected that the post-merger company will offer integrated applications and services to a broad sector of the healthcare provider market. The merger is expected to be completed before the end of the fiscal year. For the six-month period ended June 30, 2005, the Company deferred approximately \$200,000 in merger costs primarily related to legal and third party due diligence expenses.

Item 2. Management's Discussion and Analysis or Plan of Operation

This Quarterly Report on Form 10-QSB contains forward-looking statements, which reflect management's current views about future events and financial results. Management makes these statements in reliance on the safe harbor created by the Private Securities Litigation Reform Act of

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1995. Forward-looking statements include views on future financial results, financing sources, product development, capital requirements, market growth and the like, and are generally identified by phrases such as anticipates, believes, estimates, expects, intends, plans and similar words. Forward-looking statements are merely predictions and therefore inherently subject to uncertainties and other factors which could cause the actual results to differ materially from the forward-looking statement. These uncertainties and other factors include, among other things:

Unexpected technical and marketing difficulties inherent in major product development efforts such as those described about CyberLAB 7.0.

The potential need for changes in our long-term strategy in response to future developments.

Future advances in clinical information technology and procedures, as well as potential changes in government regulations and healthcare policies, both of which could adversely affect the economics of the products offered by CCA.

Rapid technological change in the microelectronics and software industries

Increasing competition from current as well as future competitors, and

The ability to complete the StorCOMM Merger and to integrate the operations of the two companies.

Set forth below are other significant uncertainties and factors affecting forward-looking statements. The readers should understand that uncertainties and other factors identified in this Quarterly Report on Form 10-QSB are not a comprehensive list of all the uncertainties and other factors that may affect forward-looking statements. We do not undertake any obligation to update or revise any forward-looking statements or the list of uncertainties and other factors that could affect those statements.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

CCA generates revenues primarily from the sale of its Clinical Information Systems (CIS), which includes the licensure of proprietary application software, the licensure of third party software, and the sale of servers upon which the application software operates. In connection with its sales of CIS products, the Company provides implementation services for the installation, integration, and training of end users personnel. The Company generates sales of ancillary software and hardware, including its data acquisition products, to its CIS clients and to third parties. The Company also generates recurring revenues from the provision of comprehensive post-implementation services to its CIS clients, pursuant to extended service agreements.

Because of the nature of its business, CCA makes significant investments in research and development for new products and enhancements to existing products. Historically, CCA has funded its research and development programs through cash flow primarily generated from operations. Management anticipates that future expenditures in research and development will either continue at current levels or may increase for the foreseeable future, and will be funded primarily out of the Company's cash flow.

CCA's results of operations for the second fiscal quarter and six-month period ended June 30, 2005 were marked by a decrease in sales and operating income over the comparable period of 2004. The Company's decrease in revenues for the second fiscal quarter and six-month period was due to a number of factors, the primary factor being the loss of members of our sales force. During the second quarter of 2005, the

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Company experienced an unexpected significant turnover in its sales force, including the loss of its Vice President of Sales, which affected its ability to close near term sales opportunities. The Company has since hired a new Vice President of Sales who began employment on July 1, 2005 and is in the process of restaffing its direct sales force. In addition, the Company has invested additional funds into marketing activities to rebuild its sales pipeline. Despite the shortfall in our new system sales, there were positive areas in our business during the first half of 2005. For instance, services revenues increased for the quarter and six-month period by \$187,500 or 17.5% and \$361,745 or 16.9%, respectively. The Company also booked three new upgrades of CyberLAB 7.0 during the period reflected in our system sales for the second quarter of 2005 and had one new system sale and other ancillary orders in backlog at the end of the quarter. The Company anticipates that as more clients migrate to CyberLAB 7.0, these clients will acquire additional hardware and professional services from the Company in order to deploy the new software. Generally, sales cycles for CIS products are lengthy and on average exceed one year from inception to closure. Because of the complexity of the sales process, a number of factors can delay the closing of transactions that are beyond the control of the Company.

Results of Operations

The following table sets forth certain line items in our condensed consolidated statement of operations as a percentage of total revenues for the periods indicated:

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	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005	Three Months Ended June 30, 2004	Six Months Ended June 30, 2004
Revenues:	19.1%	26.1%	40.3%	43.1%
System sales	80.9	73.9	59.7	56.9
Service revenues				
Total revenues	100.0	100.0	100.0	100.0
Cost of products and services sold:				
System sales	23.9	24.4	29.6	26.0
Service revenues	26.3	24.4	22.2	21.5
Total cost of products and services	50.2	48.8	51.8	47.5
Gross profit	49.8	51.2	48.2	52.5
Operating expenses:				
Selling, general and administrative	49.6	47.3	33.2	35.2
Research and development	15.7	16.5	14.4	13.7
Total operating expenses	65.3	63.8	47.6	48.9
Operating income (loss)	(15.5)	(12.6)	0.6	3.6
Income (loss) before provision for income taxes	(15.3)	(12.6)	0.6	3.6
Provision for income taxes				
Net income (loss)	(15.3)	(12.6)	0.6	3.6

Revenues

Sales for the second fiscal quarter ended June 30, 2005 decreased to \$1,556,007, as compared to \$1,794,994 for the comparable quarter ended June 30, 2004, an overall decrease of approximately \$238,987 or 13.3%. For the six-month period ended June 30, 2005, sales decreased \$372,399 or 9.9% compared to the same period of 2004. When analyzed by product category for the quarter, sales of CIS products decreased by \$457,150, or 69.9% and a decrease in other revenues of \$1,918 or 50.2%, partially offset by an increase in sales of data acquisition products of \$32,581, or 49.4%, and an increase in service revenues of \$187,500, or 17.5% when compared to the same quarter of fiscal 2004. When analyzed by product category for the six-month period ended June 30, 2005, sales of CIS products decreased by \$805,917, or 55.9% and a decrease in other revenues of \$1,500 or 23.5%, partially offset by an increase in sales of data acquisition products of \$73,273, or 43.0%, and an increase in service revenues of \$361,745, or 16.9% when compared to the same period of fiscal 2004. The decrease in sales of CIS products was primarily attributable to the turnover in the sales force as described above under *Overview*. The Company is in the process of rebuilding its direct sales force. The increase in service revenues is attributable to a greater number of client accounts under contract and an increase in the average fees charged for such contracts. Service revenues are expected to continue to increase as and when the Company's installed base of CIS installations increases.

The increase in the sales of data acquisition products is primarily attributable to a greater number of units shipped to OEM customers, however, management believes that going forward, there will be reduced sales of data acquisition products as there has been a technological shift to software-based clinical instrument interfaces. Furthermore, fewer OEM customers remain active in the marketplace or no longer use CCA's data acquisition products. Management does not believe the data acquisition product business is a material part of CCA's business today and it will not be in the future, as the Company's emphasis is being placed on its CIS products and related services.

Although the Company continues to invest in sales and marketing activities, management is cautious about the near-term outlook for the continued sale of CIS products during the second half of the 2005 fiscal year as it focuses on rebuilding its direct sales force. The Company's future operating results will continue to be subject to quarterly variations based upon a wide variety of factors, including the volume mix and timing of orders received during any quarter, and the temporary delays in the closing of new CIS sales. In addition, the Company's revenues associated with CIS sales may be

delayed due to client related issues such as client staff availability for training, IT infrastructure readiness, and the performance of third party contractors, all of which are issues outside of the control of CCA.

Costs of products and services sold

Cost of sales for the second quarter and six-month period ended June 30, 2005 decreased by \$148,632 or 16.0% and \$133,841 or 7.5%, respectively, as compared to the same periods of fiscal 2004. For the quarter and six-month period, the decrease in cost of sales was primarily attributable to a decrease in material costs of \$118,201 or 68.1% and \$105,446 or 40.3%, respectively, and a decrease in other costs of \$45,768 or 14.3% and \$48,763 or 7.8%, respectively. Such decreases were partially offset by an increase in labor costs, for the quarter and six-month period, of \$15,338 or 3.5% and \$20,369 or 2.3%, respectively. The decrease in material costs was attributable to the decrease in sales of CIS products discussed above. The increase in labor costs was attributable to additions of personnel to the Company's support and implementation departments. The decrease in other costs of sales was attributable to decreased expenses related to telephone costs as a result of better rates negotiated under a new contract for telephone and data services. For the current quarter and six-month period, cost of sales as a percentage of sales was 50% and 49%, respectively, as compared to 52% and 48%, respectively, for the comparable periods of 2004. The overall percentage decrease in cost of sales, as a percentage of sales, in the six-month period was attributable to a reduced number of sales of CIS products requiring hardware. The Company could potentially experience quarterly variations in gross margin as a result of the factors discussed above.

Selling, general and administrative expenses

Selling, general and administrative expenses increased by \$174,567 or 29.3% and \$280,903 or 21.3%, respectively, for the current fiscal quarter and six-month period ended June 30, 2005 as compared to the same periods of fiscal 2004. The increase in selling, general and administrative expenses were primarily attributable to consultant expenses related to Sarbanes-Oxley Act of 2002 Section 404 compliance requirements, additional expenses for legal and accounting fees as a result of the Company changing its fiscal year-end, expenses related to the StorCOMM merger, expenses related to the implementation of a new customer relationship management system to replace its aged help desk application, and the addition of a new product consultant and radiology product manager. Management anticipates that it will incur increases in auditing and consultant expenses in the second half of fiscal 2005 that are related to Sarbanes-Oxley Act of 2002 Section 404 compliance requirements. It is also likely that the Company will incur significant additional expenses in the second half of fiscal 2005 related to the StorCOMM Merger that will be expensed when incurred. Management also anticipates an increase in insurance costs in the current fiscal year.

Research and development expenses

Research and development expenses decreased by \$14,437, or 5.6%, during the second fiscal quarter of 2005 as compared to the same quarter of fiscal 2004. For the six-month period ended June 30, 2005, research and development expenses increased by \$44,060, or 8.6%, as compared to the same period of fiscal 2004. The increase for the six-month period is attributable to increases in salaries, other personnel related expenses, and the addition of new personnel in product engineering. In the current quarter, the product engineers were focused on completing application enhancements thereby increasing the capitalized software. For the comparable second quarters of 2005 and 2004, the Company capitalized software costs of \$214,421 and \$131,999, respectively, which are generally amortized over the estimated useful life, not to exceed five years. Such costs were attributable to enhancements and new modules for the Company's CIS products, and new applications under development, as well as the completion of new software that integrates the Company's radiology product CyberRAD with the StorCOMM PACS system.

Income taxes

For the second quarter and six-month period ended June 30, 2005, the Company did not record a tax provision due to the pretax net loss. In 2004, the Company was operating under a different fiscal year-end and at the time, the Company was in a pretax net loss position and therefore the Company did not record a tax provision.

The Company evaluates the realization of the net deferred tax asset, taking into consideration prior earnings history, projected operating results, and the reversal of temporary tax differences. At June 30, 2005, the Company evaluated the net deferred tax asset, taking into consideration operating results, and determined that its current valuation allowance

should be maintained. The Company believes it is more likely than not that the net deferred tax asset of \$793,877 will be realized in future periods. The Company will continue to assess the realizability of the deferred tax asset quarterly.

Net income (loss)

As a result of the factors discussed above, the Company incurred a net loss of \$238,538 or basic and diluted loss per share of \$.07 in the second fiscal quarter of 2005 as compared to net income of \$10,114 or basic and diluted earning per share of \$.00 for the second fiscal quarter of 2004. For the six-month period ended June 30, 2005, the Company incurred a net loss of \$425,502 or basic and diluted loss per share of \$.13 as compared to net income of \$136,811 or basic and diluted earning per share of \$.04 for the same period of 2004.

Capital Resources and Liquidity

The Company's primary need for capital has been to invest in software development, and in computers and related equipment for its internal use. The Company invested \$340,421 and \$280,624 in software development during the six-month periods ended June 30, 2005 and 2004, respectively. These expenditures related to the new browser version of the Company's LIS product, CyberLAB 7.0, and new software that integrates the Company's radiology product CyberRAD with the StorCOMM PACS system.

The Company anticipates expending additional sums during the remainder of fiscal 2005 on product enhancements to all its products and the further enhancements of the new browser version of the Company's CyberLAB 7.0 product. During the six-month period ended June 30, 2005, the Company invested an aggregate of \$169,759 in additions to fixed assets, primarily consisting of computers and software related to the new customer relationship management system, which is replacing its aged help desk application, as compared to an investment of \$46,701 in the comparable period of 2004. Furthermore, the Company deferred approximately \$200,000 in merger costs primarily related to legal and third party due diligence expenses.

As of June 30, 2005, the Company's working capital amounted to \$769,720, compared to \$1,589,832 as of December 31, 2004. The Company's current ratio was 1.3 at June 30, 2005 compared to 1.6 at December 31, 2004. At June 30, 2005, the Company's credit facilities with its bank consisted of a revolving line of credit of \$1,000,000, of which there was \$200,000 outstanding. The bank credit agreement expires on February 1, 2006. In addition, the Company is in negotiations with a small group of investors for the issuance of \$3,000,000 in common stock and warrants contingent upon the completion of the StorCOMM Merger.

Cash flows from operating activities were \$417,412 for the six-month period ended June 30, 2005 compared to cash flows of \$819,165 for the comparable period of fiscal 2004. The decrease in cash flow from operating activities was primarily attributable to the net change in accrued receivables, inventories, payables, and deferred revenues offset by the reduction in income from operations in the six-month period ended June 30, 2005 compared to the same period of fiscal 2004.

Net cash used in investing activities totaled \$709,970 for the six-month period ended June 30, 2005, compared to \$327,325 used in investing activities during the comparable period of 2004. The increase in cash used in investing activities was due to increased investment in property and equipment related to the new customer relationship management system, additional investment in capitalized software, and additions to capitalized acquisition costs.

Net cash used in financing activities amounted to \$8,000 during the six-month period ended June 30, 2005. There were no financing activities during the comparable period of fiscal 2004. The change from fiscal 2004 to fiscal 2005 resulted primarily from payments on its revolving line of credit with the bank offset by cash flows from exercises of stock options.

The Company's primary source of working capital has been generated from earnings, and from borrowings on its line of credit. The Company produced cash flows amounting to \$417,412 to fund its operations in six-month period ended June 30, 2005. Management believes that its projected cash flow from operations, together with its bank credit facilities, should be sufficient to fund its working capital requirements for its 2005 fiscal year. However, an unanticipated decline in sales or continued delays in closing new transactions, delays in implementations where payments are tied to delivery and/or performance of services, or cancellations of contracts could have a negative effect on cash flow from operations.

and could in turn create short-term liquidity problems. If such events were to occur, the Company may have to seek alternative financing.

Seasonality, Inflation and Industry Trends

The Company's sales are generally higher in the winter and spring due to budgetary cycles of its clients. Inflation has not had a material effect on the Company's business since the Company has been able to adjust the prices of its products and services in response to inflationary pressures. Management believes that most phases of the healthcare segment of the computer industry will continue to be highly competitive, and that potential healthcare reforms including those promulgated by Health Insurance Portability and Accountability Act (HIPAA) may have a long-term positive impact on its business. With respect to the compliance issues brought about by HIPAA, the Company has invested heavily in new application modules to assist its clients in meeting their regulatory goals. Management believes that the new modules will be key selling points and will provide a competitive advantage. In addition, management believes that the healthcare information technology industry will be marked with more significant technological advances, which will improve the quality of service and reduce costs. The Company is poised to meet these challenges by continuing to employ new technologies when they become available, diversifying its product offerings, improving and expanding its services, and by constantly enhancing its software applications.

Critical Accounting Policies and Estimates

Management's discussion and analysis of CCA's financial condition and results of operations are based upon the condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, management evaluates estimates, including those related to the valuation of inventory and the allowance for uncollectible accounts receivable. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements:

Inventory

The Company's inventory is comprised of a current inventory account that consists of items that are held for resale and a long-term inventory account that consists of items that are held for repairs and replacement of hardware components that are serviced by the Company under long-term Extended Service Agreements with its clients. Current inventory is valued at the lower of cost to purchase or the current estimated market value of the inventory items. Inventory is evaluated on a continual basis and adjustments to recorded costs are made based on management's estimate of future sales value, or in the case of the long-term component inventory, on management's estimation of the usage of specific inventory items and net realizable value. Management reviews inventory quantities on hand and makes determination of the excess or obsolete items in the inventory, which, are specifically reserved. In addition, adjustments are made for the difference between the cost of the inventory and the estimated market value and charged to operations in the period in which the facts that give rise to the adjustments become known. At June 30, 2005, the inventory reserve was approximately \$180,000.

Accounts Receivable

Accounts receivable balances are evaluated on a continual basis and allowances are provided for potentially uncollectible accounts based on management's estimate of the collectability of customer accounts. If the financial condition of a customer were to deteriorate, resulting in an impairment of their ability to make payments, an additional allowance may be required. Allowance adjustments are charged to operations in the period in which the facts that give rise to the adjustments become known. The accounts receivable balance at June 30, 2005 was \$710,560, net of an allowance for doubtful accounts of approximately \$48,000.

Revenue Recognition

Revenues are derived primarily from the sale of CIS products and the provision of services. The components of the system sales revenues are the licensing of computer software, installation, and the sale of computer hardware and sublicensed software. The components of service revenues are software support and hardware maintenance, training, and implementation services. The Company recognizes revenue in accordance with the provisions of Statement of Position (SOP) relating to revenue recognition and its labor relations are satisfactory; (c) there are no workers' compensation claims pending against Atlantic nor is Atlantic aware of any facts that would give rise to such a claim; (d) to the knowledge of Atlantic, no employee of Atlantic is subject to any secrecy or noncompetition agreement or any other agreement or restriction of any kind that would impede in any way the ability of such employee to carry out fully all activities of such employee in furtherance of the business of Atlantic; and (f) no employee or former 26 employee of Atlantic has any claim with respect to any intellectual property rights of Atlantic set forth in Schedule 4.13 hereto.

4.16 Affiliate Transactions. Except as set forth in Schedule 4.16 hereto, and other than pursuant to this Agreement, no officer, director or employee of Atlantic, any Atlantic Subsidiary or any member of the immediate family of any such officer, director or employee, or any entity in which any of such persons owns any beneficial interest (other than any publicly-held corporation whose stock is traded on a national securities exchange or in the over-the-counter market and less than one percent of the stock of which is beneficially owned by any of such persons) (collectively "Atlantic Insiders"), has any agreement with Atlantic (other than normal employment arrangements) or any interest in any property, real, personal or mixed, tangible or intangible, used in or pertaining to the business of Atlantic (other than ownership of capital stock of Atlantic). Atlantic is not indebted to any Atlantic Insider (except for amounts due as normal salaries and bonuses and in reimbursement of ordinary business expenses) and no Atlantic Insider is indebted to Atlantic (except for cash advances for ordinary business expenses). None of the insiders has any direct or indirect interest in any competitor, supplier or customer of Atlantic or in any person, firm or entity from whom or to whom Atlantic leases any property, or in any other person, firm or entity with whom Atlantic transacts business of any nature. For purposes of this Section 4.16, the members of the immediate family of an officer, director or employee shall consist of the spouse, parents and children of such officer, director or employee.

4.17 Compliance with Laws; Permits. (a) Except for any noncompliance that would not reasonably be expected to have a Material Adverse Effect on Atlantic, Atlantic, each Atlantic Subsidiary and their respective officers, directors, agents and employees have complied with all applicable laws, regulations and other requirements, including, but not limited to, federal, state, local and foreign laws, ordinances, rules, regulations and other requirements pertaining to equal employment opportunity, employee retirement, affirmative action and other hiring practices, occupational safety and health, workers' compensation, unemployment and building and zoning codes, and no claims have been filed against Atlantic, and Atlantic has not received any notice, alleging a violation of any such laws, regulations or other requirements. Atlantic is not relying on any exemption from or deferral of any such applicable law, regulation or other requirement that would not be available to Manhattan after it acquires Atlantic's properties, assets and business. (b) Each of Atlantic and the Atlantic Subsidiaries has, in full force and effect, all licenses, permits and certificates from federal, state, local and foreign authorities (including, without limitation, federal and state agencies regulating occupational health and safety) necessary to permit it to conduct its business and own and operate its properties (collectively, the "Atlantic Permits"). A complete list of all the Permits is set forth in Schedule 4.17 hereto. Each of Atlantic and the Atlantic Subsidiaries has conducted its business in compliance with terms and conditions of the Atlantic Permits.

4.18 Books and Records. The books of account, minute books, stock record books, and other records of Atlantic, all of which have been made available to Manhattan, have been properly kept and contain no inaccuracies except for inaccuracies that would not, individually or 27 in the aggregate, reasonably be expected to have a Material Adverse Effect on Atlantic. At the Closing, all of Atlantic's records will be in the possession of Atlantic.

4.19 Real Property. Neither Atlantic nor any Atlantic Subsidiary owns any real property. Schedule 4.19 contains an accurate list of all leaseholds and other interests of Atlantic and each Atlantic Subsidiary in any real property. Atlantic and such Atlantic Subsidiaries have good and valid title to those leaseholds and other interests free and clear of all liens and encumbrances, and the real property to which those leasehold and other interests pertain constitutes the only real property used in Atlantic's business.

4.20 Insurance. The insurance policies owned and maintained by Atlantic that are material to Atlantic are in full force and effect, all premiums due and payable thereon have been paid (other than retroactive or retrospective premium adjustments that Atlantic is not currently required, but may in the future be required, to pay with respect to any period ending prior to the date of this Agreement), and Atlantic has received no notice of cancellation or termination with respect to any such policy that has not been replaced on substantially similar terms prior to the date of such cancellation.

4.21 Environmental Matters. None of the operations of Atlantic or any Atlantic Subsidiary involves the generation, transportation, treatment, storage or disposal of hazardous waste, as defined under 40 C.F.R. Parts 260-270 or any state, local or foreign equivalent.

4.22 Proprietary Information and Inventions. Each current Atlantic employee, consultant, and advisory board member is party to either a non-disclosure agreement in the form attached as Schedule 4.22 or an alternative employment agreement with Atlantic containing comparable non-disclosure provisions. To Atlantic's Knowledge, no current or former Atlantic employee, consultant or advisory board member who is party to a non-disclosure agreement has breached that non-disclosure agreement. To Atlantic's Knowledge, no current Atlantic employee, consultant or advisory board member who is party to an alternative employment agreement with Atlantic has breached the non-disclosure provisions of that agreement.

4.23 Vote Required. The affirmative vote of a majority of the votes that holders of the outstanding shares of Atlantic Common Stock and Series A convertible preferred stock of Atlantic, voting together as one class, are entitled to cast is the only vote of the holders of any class or series of Atlantic capital stock necessary to approve the matters to be considered at the Atlantic Stockholders Meeting.

4.24 Tax Free Reorganization. Neither Atlantic nor, to Atlantic's Knowledge, any of its Affiliates has through the date of this Agreement taken or agreed to take any action that would prevent the Merger from qualifying as a reorganization under Section 368(a) of the Code.

4.25 Full Disclosure. The representations and

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warranties of Atlantic and MPAC contained in this Agreement (and in any schedule, exhibit, certificate or other instrument to be delivered under this Agreement) are true and correct in all material respects, and such representations and warranties do not omit any material fact necessary to make the statements contained therein, in light of the circumstances under which they were made, not misleading. 28 There is no fact of which Atlantic or MPAC has Knowledge that has not been disclosed to Manhattan pursuant to this Agreement, including the schedules hereto, all taken together as a whole, which has had or could reasonably be expected to have a Material Adverse Effect on Atlantic or MPAC, or materially adversely affect the ability of Atlantic or MPAC to consummate in a timely manner the transactions contemplated hereby. ARTICLE V CONDUCT OF BUSINESS PENDING THE MERGER 5.1 Conduct of Business by Atlantic. From the date of this Agreement to the Effective Date, unless Manhattan shall otherwise agree in writing or as otherwise expressly contemplated or permitted by other provisions of this Agreement, including but not limited to this Section 5.1, Atlantic shall not, directly or indirectly, (a) amend its Certificate of Incorporation or Bylaws, except as set forth on Schedule 5.1, (b) split, combine or reclassify any outstanding shares of capital stock of Atlantic, (c) declare, set aside, make or pay any dividend or distribution in cash, stock, property or otherwise with respect to the capital stock of Atlantic, (d) default in its obligations under any material debt, contract or commitment which default results in the acceleration of obligations due thereunder, except for such defaults arising out of Atlantic's entry into this Agreement for which consents, waivers or modifications are required to be obtained as set forth on Schedule 4.2, (e) conduct its business other than in the ordinary course on an arms-length basis and in accordance in all material respects with all applicable laws, rules and regulations and Atlantic's past custom and practice (except that Atlantic may license its rights to the NCT technologies and transfer its shares of stock in CryoComm, Inc. to Persons wholly or partially owned by one or more Atlantic directors or officers in return for a 10% share of any royalty, milestone or other revenues generated by the NCT technologies and shares of CryoComm, Inc.), (f) issue or sell any additional shares of, or options, warrants, conversions, privileges or rights of any kind to acquire any shares of, any of its capital stock, except as otherwise set forth in Schedule 5.1 hereto or in connection with the exercise or conversion of Atlantic securities outstanding on the date of this Agreement or payment of stock dividends on Atlantic's Series A convertible preferred stock in accordance with the terms of the certificate of designation of Atlantic's Series A convertible preferred stock, (g) acquire (by merger, exchange, consolidation, acquisition of stock or assets or otherwise) any corporation, partnership, joint venture or other business organization or division or material assets thereof or (h) make or change any material tax elections, settle or compromise any material tax liability or file any amended tax return. 5.2 Conduct of Business by Manhattan. From the date of this Agreement to the Effective Date, unless Atlantic shall otherwise agree in writing or as otherwise expressly contemplated or permitted by other provisions of this Agreement, including but not limited to this Section 5.2, Manhattan shall not, directly or indirectly, (a) amend its Certificate of Incorporation or Bylaws, (b) split, combine or reclassify any outstanding shares of capital stock of Manhattan, (c) declare, set aside, make or pay any dividend or distribution in cash, stock, property or otherwise with respect to the capital stock of Manhattan, (d) default in its obligations under any material debt, contract or commitment which default results in the acceleration of obligations due thereunder, except for such defaults arising out of Manhattan's entry into this Agreement for which consents, waivers or modifications are required to be obtained as set forth on Schedule 3.2, (e) conduct its business other than in the ordinary course on an arms-length basis and in accordance in all material respects with all applicable laws, rules and regulations and Manhattan's past custom and practice, (f) issue or sell any additional shares of, or options, warrants, conversions, privileges or rights of any kind to acquire any shares of, any of its capital stock, except as otherwise described on Schedule 5.2 hereto or in connection with exercise or conversion of Manhattan securities outstanding on the date of this Agreement, (g) acquire (by merger, exchange, consolidation, acquisition of stock or assets or otherwise) any corporation, partnership, joint venture or other business organization or division or material assets thereof or (h) make or change any material tax elections, settle or compromise any material tax liability or file any amended tax return. ARTICLE VI ADDITIONAL COVENANTS AND AGREEMENTS 6.1 Governmental Filings. Each party will use all reasonable efforts and will cooperate with the other party in the preparation and filing, as soon as practicable, of all filings, applications or other documents required under applicable laws, including, but not limited to, the Exchange Act, to consummate the transactions contemplated by this Agreement. Prior to submitting each filing, application, registration statement or other document with the applicable regulatory authority, each party will, to the extent practicable, provide the other party with an opportunity to review and comment on each such application, registration statement or other document to the extent permitted by applicable law. Each party will use all reasonable efforts and will cooperate with the other party in taking any other actions necessary to obtain such regulatory or other approvals and consents at the earliest practicable time, including participating in any required hearings or proceedings. Subject to the terms and conditions herein provided, each party will use all reasonable efforts to take, or cause to be taken, all actions and to do, or cause to be done, all things necessary, proper or advisable to consummate and make effective as promptly as practicable the transactions contemplated by this Agreement. 6.2 Expenses. Except as otherwise provided in this Agreement, all costs and expenses incurred in connection with this Agreement and the transactions contemplated hereby shall be paid by the party incurring such costs and expenses. 6.3 Due Diligence; Access to Information; Confidentiality. (a) Between the date hereof and the date of filing the Proxy Statement with the SEC, Manhattan and Atlantic shall afford to the other party and their authorized representatives the opportunity to conduct and complete a due diligence investigation of the other party as described herein. In light of the foregoing, each party shall permit the other party full access on reasonable notice and at reasonable hours to its properties and shall disclose and make available (together with the right to copy) to the other party and its officers, employees, attorneys, accountants and other representatives, all books, papers and records relating to the assets, stock, properties, operations, obligations and liabilities of such party and its subsidiaries, including, without limitation, all books of account (including, without limitation, the general ledger), tax records, minute books of directors' and stockholders' meetings, organizational documents, bylaws, contracts and agreements, filings with any regulatory authority, accountants' work papers, litigation files (including, without limitation, legal research memoranda), attorney's audit response letters, documents relating to assets and title thereto (including, without limitation, 30 abstracts, title insurance policies, surveys, environmental reports, opinions of title and other information relating to the real and personal property), plans affecting employees, securities transfer records and stockholder lists, and any books, papers and records relating to other assets or business activities in which such party may have a reasonable interest, and otherwise provide such assistance as is reasonably requested in order that each party may have a full opportunity to make such investigation and evaluation as it shall reasonably desire to make of the business and affairs of the other party; provided, however, that the foregoing rights granted to each party shall, whether or not and regardless of the extent to which the same are exercised, in no way affect the nature or scope of the representations, warranties and covenants of the respective party set forth herein. In addition, each party and its

officers and directors shall cooperate fully (including providing introductions, where necessary) with such other party to enable the party to contact third parties, including customers, prospective customers, specified agencies or others as the party deems reasonably necessary to complete its due diligence; provided that such party agrees not to initiate such contacts without the prior approval of the other party, which approval will not be unreasonably withheld. (b) Either Atlantic or Manhattan may, in its sole discretion, elect not to proceed with the Merger based upon its due diligence investigation performed pursuant to Section 6.3(a) above, if the results of such due diligence investigation, in Atlantic's or Manhattan's reasonable judgment, reveals any event, condition or occurrence (not previously disclosed in this Agreement or the schedules attached hereto) that would reasonably be expected to have a Material Adverse Effect on the other party, by providing such other party with written notice thereof on or before the date of the Proxy Statement. (c) Prior to Closing and if, for any reason, the transactions contemplated by this Agreement are not consummated, neither Atlantic nor Manhattan nor any of their officers, employees, attorneys, accountants and other representatives shall disclose to third parties or otherwise use any confidential information received from the other party in the course of investigating, negotiating, and performing the transactions contemplated by this Agreement; provided, however, that nothing shall be deemed to be confidential information which: (i) is known to the party receiving the information at the time of disclosure, unless any individual who knows the information is under an obligation to keep that information confidential; (ii) becomes publicly known or available without the disclosure thereof by the party receiving the information in violation of this Agreement; or (iii) is received by the party receiving the information from a third party not under an obligation to keep that information confidential. This provision shall not prohibit the disclosure of information required to be made under federal or state securities laws. If any disclosure is so required, the party making such disclosure shall consult with the other party prior to making such disclosure, and the parties shall use all reasonable efforts, acting in good faith, to agree upon a text for such disclosure which is satisfactory to both parties. 31 6.4 Proxy Statement. (a) In connection with the solicitation of proxies for the Atlantic Stockholder Meeting, the parties hereto shall cooperate in the preparation of an appropriate proxy statement (such proxy statement, together with any and all amendments or supplements thereto, being herein referred to as the "Proxy Statement"). (b) Manhattan shall furnish such information concerning Manhattan as is necessary in order to cause the Proxy Statement, insofar as it relates to Manhattan and Manhattan securities, to be prepared in accordance with Section 6.4(a). Manhattan shall also furnish to Atlantic, for purposes of its preparation of the Proxy Statement in accordance with Section 6.4(a), any required information regarding any Manhattan stockholders or Affiliates or any Manhattan nominees to Atlantic's board of directors. That information must be true and correct in all material respects and must not omit any material fact necessary to make that information not misleading. Manhattan agrees promptly to advise Atlantic if at any time prior to the Atlantic Stockholders Meeting any information provided by Manhattan in the Proxy Statement becomes incorrect or incomplete in any material respect, and to provide Atlantic the information needed to correct such inaccuracy or omission. (c) Atlantic shall use all reasonable efforts to promptly prepare and submit the Proxy Statement to the SEC. Atlantic shall use reasonable efforts to file the definitive Proxy Statement at the earliest practicable date. Atlantic agrees to provide Manhattan and its counsel with reasonable opportunity to review and comment on the Proxy Statement and any amendment thereto before filing with the SEC or any other governmental entity and agrees not to make such filing if Manhattan and its counsel reasonably object to the completeness or accuracy of any information contained therein. Manhattan authorizes Atlantic to utilize in the Proxy Statement the information under Section 6.4(a) provided to Atlantic for the purpose of inclusion in the Proxy Statement. Atlantic shall advise Manhattan promptly when the definitive Proxy Statement has been filed and shall furnish Manhattan with copies of all such documents. (d) At the time the Proxy Statement is mailed to the stockholders of Atlantic in order to obtain the Requisite Atlantic Stockholder Votes and at all times subsequent to such mailing until the Requisite Atlantic Stockholder Votes have been obtained, the Proxy Statement (including any amendments or supplements thereto), with respect to all information set forth therein relating to Atlantic and its stockholders, this Agreement, the Certificate of Merger, and all other transactions contemplated hereby, will (i) comply in all material respects with applicable provisions of the Exchange Act, including the rules and regulations promulgated thereunder, and (ii) not contain any untrue statement of material fact or omit to state a material fact required to be stated therein or necessary to make the statements contained therein, in light of the circumstances under which they are made, not misleading, except that, in each case, no such representations shall apply to any written information, including financial statements, of or provided by Manhattan for such Proxy Statement. (e) Atlantic shall bear all printing and mailing costs in connection with the preparation and mailing of the Proxy Statement to Atlantic stockholders. Manhattan and Atlantic shall each bear their own legal and accounting expenses in connection with the Proxy Statement. 32 6.5 Tax Treatment. None of Atlantic, MPAC or Manhattan, or the Surviving Company after the Effective Date, shall knowingly take any action which could reasonably be expected to disqualify the Merger as a "reorganization" within the meaning of Section 368(a) of the Code. 6.6 Press Releases. Manhattan and Atlantic shall agree with each other as to the form and substance of any press release or public announcement related to this Agreement or the transactions contemplated hereby; provided, however, that nothing contained herein shall prohibit either party, following notification to the other party, from making any disclosure which is required by law or regulation. If any such press release or public announcement is so required, the party making such disclosure shall consult with the other party prior to making such disclosure, and the parties shall use all reasonable efforts, acting in good faith, to agree upon a text for such disclosure which is satisfactory to both parties. 6.7 Securities Reports. Atlantic agrees to provide to Manhattan copies of all reports and other documents filed under the Securities Act or Exchange Act with the SEC by it between the date hereof and the Effective Date within two (2) days after the date such reports or other documents are filed with the SEC. 6.8 Private Placement. Each of Manhattan and Atlantic shall take all necessary action on its part such that the issuance of the Merger Consideration to Manhattan stockholders constitutes a valid "private placement" under the Securities Act. Without limiting the generality of the foregoing, Manhattan shall (1) provide each Manhattan stockholder with a stockholder qualification questionnaire in the form reasonably acceptable to both Atlantic and Manhattan (a "Stockholder Questionnaire") and (2) use its best efforts to cause each Manhattan stockholder to attest that that stockholder either (A) is an "accredited investor" as defined in Regulation D of the Securities Act, (B) has such knowledge and experience in financial and business matters that the stockholder is capable of evaluating the merits and risks of receiving the Merger Consideration, or (C) has appointed an appropriate person reasonably acceptable to both Atlantic and Manhattan to act as the stockholder's purchaser representative in connection with evaluating the merits and risks of receiving the Merger Consideration. 6.9 Stockholder Approvals. Atlantic shall call a meeting of its stockholders (the "Atlantic Stockholder Meeting") for the purpose of obtaining approval of (a) an increase in the number of authorized shares of Atlantic Common Stock so as to permit Atlantic to issue the Merger Consideration and (b) amendment of the certificate of designations of the Series A convertible preferred stock of Atlantic to provide for

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mandatory conversion immediately prior to the Effective Time of all outstanding shares of Series A convertible preferred stock of Atlantic (the "Atlantic Proposals"). Such meeting shall be held as soon as practicable following the date of this Agreement, but in no event later than February 7, 2003. The Board of Directors of Atlantic and Manhattan shall recommend approval of this Agreement and the Merger and use all reasonable efforts (including, without limitation, soliciting proxies for such approvals) to obtain approvals thereof from its stockholders; provided, however, either party's Board of Directors may fail to make such recommendation, and/or to seek to obtain the stockholder approval referred to in this sentence, or withdraw, modify or change any such recommendation, if such Board of Directors determines, in good faith, after consultation with counsel, that the making of such recommendation, the seeking to obtain such stockholder approval, or the failure to so 33 withdraw, modify or change its recommendation, may constitute a breach of the fiduciary or legal obligations of such Board of Directors.

6.10 Manhattan Stockholders' Meeting; Materials to Stockholders. (a) Manhattan shall, in accordance with Section 251 of the DGCL and its certificate of incorporation and by-laws, duly call, give notice of, convene and hold a special meeting of Manhattan Stockholders (the "Manhattan Stockholder Meeting") as promptly as practicable after the date hereof for the purpose of considering and taking action upon this Agreement and the Merger. In addition, Manhattan shall use its best efforts to obtain, prior to the Manhattan Stockholder Meeting, unanimous written consent of Manhattan stockholders approving this Agreement and the Merger. (b) Manhattan shall as promptly as practicable following the date of this Agreement prepare and mail to Manhattan stockholders all information as may be required to comply with the DGCL, the Securities Act and the Exchange Act.

6.11 No Solicitation. (a) Unless and until this Agreement shall have been terminated pursuant to Section 8.1, neither Atlantic nor its officers, directors or agents shall, directly or indirectly, encourage, solicit or initiate discussions or negotiations with, or engage in negotiations or discussions with, or provide non-public information to, any corporation, partnership, person or other entity or groups concerning any merger, sale of capital stock, sale of substantial assets or other business combination; provided that Atlantic may engage in such discussion in response to an unsolicited proposal from an unrelated party if the Board of Directors of Atlantic determines, in good faith, after consultation with counsel, that the failure to engage in such discussions may constitute a breach of the fiduciary or legal obligations of the Board of Directors of Atlantic. Atlantic will promptly advise Manhattan if it receives a proposal or inquiry with respect to the matters described above. (b) Unless and until this Agreement shall have been terminated pursuant to Section 8.1, neither Manhattan nor its officers, directors or agents shall, directly or indirectly, encourage, solicit or initiate discussions or negotiations with, or engage in negotiations or discussions with, or provide non-public information to, any corporation, partnership, person or other entity or groups concerning any merger, sale of capital stock, sale of substantial assets or other business combination; provided that Manhattan may engage in such discussion in response to any unsolicited proposal from an unrelated party if the Board of Directors of Manhattan determines, in good faith, after consultation with counsel, that the failure to engage in such discussions may constitute a breach of the fiduciary or legal obligations of the Board of Directors of Manhattan. Manhattan will promptly advise Atlantic if it receives a proposal or inquiry with respect to the matters described above.

6.12 Failure to Fulfill Conditions. In the event that either of the parties hereto determines that a condition to its respective obligations to consummate the transactions contemplated hereby cannot be fulfilled on or prior to the termination of this Agreement, it will promptly notify the other party.

6.13 Tax Opinion. Manhattan and Atlantic shall make such representations, warranties and covenants as are reasonably requested by Maslon Edelman Borman & Brand, LLP in order for it to render the tax opinion contemplated by Section 7.1(c).

6.14 Resignations and Election of Directors. Before the Effective Time, Atlantic shall deliver the voluntary resignations of each officer of Atlantic and each director of Atlantic not continuing to serve in that capacity following the Effective Time. Such resignations shall be effective upon the Effective Time. Immediately after the Effective Time, the remaining director(s) of Atlantic shall appoint the persons identified in Section 2.7 to serve as directors of Atlantic following the Effective Time.

6.15 Rule 144 Reporting and Rule 144. With a view to making it possible for holders of shares of Atlantic Common Stock received in the Merger to sell those shares under Rule 144 promulgated under the Securities Act ("Rule 144"), Atlantic shall use commercially reasonable efforts to (1) make and keep available current public information, as defined in Rule 144, (2) timely file with the SEC all reports and other documents required to be filed by Atlantic under the Securities Act and the Exchange Act, and (3) comply with all rules and regulations of the SEC applicable in connection with the use of Rule 144 and take such other actions and furnish each holder of shares of Atlantic Common Stock received in the Merger with such other information as that holder reasonably requests in order to avail itself of Rule 144.

6.16 Registration Rights. (a) Subject to reasonable and customary black-out periods in the case of certain public offerings by Atlantic as may be requested by the managing underwriter in connection with such offerings (but in no event more than one hundred eighty (180) days during any twelve month period), upon receipt of a written request of holders of at least fifty percent (50%) of the Atlantic Common Stock issued by Atlantic under this Agreement and unregistered through the date of such request (the "Registrable Securities"), Atlantic shall use its reasonable best efforts, at its own expense (excluding underwriting commissions and discounts) for one demand, to file within thirty (30) days from the date of such written notice, a registration statement with the SEC under the Securities Act registering the Registrable Securities for public resale (the "Demand Registration Statement") and shall use its best efforts to have such registration statement declared effective by the SEC; provided, however, that the registration rights granted under this Section shall not be assignable by the stockholders of Manhattan immediately prior to the Effective Time, except for transfers to family trusts or controlled Affiliates. Atlantic is not required to maintain the effectiveness of any Demand Registration Statement required to be filed in accordance with this paragraph (a) beyond the period ending on the earlier of the following dates: (i) the date one year after the effective date of the Demand Registration Statement; and (ii) the date on which all Registrable Securities covered by the Demand Registration Statement have been sold and the distribution thereby has been completed. (b) If at any time prior to the first anniversary of the Effective Date, Atlantic proposes to register under the Securities Act (except by a Form S-4 or Form S-8 Registration Statement or any successor forms thereto or a registration statement covering only (1) an employee stock option, stock purchase or compensation plan or securities issued or issuable pursuant to any such plan, or (2) a dividend reinvestment plan) or qualify for a public 35 distribution under Section 3(b) of the Securities Act, any of its equity securities or debt with equity features (other than in accordance with Section 6.16(a)), it will give written notice to all holders of the Registrable Securities of its intention to do so and, on the written request of the holders of at least fifty percent (50%) of the Registrable Securities received within twenty (20) after receipt of any such notice, Atlantic will use its best efforts to cause all of the Registrable Securities to be included in such registration statement proposed to be filed by Atlantic; provided, however, that nothing herein shall prevent Atlantic from, at any time, abandoning or delaying any registration. The right of the holders of the Registrable Securities to include the such securities in any such registration statement may be subject to approval by selling securityholders whose securities are being registered in the registration

statement. If any registration pursuant to this Section 6.16(b) is underwritten in whole or in part, Atlantic may require that the Registrable Securities be included in the underwriting on the same terms and conditions as the securities otherwise being sold through the underwriters and each holder of Registrable Securities shall execute any underwriting agreement, "lock-up" letters or other customary agreements or documents executed by Atlantic in connection with that underwritten offering. If, in the reasonable opinion of the managing underwriter of the proposed offering, the number of Registrable Securities offered for participation in the proposed offering cannot be accommodated without adversely affecting the proposed offering, then the amount of Registrable Securities proposed to be offered, as well as the number of securities of any other selling stockholders participating in the registration (other than holders of Registrable Securities being registered in accordance with Section 6.16(a)), shall be proportionately reduced to a number deemed satisfactory by the managing underwriter.

6.17 Notification of Certain Matters. On or prior to the Effective Date, each party shall give prompt notice to the other party of (i) the occurrence or failure to occur of any event or the discovery of any information, which occurrence, failure or discovery would be likely to cause any representation or warranty on its part contained in this Agreement to be untrue, inaccurate or incomplete after the date hereof in any material respect or, in the case of any representation or warranty given as of a specific date, would be likely to cause any such representation or warranty on its part contained in this Agreement to be untrue, inaccurate or incomplete in any material respect as of such specific date, and (ii) any material failure of such party to comply with or satisfy any covenant or agreement to be complied with or satisfied by it hereunder.

ARTICLE VII CONDITIONS

7.1 Conditions to Obligations of Each Party. The respective obligations of each party to effect the transactions contemplated hereby are subject to the fulfillment or waiver at or prior to the Effective Date of the following conditions: (a) No Prohibitive Change of Law. There shall have been no law, statute, rule or regulation, domestic or foreign, enacted or promulgated which would prohibit or make illegal the consummation of the transactions contemplated hereby. (b) Federal Tax Opinion. Manhattan shall have received from Maslon Edelman Borman & Brand, LLP a tax opinion dated as of the Closing Date to the effect that for federal income tax purposes: (i) The Merger will qualify as a reorganization under Section 368(a) of the Code. Atlantic and Manhattan will each be a party to the reorganization within the meaning of Section 368(b) of the Code. (ii) No gain or loss will be recognized by stockholders of Manhattan upon the receipt of the Merger Consideration. (c) Stockholder Approvals. This Agreement and the Merger shall have been approved by the Requisite Manhattan Stockholder Vote and the Atlantic Proposals shall have been approved by the Requisite Atlantic Stockholder Votes. (d) Adverse Proceedings. There shall not be threatened, instituted or pending any action or proceeding before any court or governmental authority or agency (i) challenging or seeking to make illegal, or to delay or otherwise directly or indirectly restrain or prohibit, the consummation of the transactions contemplated hereby or seeking to obtain material damages in connection with such transactions, (ii) seeking to prohibit direct or indirect ownership or operation by Atlantic or MPAC of all or a material portion of the business or assets of Manhattan, or to compel Atlantic or MPAC or any of their respective subsidiaries or Manhattan to dispose of or to hold separately all or a material portion of the business or assets of Atlantic or any Atlantic Subsidiary or of Manhattan, as a result of the transactions contemplated hereby; (iii) seeking to invalidate or render unenforceable any material provision of this Agreement or any of the other agreements attached as exhibits hereto or contemplated hereby, or (iv) otherwise relating to and materially adversely affecting the transactions contemplated hereby. (e) Governmental Action. There shall not be any action taken, or any statute, rule, regulation, judgment, order or injunction proposed, enacted, entered, enforced, promulgated, issued or deemed applicable to the transactions contemplated hereby, by any federal, state or other court, government or governmental authority or agency, that would reasonably be expected to result, directly or indirectly, in any of the consequences referred to in Section 7.1(d). (f) Market Condition. There shall not have occurred any general suspension of trading on the New York Stock Exchange, the Nasdaq Stock Markets, or any suspension of trading in Atlantic Common Stock, or any general bank moratorium or closing or any war, national emergency or other event affecting the economy or securities trading markets generally that would make completion of the Merger impossible. (g) Conversion of Preferred Stock. Immediately prior to the Effective Time all shares of Series A convertible preferred stock of Atlantic shall have been converted into shares of Atlantic Common Stock, as contemplated by the applicable Atlantic Proposal. (h) Amendment of Employment Agreements. Atlantic shall have entered into amended employment agreements with Frederic P. Zotos, Nicholas J. Rossettos, A. Joseph Rudick, Michael Ferrari, and Sarah Laut, the terms of which shall be subject to the consent of 37 Manhattan, which shall not be unreasonably withheld. Such amended agreements shall provide that one-half of the deferred salary and accrued bonus payable to each such employee upon the termination of his or her employment by Atlantic without cause shall be paid at such time that Atlantic has received aggregate cash funds of \$3 million from financings or other sources on or after the Effective Time; and the remaining one-half of the deferred salary and accrued bonus shall be paid at such time as Atlantic has received aggregate cash funds of \$6 million from financings or other sources on or after the Effective Time. (i) Manhattan Available Capital. Manhattan shall have at least \$500,000 in cash (or cash equivalents) available to the Surviving Company.

7.2 Additional Conditions to Obligation of Atlantic and MPAC. The obligation of Atlantic and MPAC to consummate the transactions contemplated hereby in accordance with the terms of this Agreement is also subject to the fulfillment or waiver of the following conditions: (a) Representations and Compliance. The representations of Manhattan contained in this Agreement were accurate as of the date of this Agreement and are accurate as of the Effective Time, in all respects (in the case of any representation containing any materiality qualification) or in all material respects (in the case of any representation without any materiality qualification). Manhattan shall in all material respects have performed each obligation and agreement and complied with each covenant to be performed and complied with by it hereunder at or prior to the Effective Date. (b) Officers' Certificate. Manhattan shall have furnished to Atlantic a certificate of the Chief Executive Officer and the Treasurer of Manhattan, dated as of the Effective Date, in which such officers shall certify that, to their best Knowledge, the conditions set forth in Section 7.2(a) have been fulfilled. (c) Secretary's Certificate. Manhattan shall have furnished to Atlantic (i) copies of the text of the resolutions by which the corporate action on the part of Manhattan necessary to approve this Agreement, the Certificate of Merger and the transactions contemplated hereby and thereby were taken, (ii) a certificate dated as of the Effective Date executed on behalf of Manhattan by its corporate secretary or one of its assistant corporate secretaries certifying to Atlantic that such copies are true, correct and complete copies of such resolutions and that such resolutions were duly adopted and have not been amended or rescinded, (iii) an incumbency certificate dated as of the Effective Date executed on behalf of Manhattan by its corporate secretary or one of its assistant corporate secretaries certifying the signature and office of each officer of Manhattan executing this Agreement, the Certificate of Merger or any other agreement, certificate or other instrument executed pursuant hereto by Manhattan, (iv) a copy of the Certificate of Incorporation of Manhattan, certified by the Secretary of State of Delaware, and a certificate from the Secretary of State of Delaware evidencing

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the good standing of Manhattan in such jurisdiction. (d) Consents and Approvals. Manhattan shall have obtained all consents and approvals necessary to consummate the transactions contemplated by this Agreement, including, without limitation, those set forth on Schedule 3.2, in order that the transactions contemplated herein not constitute a breach or violation of, or result in a right of termination or acceleration of, 38 or creation of any encumbrance on any of Manhattan's assets pursuant to the provisions of, any agreement, arrangement or undertaking of or affecting Manhattan or any license, franchise or permit of or affecting Manhattan. (e) Dissenters' Rights. Holders of no more than two (2) percent of the outstanding shares of Manhattan Common Stock shall have validly exercised, or remained entitled to exercise, their appraisal rights under Section 262 of the DGCL. (f) Fairness Opinion. Atlantic shall have received a written opinion addressed to it for inclusion in the Proxy Statement that the consideration to be received by it in the Merger is fair to the stockholders of Atlantic from a financial point of view, and that fairness opinion shall not have been revoked or withdrawn. (g) Merger Certificate. Manhattan shall have executed a copy of the Certificate of Merger. (h) Stockholder Questionnaire. Each of the Manhattan stockholders shall have executed and delivered to Atlantic a completed Stockholder Questionnaire that is accurate in all material respects. 7.3 Additional Conditions to Obligation of Manhattan. The obligation of Manhattan to consummate the transactions contemplated hereby in accordance with the terms of this Agreement is also subject to the fulfillment or waiver of the following conditions: (a) Representations And Compliance. The representations of Atlantic and MPAC contained in this Agreement were accurate as of the date of this Agreement and are accurate as of the Effective Time, in all respects (in the case of any representation containing any materiality qualification) or in all material respects (in the case of any representation without any materiality qualification). Atlantic and MPAC, respectively, shall in all material respects have performed each obligation and agreement and complied with each covenant to be performed and complied with by them hereunder at or prior to the Effective Date. (b) Officers' Certificate. Atlantic shall have furnished to Manhattan a certificate of the Chief Executive Officer and the Chief Financial Officer of Atlantic, dated as of the Effective Date, in which such officers shall certify that, to their best Knowledge, the conditions set forth in Section 7.3(a) have been fulfilled. (c) Secretary's Certificate. Atlantic shall have furnished to Manhattan (i) copies of the text of the resolutions by which the corporate action on the part of Atlantic necessary to approve this Agreement and the Certificate of Merger, the election of the directors of Atlantic to serve following the Effective Time and the transactions contemplated hereby and thereby were taken, which shall be accompanied by a certificate of the corporate secretary or assistant corporation secretary of Atlantic dated as of the Effective Date certifying to Manhattan that such copies are true, correct and complete copies of such resolutions and that such resolutions were duly adopted and have not been amended or rescinded, (ii) an incumbency certificate dated as of the Effective Date executed on behalf of Atlantic by its corporate secretary or one of its assistant corporate secretaries certifying the signature and office of each officer of Atlantic executing this Agreement, the Certificate of Merger or any other agreement, certificate 39 or other instrument executed pursuant hereto, and (iii) a copy of the Certificate of Incorporation of Atlantic, certified by the Secretary of State of Delaware, and certificates from the Secretary of State of Delaware evidencing the good standing of Atlantic in such jurisdiction. (d) Consents and Approvals. Atlantic and MPAC shall have obtained all consents and approvals necessary to consummate the transactions contemplated by this Agreement, including, without limitation, those set forth on Schedule 4.2, in order that the transactions contemplated herein not constitute a breach or violation of, or result in a right of termination or acceleration of, or creation of any encumbrance on any of Atlantic's or MPAC's assets pursuant to the provisions of, any agreement, arrangement or undertaking of or affecting Atlantic or any Atlantic Subsidiary or any license, franchise or permit of or affecting Atlantic or any Atlantic Subsidiary. (e) Resignations. Each of the officers and non-continuing directors of Atlantic immediately prior to the Effective Time shall deliver duly executed resignations from their positions with Atlantic effective immediately after the Effective Time. (f) Atlantic Warrant Exchange. All of Atlantic's currently outstanding warrants issued on or about December 3, 2001 to purchase an aggregate of 9,166,649 shares of Atlantic Common Stock at \$0.29 per share shall have been exchanged for shares of Atlantic Common Stock on the basis of one (1) share of Atlantic Common Stock for every three (3) warrants surrendered for exchange. ARTICLE VIII TERMINATION, AMENDMENT AND WAIVER 8.1 Termination. This Agreement may be terminated prior to the Effective Date: (a) by mutual consent of Manhattan and Atlantic, if the Board of Directors of each so determines by vote of a majority of the members of its entire board; (b) by Atlantic, if any representation of Manhattan set forth in this Agreement was inaccurate when made or becomes inaccurate such that the condition set forth in Section 7.2(a) could not be satisfied; (c) by Manhattan if any representation of Atlantic set forth in this Agreement was inaccurate when made or becomes inaccurate such that the condition set forth in Section 7.3(a) could not be satisfied; (d) by Atlantic if Manhattan fails to perform or comply with any of the obligations that it is required to perform or to comply with under this Agreement such that the condition set forth in Section 7.2(a) could not be satisfied; (e) by Manhattan if Atlantic fails to perform or comply with any of the obligations that it is required to perform or to comply with under this Agreement such that the condition set forth in Section 7.3(a) could not be satisfied; 40 (f) by either Manhattan or Atlantic, if, following a vote by the stockholders of each company at the Atlantic Stockholder Meeting and the Manhattan Stockholder Meeting, the Merger and this Agreement are not duly approved by the stockholders of each of Manhattan or Atlantic; (g) by either Manhattan or Atlantic if the Effective Date is not on or before February 7, 2003, or such later date as Manhattan and Atlantic may mutually agree (unless the failure to consummate the Merger by such date shall be due to the action or failure to act of the party seeking to terminate this Agreement in breach of such party's obligations under this Agreement); or (h) by either Atlantic or Manhattan pursuant to Section 6.3 above. Any party desiring to terminate this Agreement shall give prior written notice of such termination and the reasons therefor to the other party. ARTICLE IX GENERAL PROVISIONS 9.1 Notices. All notices and other communications hereunder shall be in writing and shall be sufficiently given if made by hand delivery, by fax, by telecopier, by overnight delivery service, or by registered or certified mail (postage prepaid and return receipt requested) to the parties at the following addresses (or at such other address for a party as shall be specified by it by like notice): If to Manhattan: Manhattan Pharmaceuticals, Inc. 787 Seventh Avenue, 48th Floor New York, New York 10019 Facsimile: (212) 554-4355 Attn: Joshua A. Kazam With copies to: Maslon Edelman Borman & Brand, LLP 90 South Seventh Street, Suite 3300 Minneapolis, MN 55402 Facsimile: (612) 642-8358 Attn: William M. Mower, Esq. If to Atlantic Atlantic Technology Ventures, Inc. or MPAC: 350 Fifth Avenue, Suite 5507 New York, New York 10118 Facsimile: (212) 267-2159 Attn: Frederic P. Zotos, President With copies to: Kramer Levin Naftalis & Frankel LLP 919 Third Avenue New York, NY 10022 Facsimile: (212) 715-8000 Attn: Ezra G. Levin, Esq. 41 All such notices and other communications shall be deemed to have been duly given as follows: when delivered by hand, if personally delivered, when received, if delivered by registered or certified mail (postage prepaid and return receipt requested), when receipt acknowledged; if faxed or telecopied, on the day of transmission or, if that day is not a business day, on the next

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business day; and the next day delivery after being timely delivered to a recognized overnight delivery service. 9.2 No Survival. The representations and warranties and obligations contained in this Agreement will terminate at the Effective Time or on termination of this Agreement in accordance with Section 8.1, except that the obligations contained in Article II and any other obligation contained in this Agreement requiring performance or compliance after the Effective Time (including without limitation Section 6.3(c)) will survive the Effective Time indefinitely. 9.3 Interpretation. The headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. References to Sections and Articles refer to Sections and Articles of this Agreement unless otherwise stated. Words such as "herein," "hereinafter," "hereof," "hereto," "hereby" and "hereunder," and words of like import, unless the context requires otherwise, refer to this Agreement (including the Exhibits and Schedules hereto). As used in this Agreement, the masculine, feminine and neuter genders shall be deemed to include the others if the context requires. 9.4 Severability. If any term, provision, covenant or restriction of this Agreement is held by a court of competent jurisdiction to be invalid, void or unenforceable, the remainder of the terms, provisions, covenants and restrictions of this Agreement shall remain in full force and effect and shall in no way be affected, impaired or invalidated, and the parties shall negotiate in good faith to modify this Agreement and to preserve each party's anticipated benefits under this Agreement. 9.5 Amendment. This Agreement may not be amended or modified except by an instrument in writing approved by the parties to this Agreement and signed on behalf of each of the parties hereto. 9.6 Waiver. At any time prior to the Effective Date, any party hereto may (a) extend the time for the performance of any of the obligations or other acts of the other party hereto or (b) waive compliance with any of the agreements of the other party or with any conditions to its own obligations, in each case only to the extent such obligations, agreements and conditions are intended for its benefit. Any such extension or waiver shall only be effective if made in writing and duly executed by the party giving such extension or waiver. 9.7 Miscellaneous. This Agreement (together with all other documents and instruments referred to herein): (a) constitutes the entire agreement, and supersedes all other prior agreements and undertakings, both written and oral, among the parties, with respect to the subject matter hereof; and (b) shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns, but shall not be assignable by either party hereto without the prior written consent of the other party hereto. 9.8 Counterparts. This Agreement may be executed in any number of counterparts, and each such counterpart shall be deemed to be an original instrument, but all such counterparts together shall constitute but one agreement. 9.9 Third Party Beneficiaries. Except as provided in the next following sentence, each party hereto intends that this Agreement shall not benefit or create any right or cause of action in or on behalf of any person other than the parties hereto. The provisions of Section 6.16 are intended for the benefit of the stockholders of Manhattan and their respective assigns. 9.10 Governing Law. This Agreement is governed by the internal laws of the State of New York, except to the extent the mandatory law of the State of Delaware applies. 9.11 Jurisdiction; Service of Process. Any action or proceeding seeking to enforce any provision of, or based on any right arising out of, this Agreement must be brought against any of the parties in the courts of the State of New York, County of New York, or, if it has or can acquire jurisdiction, in the United States District Court for the Southern District of New York, and each of the parties consents to the jurisdiction of those courts (and of the appropriate appellate courts) in any such action or proceeding and waives any objection to venue laid therein. Process in any such action or proceeding may be served by sending or delivering a copy of the process to the party to be served at the address and in the manner provided for the giving of notices in Section 9.1. Nothing in this Section 9.11, however, affects the right of any party to serve legal process in any other manner permitted by law. [Remainder of Page Left Intentionally Blank - Signature Page to Follow] 43 IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed on the date first written above by their respective officers. MANHATTAN PHARMACEUTICALS, INC. By: /s/ John Knox ----- Name: John Knox Title: Treasurer ATLANTIC TECHNOLOGY VENTURES, INC. By: /s/ Frederick P. Zotos ----- Name: Frederick P. Zotos Title: President and Chief Executive Officer MANHATTAN PHARMACEUTICALS ACQUISITION CORP. By: /s/ Frederick P. Zotos ----- Name: Frederick P. Zotos Title: President and Chief Executive Officer 44 Exhibit B [Fairness Opinion not yet completed; to be filed with the definitive proxy.] Exhibit C CERTIFICATE OF AMENDMENT OF THE CERTIFICATE OF INCORPORATION OF ATLANTIC TECHNOLOGY VENTURES, INC. Pursuant to Section 242 of the General Corporation Law of the State of Delaware It is hereby certified that: 1. Atlantic Technology Ventures, Inc. is a corporation formed under the laws of the State of Delaware, and its certificate of incorporation was filed in the office of the Secretary of State on May 18, 1993. 2. The certificate of incorporation is hereby amended by deleting the existing Article FIRST and replacing it in its entirety with the following amendment: "FIRST: The name of the corporation is Manhattan Pharmaceuticals, Inc." 3. The certificate of incorporation is hereby amended by deleting the text of Article FOURTH, A. in its entirety and replacing it with the following: The corporation is authorized to issue two classes of shares designated "Common Stock" and "Preferred Stock," respectively. The total number of shares of Common Stock authorized to be issued is [150,000,000], and each such share will have a par value of \$0.001. The total number of shares of Preferred Stock authorized to be issued is 10,000,000, and each such share will have a par value of \$0.001. The rights, preferences, privileges and restrictions granted to and imposed upon the two classes of shares are as set forth in this Article and in the Certificate of Designations of Series A Convertible Preferred Stock. 4. This amendment to the certificate of incorporation has been duly adopted in accordance with Section 242 of the General Corporation Law of the State of Delaware. The undersigned is signing this certificate on _____, 2003. ----- Frederic P. Zotos President and Chief Executive Officer Exhibit D CERTIFICATE OF AMENDMENT OF THE CERTIFICATE OF DESIGNATIONS OF SERIES A CONVERTIBLE PREFERRED STOCK OF ATLANTIC TECHNOLOGY VENTURES, INC. Pursuant to Section 151 of the General Corporation Law of the State of Delaware It is hereby certified that: 1. Atlantic Technology Ventures, Inc. (the "Corporation") is a corporation formed under the laws of the State of Delaware, and its certificate of incorporation was filed in the office of the Secretary of State on May 18, 1993. 2. The certificate of incorporation is hereby amended by deleting the existing Article FIRST and replacing it in its entirety with the following amendment: "FIRST: The name of the corporation is Manhattan Pharmaceuticals, Inc." 3. The certificate of designations of the Series A convertible preferred stock is hereby amended by adding after the first paragraph of Section 5 a paragraph that reads as follows: Immediately prior to the execution of a merger agreement between the Corporation, a wholly owned subsidiary of the Corporation, and Manhattan Pharmaceuticals, Inc., a Delaware corporation, the Series A Preferred Stock shall automatically convert into fully paid and nonassessable shares of Common Stock at the Conversion Rate then in effect. Any shares of Series A Preferred Stock so converted shall be treated as having been surrendered by the holder thereof for conversion in accordance with Section 4 on the date of such mandatory conversion. 4. These amendments to the certificate of incorporation has been duly

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adopted in accordance with Section 151 of the General Corporation Law of the State of Delaware. The undersigned is signing this certificate on _____, 2003. ----- Frederic P. Zotos President and Chief Executive Officer Exhibit E CHARTER AND POWERS OF THE AUDIT COMMITTEE RESOLVED, that the membership of the Audit Committee shall consist of at least one independent member of the board of directors (in conformity with the small business rules of the Nasdaq) who shall serve at the pleasure of the board of directors. RESOLVED, that the charter and powers of the Audit Committee of the Board of Directors (the "Audit Committee") shall be: o Assisting the Board of Directors in the oversight of the maintenance by management of the reliability and integrity of the accounting policies and financial reporting and disclosure practices of Atlantic. o Assisting the Board of Directors in the oversight of the establishment and maintenance by management of processes to assure that an adequate system of internal control is functioning within Atlantic. o Assisting the Board of Directors in the oversight of the establishment and maintenance by management of process to assure compliance by Atlantic with all applicable laws, regulations and Company policy. RESOLVED, that the Audit Committee shall have the following specific powers and duties: 1. Holding such regular meetings as may be necessary and such special meetings as may be called by the Chairman of the Audit Committee or at the request of the independent accountants; 2. Reviewing the performance of the independent accountants and making recommendations to the Board of Directors regarding the appointment or termination of the independent accountants; 3. Ensuring its receipt from the independent accountants of a formal written statement delineating all relationships between the independent accountants and Atlantic consistent with Independence Standards Board Standard; 4. Actively engaging in a dialogue with the independent accountants with respect to any disclosed relationships or services that may impact the objectivity and independence of the independent accountants and for taking or recommending that the Board of Directors take appropriate action to oversee the independence of the outside auditor; 5. Selecting, evaluating and, where appropriate, replacing the independent auditors (or nominating independent auditors to be proposed for shareholder approval in any proxy statement, which independent auditors shall ultimately be accountable to the Board of Directors and the Audit Committee; 6. Conferring with the independent accountants concerning the scope of their examinations of the books and records of Atlantic and its subsidiaries: reviewing and approving the independent accountants' annual engagement letter: reviewing and approving Atlantic's internal annual audit plans and procedures: and authorizing the auditors to perform such supplemental reviews or audits as the Committee may deem desirable; 7. Reviewing with management, the independent accountants significant risks and exposures, audit activities and significant audit findings; 8. Reviewing the range and cost of audit and non-audit services performed by the independent accountants; 9. Reviewing Atlantic's audited annual financial statements and the independent accountants opinion rendered with respect to such financial statements, including reviewing the nature and extent of any significant changes in accounting principles or the application thereof; 10. Reviewing the adequacy of Atlantic's systems of internal control; 11. Obtaining from the independent accountants their recommendations regarding internal controls and other matters relating to the accounting procedures and the books and records of Atlantic and its subsidiaries and reviewing the correction of controls deemed to be deficient; 12. Providing an independent, direct communication between the Board of Directors, and independent accountants; 13. Reviewing the adequacy of internal controls and procedures related to executive travel and entertainment; 14. Reviewing the programs and policies of Atlantic designed to ensure compliance with applicable laws and regulations and monitoring the results of these compliance efforts; 15. Reporting through its Chairman to the Board of Directors following the meetings of the Audit Committee; 16. Reviewing the powers of the Committee annually and reporting and making recommendations to the Board of Directors on these responsibilities; 17. Conducting or authorizing investigations into any matters within the Audit Committee's scope of responsibilities; and 18. Considering such other matters in relation to the financial affairs of Atlantic and its accounts, and in relation to the internal and external audit of Atlantic as the Audit Committee may, in its discretion, determine to be advisable. IN WITNESS WHEREOF, the undersigned have executed this written Consent, which written Consent may be signed in one or more counterparts which taken together shall constitute one and the same written consent, as of this 13th day of June, 2000. /s/ Steve H. Kanzer ----- Steve H. Kanzer /s/ Peter O. Kliem ----- Peter O. Kliem /s/ A. Joseph Rudick ----- A. Joseph Rudick /s/ Frederic P. Zotos Frederic P. Zotos ATLANTIC TECHNOLOGY VENTURES, INC. PROXY ANNUAL MEETING OF SHAREHOLDERS, _____, 2003 THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF ATLANTIC TECHNOLOGY VENTURES, INC. The undersigned revokes all previous proxies, acknowledges receipt of the notice of the annual meeting of shareholders to be held _____, 2003 and the proxy statement and appoints Frederic P. Zotos and Mr. Nicholas J. Rossettos, and each of them, the proxy of the undersigned, with full power of substitution, to vote all shares of common stock of Atlantic Technology Ventures, Inc. that the undersigned is entitled to vote, either on his or her own behalf or on behalf of any entity or entities, at the annual meeting of shareholders of Atlantic to be held at the offices of Kramer Levin Naftalis & Frankel LLP, at 919 Third Avenue, 40th Floor, New York, New York 10022, on _____, 2003 at 10:00 a.m. New York time, and at any adjournment or postponement thereof, with the same force and effect as the undersigned might or could do if personally present at the annual meeting. The shares represented by this proxy will be voted in the manner set forth below. 1. To amend Atlantic's certificate of incorporation to increase the total number of authorized shares of Atlantic common stock, par value \$0.001, from 50 million to 150 million. FOR [] AGAINST [] ABSTAIN [] 2. To amend the certificate of designations of Atlantic's Series A preferred stock to provide for the mandatory conversion of all outstanding shares of Series A preferred stock immediately prior to the effectiveness of a merger of a wholly owned subsidiary of Atlantic into Manhattan Pharmaceuticals, Inc. FOR [] AGAINST [] ABSTAIN [] 3. To amend our certificate of incorporation to change Atlantic's name to "Manhattan Pharmaceuticals, Inc." FOR [] AGAINST [] ABSTAIN [] 4. To elect five directors to serve on Atlantic's board of directors for the ensuing year and until their respective successors are duly elected and qualified. To withhold authority to vote for any FOR nominees, enter their name or names below: Frederic P. Zotos [] _____ Steve H. Kanzer [] _____ Peter O. Kliem [] _____ A. Joseph Rudick [] _____ David M. Tanen [] _____ 5. To ratify the board of directors' selection of J.H. Cohn, LLP to serve as Atlantic's independent auditors for the year ending December 31, 2002. FOR [] AGAINST [] ABSTAIN [] The board of directors recommends a vote in favor of each of the directors listed above and a vote in favor of the other proposals. This proxy, when properly executed, will be voted as specified above. If no direction is made, this proxy will be voted in favor of election of the directors listed above and in favor of the other proposals. Please print the shareholder name exactly as it appears on your stock certificate. If the shares are registered in more than one name, the signature of each person in whose name the shares are registered is required. A corporation should sign in its full corporate name, with a duly authorized officer signing on behalf of the corporation and stating his or her title.

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Trustees, guardians, executors, and administrators should sign in their official capacity, giving their full title as such. A partnership should sign in its partnership name, with an authorized person signing on behalf of the partnership. ----- (Print name)
----- (Authorized Signature) Date: _____ ATLANTIC TECHNOLOGY VENTURES, INC. PROXY ANNUAL MEETING OF SHAREHOLDERS, _____, 2003 THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF ATLANTIC TECHNOLOGY VENTURES, INC. The undersigned revokes all previous proxies, acknowledges receipt of the notice of the annual meeting of shareholders to be held _____, 2003 and the proxy statement and appoints Frederic P. Zotos and Mr. Nicholas J. Rossetos, and each of them, the proxy of the undersigned, with full power of substitution, to vote all shares of Series A preferred stock of Atlantic Technology Ventures, Inc. that the undersigned is entitled to vote, either on his or her own behalf or on behalf of any entity or entities, at the annual meeting of Shareholders of Atlantic to be held at the offices of Kramer Levin Naftalis & Frankel LLP, at 919 Third Avenue, 40th Floor, New York, New York 10022, on _____, 2003 at 10:00 a.m. New York time, and at any adjournment or postponement thereof, with the same force and effect as the undersigned might or could do if personally present at the annual meeting. The shares represented by this proxy will be voted in the manner set forth below. 1. To amend Atlantic's certificate of incorporation to increase the total number of authorized shares of Atlantic common stock, par value \$0.001, from 50 million to 150 million. FOR AGAINST ABSTAIN 2. To amend the certificate of designations of Atlantic's Series A preferred stock to provide for the mandatory conversion of all outstanding shares of Series A preferred stock immediately prior to the effectiveness of a merger of a wholly owned subsidiary of Atlantic into Manhattan Pharmaceuticals, Inc. FOR AGAINST ABSTAIN 3. To amend our certificate of incorporation to change Atlantic's name to "Manhattan Pharmaceuticals, Inc." FOR AGAINST ABSTAIN 4. To elect five directors to serve on Atlantic's board of directors for the ensuing year and until their respective successors are duly elected and qualified. To withhold authority to vote for any nominees, enter their name or names FOR below: Frederic P. Zotos _____ Steve H. Kanzer _____ Peter O. Kliem _____ A. Joseph Rudick _____ David M. Tanen _____ 5. To ratify the board of directors' selection of J.H. Cohn, LLP to serve as Atlantic's independent auditors for the year ending December 31, 2002. FOR AGAINST ABSTAIN The board of directors recommends a vote in favor of each of the directors listed above and a vote in favor of the other proposals. This proxy, when properly executed, will be voted as specified above. If no direction is made, this proxy will be voted in favor of election of the directors listed above and in favor of the other proposals. Please print the shareholder name exactly as it appears on your stock certificate. If the shares are registered in more than one name, the signature of each person in whose name the shares are registered is required. A corporation should sign in its full corporate name, with a duly authorized officer signing on behalf of the corporation and stating his or her title. Trustees, guardians, executors, and administrators should sign in their official capacity, giving their full title as such. A partnership should sign in its partnership name, with an authorized person signing on behalf of the partnership. ----- (Print name) ----- (Authorized Signature) Date:
