EARTHSHELL CORP
Form 10-Q
November 14, 2003

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

FORM 10-Q

|X| QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended September 30, 2003

| | TRANSITION REPORT PURSUANT SECTION 13 OR 15 (d)
OF SECURITIES EXCHANGE ACT OF 1934

For the Transition Period From ______to_________

Commission File Number 333-13287

EARTHSHELL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware 77-0322379
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

6740 Cortona Drive, Santa Barbara, California 93117
(Address of principal executive office) (Zip Code)

(805) 571-8232
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes |X| No | |

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes |X| No | |

The number of shares outstanding of the Registrant's Common Stock as of November 11, 2003 is 13,988,551.

EARTHSHELL CORPORATION

FORM 10-Q

For the Quarter Ended September 30, 2003

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EARTHSHELL CORPORATION
(A Development Stage Enterprise)
CONSOLIDATED BALANCE SHEETS

	September 30, 2003
	(Unaudited)
ASSETS	

CURRENT ASSETS	
Cash and cash equivalents	$ 1,469,170
Restricted cash	3,500,000
Prepaid expenses and other current assets	412,849
Total current assets	5,382,019
PROPERTY AND EQUIPMENT, NET	4,137,026
INVESTMENT IN JOINT VENTURE	112,098
TOTALS	$ 9,631,143
LIABILITIES AND STOCKHOLDERS' DEFICIT	
CURRENT LIABILITIES	
Accounts payable and accrued expenses	$ 4,921,199
Payable to related party	-
Accrued purchase commitment	3,500,000
Notes payable to related party	-
Convertible debentures	-
Total current liabilities	8,421,199
PAYABLES TO RELATED PARTY	1,393,302
CONVERTIBLE DEBENTURES	5,605,268
NOTES PAYABLE TO RELATED PARTY	2,510,496
OTHER LONG-TERM LIABILITY	50,000
Total liabilities	17,980,265
STOCKHOLDERS' DEFICIT	
Preferred stock, $.01 par value, 10,000,000 shares authorized; 9,170,000 Series A shares designated; no shares issued and outstanding as of September 30, 2003 and December 31, 2002	-
Common stock, $.01 par value, 25,000,000 shares authorized; 13,892,200 and 12,054,637 shares issued and outstanding as of September 30, 2003 and December 31, 2002, respectively	138,922
Additional paid-in common capital	300,682,833
Deficit accumulated during the development stage	(309,133,648)
Accumulated other comprehensive loss	(37,229)
Total stockholders' deficit	(8,349,122)
TOTALS	$ 9,631,143

See Notes to Consolidated Financial Statements.

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EARTHSHELL CORPORATION
(A Development Stage Enterprise)

CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	For the Three Months Ended September 30,		For t Nine Mo Ended Septe
	2003	2002	2003
Operating Expenses:			
Related party license fee and research and development expenses....................	$ 353,907	$ 300,000	$ 1,012,374
Other research and development expenses.....	1,287,516	2,941.860	4,892,009
Related party general and administrative expenses................................	-	-	(4,074)
Other general and administrative expenses...	1,361,900	2,366,377	4,408,944
Depreciation and amortization...............	95,207	795,065	311,483
Related party patent expenses...............	-	-	-
Total operating expenses................	3,098,530	6,403,302	10,620,736
Other Expenses (Income):			
Interest income.............................	(16,705)	(18,345)	(80,956)
Related party interest expense..............	95,697	-	265,931
Other interest expense......................	292,251	79,447	1,214,988
Gain on sales of property and equipment.....	(122,964)	-	(185,964)
Other (income) expense......................	(486,659)	-	(399,701)
Loss on extinguishment of debentures........	-	-	1,697,380
Debenture conversion costs..................	60,647	320,970	166,494
Loss before income taxes....................	2,920,797	6,785,374	13,298,908
Income taxes................................	-	-	800
Net loss....................................	2,920,797	6,785,374	13,299,708
Preferred dividends	-	-	-
Net loss available to common stockholders...........................	$ 2,920,797	$6,785,374	$13,299,708
Basic and diluted loss per common share..................................	$0.21	$0.59	$1.02
Weighted average number of common shares outstanding.....................	13,595,973	11,541,668	12,993,999

See Notes to Consolidated Financial Statements.

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EARTHSHELL CORPORATION
(A Development Stage Enterprise)
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' (DEFICIT) EQUITY
(Unaudited)

	Cumulative Convertible Preferred Stock Series A		Additional Paid-In Preferred Capital	Common Stock	
	Shares	Amount		Shares	Amount
ISSUANCE OF COMMON STOCK AT INCEPTION.................	--	--	--	6,877,500	$ 3,150
Sale of preferred stock, net.	582,404	$ 267	$24,472,734	--	--
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 1993...	582,404	267	24,472,734	6,877,500	3,150
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 1994...	582,404	267	24,472,734	6,877,500	3,150
Contribution to equity.......	--	--	--	--	--
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 1995...	582,404	267	24,472,734	6,877,500	3,150
Contribution to equity.......	--	--	--	--	--
Issuance of stock warrants...	--	--	--	--	--
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 1996...	582,404	267	24,472,734	6,877,500	3,150
Compensation related to stock options, warrants and stock grants..........	--	--	--	--	--
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 1997...	582,404	267	24,472,734	6,877,500	3,150
262 to 1 stock split	--	5,557	(5,557)	--	65,625
Conversion of preferred stock into common stock...	(582,404)	(5,824)	(24,467,177)	582,404	5,824
Issuance of common stock.....	--	--	--	877,193	8,772
Preferred stock dividends....	--	--	--	--	--
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 1998...	--	--	--	8,337,097	83,371
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 1999...	--	--	--	8,337,097	83,371
Issuance of common stock.....	--	--	--	371,431	3,714
Net loss.....................	--	--	--	--	--
BALANCE, DECEMBER 31, 2000...	--	--	--	8,708,528	87,085
Issuance of common stock.....	--	--	--	1,126,727	11,268
Compensation related to stock options, warrants					

and stock grants..........	--	--	--	25,000	250
Net loss....................	--	--	--	--	--
BALANCE, DECEMBER 31, 2001...	--	--	--	9,860,255	98,603
Issuance of common stock.....	--	--	--	2,025,686	20,256
Common stock warrants issued in connection with convertible debentures....	--	--	--	--	--
Conversion of convertible debentures to common stock	--	--	--	168,696	1,687
Debentures conversion costs..	--	--	--	--	--
Net loss....................					
Foreign currency translation adjustment................	--	--	--	--	--
Comprehensive loss..........	--	--	--	--	--
BALANCE, DECEMBER 31, 2002...	--	--	--	12,054,637	120,546
Interest paid in common stock	--	--	--	17,162	172
Conversion of convertible debentures to common stock.	--	--	--	1,216,485	12,165
Issuance of common stock.....	--	--	--	603,916	6,039
Issuance of stock warrants...	--	--	--	--	--
Beneficial conversion value due to change in debentures conversion price....................	--	--	--	--	--
Net loss....................	--	--	--	--	--
Foreign currency translation adjustment................	--	--	--	--	--
Comprehensive loss..........	--	--	--	--	--
BALANCE, SEPTEMBER 30, 2003	--	$ --	$ --	13,892,200	$ 138,922

	Additional Paid-In Common Capital	Deficit Accumulated during Development Stage	Accum-ulated Other Compre-hensive Loss	Total
ISSUANCE OF COMMON STOCK AT INCEPTION.................	$ 6,850	--	--	$ 10
Sale of preferred stock, net.	--	--	--	24,473
Net loss....................	--	$ (7,782,551)	--	(7,782
BALANCE, DECEMBER 31, 1993...	6,850	(7,782,551)	--	16,700

Net loss....................	--	(16,582,080)	--	(16,582
BALANCE, DECEMBER 31, 1994...	6,850	(24,364,631)	--	118
Contribution to equity.......	1,117,723	--	--	1,117
Net loss....................	--	(13,914,194)	--	(13,914
BALANCE, DECEMBER 31, 1995...	1,124,573	(38,278,825)	--	(12,678
Contribution to equity.......	650,000	--	--	650
Issuance of stock warrants...	246,270	--	--	246
Net loss....................	--	(16,950,137)	--	(16,950
BALANCE, DECEMBER 31, 1996...	2,020,843	(55,228,962)	--	(28,731
Compensation related to stock options, warrants and stock grants..........	3,156,659	--	--	3,156
Net loss....................	--	(18,992,023)	--	(18,992
BALANCE, DECEMBER 31, 1997...	5,177,502	(74,220,985)	--	(44,567
262 to 1 stock split	(65,625)	--	--	
Conversion of preferred stock into common stock...	24,467,177	--	--	
Issuance of common stock.....	205,979,984	--	--	205,988
Preferred stock dividends....	(9,926,703)	--	--	(9,926
Net loss....................	--	(26,620,052)	--	(26,620
BALANCE, DECEMBER 31, 1998...	225,632,335	(100,841,037)	--	124,874
Net loss....................	--	(44,188,443)	--	(44,188
BALANCE, DECEMBER 31, 1999...	225,632,335	(145,029,480)	--	80,686
Issuance of common stock.....	10,518,074	--	--	10,521
Net loss....................	--	(48,911,605)	--	(48,911
BALANCE, DECEMBER 31, 2000...	236,150,409	(193,941,085)	--	42,296
Issuance of common stock.....	30,542,772	--	--	30,554
Compensation related to stock options, warrants and stock grants..........	986,869	--	--	987
Net loss....................	--	(62,301,511)	--	(62,301
BALANCE, DECEMBER 31, 2001...	267,680,050	(256,242,596)	--	11,536
Issuance of common stock.....	21,881,460	--	--	21,901
Common stock warrants issued in connection with convertible debentures....	1,521,046	--	--	1,521
Conversion of convertible debentures to common stock	998,313	--	--	1,000
Debentures conversion costs..	176,471	--	--	176
Net loss....................		(39,591,344)		(39,591
Foreign currency translation adjustment................	--	--	$(16,632)	(16
Comprehensive loss...........	--	--	--	(39,607

BALANCE, DECEMBER 31, 2002...	292,257,340	(295,833,940)	(16,632)	(3,472
Interest paid in common stock	92,062	--	--	92
Conversion of convertible debentures to common stock.	5,626,063	--	--	5,638
Issuance of common stock.....	2,043,846	--	--	2,049
Issuance of stock warrants...	303,522	--	--	303
Beneficial conversion value due to change in debentures conversion price....................	360,000	--	--	360
Net loss.....................	--	(13,299,708)	--	(13,299
Foreign currency translation adjustment................	--	--	(20,597)	(20
Comprehensive loss...........	--	--	--	(13,320
BALANCE, SEPTEMBER 30, 2003	$300,682,833	$(309,133,648)	$(37,229)	$(8,349

See Notes to Consolidated Financial Statements.

EARTHSHELL CORPORATION
(A Development Stage Enterprise)
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30,	
	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss..	$ (13,299,708)	$(24,157,521)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization............................	311,483	2,385,770
Compensation related to issuance of stock, stock options and warrants to directors, consultants and officers....	-	-
Amortization and accretion of debt issue costs............	753,428	76,052
Debentures issuance and conversion costs.................	166,494	320,970
Gain on change in fair value of warrant obligation........	(399,701)	-
Loss on extinguishment of debentures.....................	1,697,380	-
Beneficial conversion value due to change in debentures conversion price.....................................	360,000	-
(Gain) Loss on sale, disposal, or impairment of property and equipment.......................................	(185,964)	1,842,143
Equity in the losses of joint venture....................	280,018	45,000
Accrued purchase commitment..............................	-	-
Net loss on sale of investments..........................	-	-
Accretion of discounts on investments....................	-	-

Other non-cash expense items	590	-
Changes in operating assets and liabilities:		
Prepaid expenses and other current assets	157,916	66,480
Accounts payable and accrued expenses	(2,955,813)	(1,014,011)
Payable to related party	768,877	-
Other long term liability	50,000	-
Net cash used in operating activities	(12,295,000)	(20,435,117)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investments in U.S. government securities	-	-
Purchase of restricted time deposit in connection with purchase commitment	-	(9,000,000)
Proceeds from sales and redemption of investments	-	-
Proceeds from sales of property and equipment	214,949	9,500
Investment in joint venture	(26,104)	-
Purchase of property and equipment	(1,320)	(2,662,278)
Net cash provided by (used in) investing activities	187,525	(11,652,778)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of common stock	-	19,505,758
Common stock issuance costs	-	3,030,000
Proceeds from issuance of common stock and convertible debentures	8,659,079	10,000,000
Proceeds from issuance of convertible debentures	-	-
Purchase of restricted time deposit in connection with issuance of convertible debentures	-	-
Proceeds from release of restricted time deposit upon conversion of convertible debentures into common stock.	1,800,000	-
Repayment of convertible debentures	(5,200,000)	-
Proceeds from release of restricted cash for repayment of convertible debentures	5,200,000	-
Proceeds from release of restricted cash upon exchange of convertible debentures	2,000,000	-
Proceeds from issuance of notes payable to related party	1,010,000	-
Repayment of notes payable to related party	-	(1,030,000)
Proceeds from drawings on line of credit with bank	-	-
Repayment of line of credit with bank	-	-
Preferred dividends paid	-	-
Proceeds from issuance of preferred stock	-	-
Preferred stock issuance costs	-	-
Net cash provided by financing activities	13,469,079	31,505,758
Effect of exchange rate changes on cash and cash equivalents	(3,449)	-
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	1,358,155	(582,137)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	111,015	828,007
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 1,469,170	$ 245,870

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

Cash paid for:		
Income taxes..	$ -	$ 800
Interest..	77,579	-
Common stock warrants issued in connection with convertible debentures...	745,562	1,521,046
Conversion of convertible debentures into common stock......	6,975,000	1,000,000
Transfer of property from EKI...............................	-	-
Interest paid in Common Stock...............................	92,234	-
Commission paid in common stock............................	29,500	-
Common stock issued to service providers in connection with the March 2003 financing..........................	484,500	-
Conversion of preferred stock to common stock..............	-	-

See Notes to Consolidated Financial Statements.

EARTHSHELL CORPORATION
(A Development Stage Enterprise)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
September 30, 2003

Organized in November 1992 as a Delaware corporation, EarthShell Corporation is engaged in the commercialization of composite material technology for the manufacture of foodservice disposable packaging designed with the environment in mind. EarthShell Packaging(R) is based on patented composite material technology (collectively, the "EarthShell Technology"), licensed on an exclusive, worldwide basis from E. Khashoggi Industries LLC and its wholly owned subsidiaries.

The EarthShell Technology has been developed over many years in consultation with leading material scientists and environmental experts to reduce the environmental burdens of foodservice disposable packaging through the careful selection of raw materials, processes, and suppliers. EarthShell Packaging(R), including hinged-lid sandwich containers, plates, bowls, and cups, is primarily made from commonly available natural raw materials such as natural ground limestone and potato starch. EarthShell believes that EarthShell Packaging(R) has comparable or superior performance characteristics and can be commercially produced and sold at prices that are competitive with comparable paper and plastic foodservice disposable packaging.

Presentation of Financial Information

The foregoing interim financial information is unaudited and has been prepared from the books and records of EarthShell Corporation. EarthShell Corporation's consolidated financial statements include the accounts of its wholly-owned subsidiary, EarthShell GmbH. All significant intercompany balances and

transactions have been eliminated in consolidation. Both EarthShell Corporation and its subsidiary (collectively "EarthShell" or the "Company") are development stage enterprises. In the opinion of management, the financial information reflects all adjustments necessary for a fair presentation of the financial condition, results of operations and cash flows of the Company in conformity with generally accepted accounting principles. All such adjustments were of a normal recurring nature for interim financial reporting. Certain reclassifications have been made to the 2002 financial statements to conform to the 2003 presentation.

The accompanying unaudited consolidated financial statements and these notes do not include certain information and footnote disclosures required by accounting principles generally accepted in the United States, which were included in the Company's consolidated financial statements for the year ended December 31, 2002. The information included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Company's consolidated financial statements and notes thereto for the year ended December 31, 2002 included in the Company's Annual Report on Form 10-K/A.

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. During the period from November 1, 1992 (inception) to September 30, 2003, the Company has incurred a cumulative net loss of $309,133,648 and has a stockholders' deficit of $8,349,122 at September 30, 2003. These factors among others may indicate that the Company will be unable to continue as a going concern for a reasonable period of time.

The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. The Company's continuation as a going concern is dependent upon its ability to generate sufficient cash flow to meet its obligations on a timely basis, to obtain additional financing or refinancing as may be required, and ultimately to attain successful operations.

Basic loss per common share is computed by dividing net loss available to common stockholders by the weighted-average number of common shares outstanding during the period. Diluted loss per common share is computed by dividing net loss available to common stockholders by the weighted-average number of common shares outstanding plus an assumed increase in common shares outstanding for potentially dilutive securities, which consist of options and warrants to acquire common stock and convertible debentures. Potentially dilutive shares are excluded from the computation in loss periods, as their effect would be anti-dilutive. The dilutive effect of options and warrants to acquire common stock is measured using the treasury stock method. The dilutive effect of convertible debentures is measured using the if-converted method. Basic and diluted loss per common share is the same for all periods presented because the impact of potentially dilutive securities is anti-dilutive. As noted in "Subsequent Events," the Company effected a reverse split of its common stock, effective as of October 31, 2003. Accordingly, the split has been retroactively reflected in these financial statements.

Since March 5, 2003 the Company's common stock has traded on the NASDAQ SmallCap Market under

the symbol "ERTH." Due to the October 31, 2003 reverse stock split (see "Subsequent Events"), the Company's common stock will trade under the symbol

"ERTHD" from October 31, 2003 through November 28, 2003, at which time it will revert back to "ERTH."

Related Party Transactions

E. Khashoggi Industries LLC and its wholly owned subsidiaries ("EKI") own approximately 30% of the Company's outstanding shares, and may be deemed to be a controlling stockholder. In connection with the formation of the Company, the Company entered into a Master License Agreement with EKI (the "EKI License Agreement"), pursuant to which the Company has an exclusive, worldwide, royalty-free license to use and license the EKI technology to manufacture and sell disposable, single-use containers for packaging or serving food or beverages intended for consumption within a short period of time (less than 24 hours). Effective January 1, 2001, EKI granted to the Company priority rights to license certain product applications on an exclusive basis from Biotec, a wholly owned subsidiary of EKI, in consideration for payment by the Company of a $100,000 monthly licensing fee to Biotec. In addition, Biotec agreed to render technical services to the Company, as required, at Biotec's cost plus 5%. Effective July 29, 2002, the Company restated its agreements with Biotec in a definitive License & Information Transfer Agreement with Biotec to utilize the Biotec technology for foodservice applications, including food wraps and cutlery (the "Biotec License Agreement"). Under the terms of the Biotec License Agreement, the Company paid or accrued $353,907 and $300,000 during the three months ended September 30, 2003 and 2002, respectively, and $1,012,374 and $1,068,313 during the nine months ended September 30, 2003 and 2002, respectively, consisting of the $100,000 per month licensing fee plus materials and services provided by EKI, which vary based upon the Company's requirements.

In September 2002, the Company entered into a Loan Agreement with EKI whereby EKI agreed to extend certain loans to the Company at EKI's sole discretion, at interest rates of 7% to 10%. As of December 31, 2002 the outstanding principal amount of outstanding loans was $1,745,000. In January 2003, the Company borrowed an additional $1,010,000 from EKI under the Loan Agreement, bringing the total outstanding principal amount of the loans to $2,755,000. As part of the new convertible debenture financing completed in March 2003 (see Convertible Debentures), repayment of these loans and related interest was subordinated to the new debentures with strict covenants governing their repayment. Therefore, at September 30, 2003, the loans totaling $2,755,000 and related interest of $252,559 are classified as noncurrent liabilities. In March 2003, the Company issued to EKI a warrant, which was immediately exercisable, to purchase 83,333 shares of the Company's common stock at $6.00 per share in connection with the subordination of the loans totaling $2,755,000. The fair value of the warrant was estimated to be approximately $303,522 using the Black-Scholes option pricing model and was recorded as a discount on the outstanding loans.

Convertible Debentures

On March 5, 2003, the Company received proceeds of approximately $9.0 million, net of financing costs of approximately $1.5 million, from the issuance to a group of institutional investors of 416,667 shares of common stock and $10.55 million in aggregate principal amount of secured convertible debentures due in 2006 (the "2006 Debentures"). The 2006 Debentures bear interest at a rate of 2.0% per annum, payable quarterly in arrears on each January 31, April 30, July 31 and October 31. The holders of the 2006 Debentures have the right to convert such debentures into the Company's common stock at a conversion price of $6.00 per share. While the 2006 Debentures are outstanding, the conversion price is subject to adjustment in certain instances, such as a result of stock dividends and splits, distributions of property to common stockholders, the sale of substantially all of the Company's assets, the consummation of a merger, or sales of common stock or common stock equivalents for per share prices lower than the conversion price in effect. In addition to the holders' conversion option, after the first anniversary of the issuance of the 2006 Debentures the

Company has the right to force conversion of all or a portion of the outstanding principal amount of the 2006 Debentures if certain conditions are met, including a requirement that the closing price of the common stock has been equal to or greater than 300% of the conversion price for at least the 10 consecutive days immediately preceding the conversion. The principal amount of the 2006 Debentures is due and payable on March 5, 2006; however, earlier repayment may occur if the Company receives cash

proceeds in excess of $2.65 million (the "Excess Amount") from the sale of debt or equity securities, equipment sales to unrelated third parties, operating revenues, or any cash that becomes available to the Company as a result of a reduction in a $3.5 million letter of credit the Company issued to a third party in 1998. If the Excess Amount arises, the holders of the 2006 Debentures can elect to require one third of such amount to be applied as a 102% prepayment of principal and interest of the 2006 Debentures.

In accordance with Accounting Principles Board Opinion No. 14, "Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants," the Company allocated the net proceeds of $9.0 million to the 2006 Debentures and the common stock based their relative fair values. A discount on the 2006 Debentures of $3.4 million and a discount on the common stock of $604,000 resulted from the fair value allocation. Based on the conversion price of the 2006 Debentures relative to the fair market value for a share of the Company's common stock at the date of issue, the conversion feature of the 2006 Debentures was determined to have no intrinsic value to the holders. If subsequent to the issuance date the conversion price of the 2006 Debentures is adjusted downward, the value of the conversion feature will be re-measured to determine if any beneficial conversion value should be recorded as of the date the conversion price is adjusted. The principal amount of the 2006 Debentures of $10.55 million was recorded as a noncurrent liability, net of a $3.4 million discount. The total discount on the 2006 Debentures of $3.4 million, which is being amortized to interest expense over the 36-month term of the 2006 Debentures using the effective interest method, may be subject to downward adjustments to the extent partial conversions of the 2006 Debentures occur. These adjustments, if required, would reduce the discount and reduce additional paid-in capital.

In addition to the $1.5 million of financing costs, the Company also incurred approximately $646,000 of non-cash costs attributable to 54,167 shares of common stock issued to the lead purchaser of the 2006 Debentures and two warrants issued to a placement agent, both of whom received the instruments as compensation for their services rendered in connection with the transaction. The fair value of the 54,167 shares of common stock issued to the lead purchaser was determined to be $247,000, based on the closing price of $4.56 per share of the Company's common stock on the NASDAQ SmallCap Market on March 5, 2003. The fair value of approximately $42,000 of the first of the two warrants issued to the placement agent, which expires in March 2006 and is immediately exercisable by the placement agent to purchase 28,810 shares of the Company's common stock for $10.08 per share, was estimated using the Black Scholes option-pricing model and is reflected in the accompanying financial statements as an increase in additional paid-in capital and as a component of the $4.0 million aggregate discount on the 2006 Debentures and common stock issued in the March 2003 transaction. The second of the two warrants issued to the placement agent, which expires in March 2006, is immediately exercisable by the placement agent to purchase $1.055 million in aggregate principal amount of the 2006 Debentures and 416,667 shares of the Company's common stock, except if, prior to exercise of the warrant, all of the 2006 Debentures have been redeemed, repurchased or converted, in which case the portion of the warrant exercisable into the 2006 Debentures becomes exercisable into common stock as if the 2006 Debentures

included in the warrant had been converted to common stock. The exercise price of the convertible debenture portion of the warrant is $1,200 for each $1,000 of principal and is subject to adjustment consistent with the provisions of the 2006 Debentures. The exercise price of the common stock portion of the warrant is $7.20 per share. The estimated fair value of this warrant was reflected in the financial statements as a warrant obligation and as a component of the $4.0 million aggregate discount on the 2006 Debentures and common stock issued in the March 2003 financing transaction. At September 30, 2003, the Company evaluated the current value of this warrant, considering its current cash flow projections, continued operating losses, the prospects of raising additional equity capital, the significant excess of the conversion price to the current stock price and the volatility in the Company's stock price. Based upon these factors, the Company determined that the likelihood of the warrant being exercised is remote and has written off the balance of the warrant obligation as of September 30, 2003, resulting in a $0.5 million gain in the three months ended September 30, 2003 that is reflected in "Other (income) expense" in the Statements of Operations.

In connection with the March 2003 financing transactions, the Company prepaid $5.2 million of the $8.2 million principal amount outstanding of the convertible debentures due in 2007 (the "2007 Debentures"), resulting in a prepayment penalty of $208,000. The Company also issued to the holders of the 2007

Debentures 52,083 shares of common stock, valued at $237,500 based upon the closing price of the Company's common stock on the NASDAQ SmallCap Market of $4.56 per share on March 5, 2003. In addition, one of the holders of the 2007 Debentures exchanged $2.0 million aggregate principal amount of 2007 Debentures for $2.0 million aggregate principal amount of 2006 Debentures and 78,989 shares of common stock valued at approximately $360,000 based upon the closing price of the Company's common stock of $4.56 per share on March 5, 2003. In connection with the prepayment and exchange transactions, the Company incurred cash transaction costs of approximately $296,000, excluding the prepayment penalty. The Company recognized a $1.7 million loss upon extinguishment of the 2007 Debentures through the prepayment and exchange. The prepayment of the 2007 Debentures and the debenture exchange resulted in the release to the Company of $2.0 million of restricted cash.

The issuance of the 2006 Debentures, prepayment of the 2007 Debentures (from restricted cash) and the debenture exchange provided the Company with aggregate net proceeds of approximately $11.0 million.

During the quarter ended March 31, 2003, $1.0 million principal amount of the 2006 Debentures was converted into 166,667 shares of common stock resulting in the approximately $665,000 carrying amount of the 2006 Debentures being transferred to common stock.

During the quarter ended June 30, 2003, $850,000 principal amount of the 2006 Debentures was converted into 141,667 shares of common stock resulting in the approximately $773,000 carrying amount of the 2006 Debentures being transferred to common stock.

During the quarter ended September 30, 2003, $3.325 million principal amount of the 2006 Debentures was converted into 554,167 shares of common stock resulting in the approximately $2.5 million carrying amount of the 2006 Debentures being transferred to common stock.

At September 30, 2003, the outstanding principal balance of 2006 Debentures was

$7.375 million, which is reflected on the accompanying balance sheet net of an unamortized discount of approximately $1.8 million.

In October 2003, $575,000 principal amount of the 2006 Debentures was converted into 95,833 shares of common stock, reducing the outstanding principal balance of 2006 Debentures to $6.8 million.

In January and February 2003, the Company forced the conversion of $800,000 principal amount of the 2007 Debentures for 139,599 shares of common stock, resulting in the release to the Company of $800,000 of restricted cash. In June 2003, the holders converted $491,000 principal amount of 2007 Debentures for 81,833 shares of common stock, resulting in the release to the Company of $491,000 of restricted cash. In July 2003, the Company forced the conversion of the remaining $509,000 principal amount of 2007 Debentures for 132,552 shares of common stock, resulting in the release to the Company of $509,000 of restricted cash.

In connection with the March 2003 financing transactions, EKI agreed to subordinate the repayment of its outstanding loans totaling $2,755,000 to the Company's payment obligations under the 2006 Debentures. In addition, EKI and Biotec agreed to subordinate certain payments to which they were otherwise entitled under the Biotec License Agreement (other than their respective percentages of any royalties received by the Company) to the satisfaction of the Company's payment obligations under the 2006 Debentures. They further agreed not to assert any claims against the Company for breaches of the Biotec License Agreement (other than the assertion of certain equitable remedies to enjoin the Company from, for example, selling products outside its field of use) until such time as the Company's obligations under the 2006 Debentures are satisfied in full. EKI and Biotec also agreed to allow the Company to pledge their respective interests in the EKI and Biotec License Agreements to secure the Company's obligations under the 2006 Debentures, and certain additional concessions were made by EKI and Biotec to permit the Company greater flexibility in selling its rights under the EKI and Biotec License Agreements to third parties in an insolvency context. These rights terminate upon the satisfaction in full of the obligations under the 2006 Debentures. In consideration for its willingness to subordinate the payments and advances that are owed to it, in March

2003 the Company issued to EKI a warrant, expiring in ten years, to acquire 83,333 shares of the Company's common stock for $6.00 per share. The fair value of the warrant was estimated to be approximately $303,522 using the Black-Scholes option pricing model and was recorded as a discount on the outstanding loans.

Commitments

During 1998, EKI entered into certain agreements with an equipment manufacturer providing for the purchase by EKI of certain technology applicable to starch-based disposable packaging. EKI licenses such technology to the Company on a royalty-free basis pursuant to the License Agreement. In connection with the purchase, and pursuant to the terms of a letter agreement with EKI, the Company agreed to pay the seller of the technology $3.5 million on or about December 31, 2003, which obligation is secured by a letter of credit, which in turn is secured by $3.5 million of the Company's restricted cash. The Company's obligation to the seller of the technology will be reduced by 5% of the purchase price of any equipment purchased from the seller of the technology by EKI, the Company or their respective licensees prior to the obligation payment date. While the Company believes demand for such equipment will arise in the future, it is unable to estimate when such demand will occur or if such demand will

result in any reduction of this obligation. As a result of these uncertainties and since the obligation will become payable on or about December 31, 2003, the Company established a liability as of December 31, 2002 for the $3.5 million commitment.

In addition, the Company would be required to pay the seller $3.0 million over the five-year period commencing January 1, 2004 if EKI, the Company or their respective licensees make active use of the technology and have not purchased, by December 31, 2003, at least $35.0 million of equipment from the seller. As of September 30, 2003, the Company and its respective licensees have neither actively used the technology nor purchased equipment from the seller. The Company does not plan to make active use of the technology during the year ending December 31, 2003. EKI has agreed to indemnify the Company to the extent the Company is required to pay any portion of this $3.0 million obligation solely as a result of EKI's or its licensees' active use of such patents and related technology (other than use by the Company or its sublicenses). The $3.0 million obligation to the seller of the technology is subject to reduction in an amount equal to 5% of the purchase price of any equipment purchased from the seller by EKI, the Company or their sublicenses during the five-year period commencing January 1, 2004.

Property and Equipment

The cost and accumulated depreciation of property and equipment at September 30, 2003 and December 31, 2002 were as follows:

	September 30, 2003
Commercial Manufacturing Equipment	
Goettingen, Germany..	$ 4,000,000
Other Property and Equipment	
Product development center....................................	1,316,584
Office furniture and equipment................................	718,596
Leasehold improvements..	-
	2,035,180
Total cost..	6,035,180
Less: Accumulated depreciation and amortization.......................	(1,898,154
Property and equipment - net..	$ 4,137,02

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The commercial production line in Goettingen, Germany is being financed and constructed by the Company for the Company's joint venture with Huhtamaki Oyj ("Huhtamaki"). During the third quarter of 2002 the company obtained quotations from various machinery suppliers and determined that the cost to build an identical line was approximately $4.0 million. The Company wrote the carrying value of the line down to its estimated replacement cost.

As the Company sold non-essential machine shop equipment and excess office furniture and equipment in 2003, the related cost and accumulated depreciation were removed from the applicable asset account and Accumulated depreciation, respectively. At the expiration of the leases at the Company's Santa Barbara and Goleta, California facilities in 2003, all leasehold improvements were fully amortized. Due to the relocation to new office space in Santa Barbara, the Company removed the fully amortized leasehold improvements from both the Leasehold improvements and Accumulated amortization accounts.

Stock Options

The Company accounts for stock options in accordance with the provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and complies with the disclosure provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation." Under APB Opinion No. 25, compensation expense is based on the difference, if any, on the date of grant, between the fair value of the Company's common stock and the exercise price of the option. For disclosure purposes, to measure stock-based compensation in accordance with SFAS No. 123, "Accounting for Stock-Based Compensation," the fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The fair value of each option grant is then amortized as pro forma compensation expense over the vesting period of the options. The following table sets forth the pro forma net loss and loss per share resulting from applying SFAS No. 123.

	Three Months Ended September 30,		Ende
	2003	2002	2003
Net Loss as reported..........................	$2,920,797	$6,785,374	$13,299
Deduct: Stock-based employee compensation expense included in reported net loss, net of tax....................................	--	--	
Add: Total stock-based employee compensation determined under fair value based method for all awards, net of tax.................	498,509	1,777,375	695
Pro forma net loss............................	$3,419,306	$8,562,749	$13,995
Net loss per common share			
As reported................................	$0.21	$0.59	$
Pro forma..................................	0.25	0.74	

In December 2002, the Financial Accounting Standards Board issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - An Amendment of FASB Statement No. 123." SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation and requires prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company has elected not to adopt the recognition and measurement provisions of SFAS No. 123 and continues to account for its stock-based employee compensation plans under APB Opinion No. 25 and related interpretations and therefore the transition provisions will not have an impact on the Company's financial position or results of operations. The required

expanded interim disclosures are provided above.

Subsequent Events

Subsequent to September 30, 2003, the Company's Board of Directors approved an amendment, effective as of October 31, 2003, to the Company's Certificate of Incorporation to effect a reverse split of the Company's common stock. This action by the Board of Directors followed approval by 88% of the stockholders of a proposal at the 2003 Annual Meeting that authorized the Board to take such action. The decision by the Board of Directors was prompted by the need to maintain compliance with certain covenants of the Company's 2006 Debentures that require the Company to retain its listing on a national market. To retain its listing on the NASDAQ SmallCap Market, the Company's common stock must trade above a $1.00 minimum bid price for ten consecutive trading days prior to November 18, 2003.

After careful analysis, the Company's Board approved the final ratio for the split at one-for-twelve (1:12), whereby each twelve shares of the Company's issued and outstanding common stock was automatically converted into one share of new common stock. The percentage of the Company's stock owned by each shareholder remained the same. No fractional shares were issued, and instead, the Company's transfer agent will aggregate and sell any fractional shares on the open market and will distribute the pro rata share of the cash proceeds to the holders of fractional share interests.

The reverse split has been retroactively reflected in these financial statements.

In conjunction with the reverse split, the authorized shares of common stock were reduced from 200,000,000 to 25,000,000 as of October 31, 2003.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward Looking Statements

Information contained in this Quarterly Report on Form 10-Q, including "Management's Discussion and Analysis of Financial Condition and Results of Operations," contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. These statements may be identified by the use of forward-looking terminology such as "may," "will," "expect," "anticipate," "estimate," or "continue," or the negative thereof or other comparable terminology. Any one factor or combination of factors could cause the Company's actual operating performance or financial results to differ substantially from those anticipated by management that are described herein. Investors should carefully review the risk factors set forth in other Company reports or documents filed with the Securities and Exchange Commission, including Forms 10-Q, 10-K, 10-K/A and 8-K. Factors influencing the Company's operating performance and financial results include, but are not limited to, changes in the general economy, the availability of financing, governmental regulations concerning, but not limited to, environmental issues, and other risks and unforeseen circumstances affecting the Company's business. This Quarterly Report on Form 10-Q should be read in conjunction with the Company's Annual Report on Form 10-K/A for the fiscal year ended December 31, 2002.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with generally accepted accounting principles requires management to make judgments, assumptions and estimates that affect the amounts reported in the Company's financial statements and the accompanying notes. The amounts of assets and liabilities reported in the Company's balance sheet and the amounts of expenses reported for each fiscal period are affected by estimates and assumptions which are used for, but not limited to, the accounting for asset impairments. Actual results could differ from these estimates. The following critical accounting policies are significantly affected by judgments, assumptions and estimates used in the preparation of the consolidated financial statements.

Estimated Net Realizable Value of Property and Equipment. The Company has been engaged in the development of manufacturing equipment to validate acceptance of EarthShell products and their pricing. To this end the Company constructed manufacturing lines in Owings Mills, Maryland, in Goleta, California and in Goettingen, Germany. The Company evaluates the recoverability of property and equipment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If there is an indication that the carrying value of an asset may not be recoverable and the estimated future cash flows (undiscounted and without interest charges) from the use of the asset are less than the carrying value, a write-down is recorded to reduce the related asset to its estimated fair value.

The Company's ongoing business plans for 2003 call for the transfer of operational and financial control of the manufacturing line in Germany to the Company's manufacturing licensee, PolarCup EarthShell ApS. At such time as the machinery is demonstrated to perform at an agreed upon level, the Company expects to receive reimbursement for the replacement value of the line. The Company is carrying the equipment at its expected replacement value based on quotations from various equipment suppliers for the cost of an identical line. Failure of the equipment to perform at a level satisfactory to the licensee or failure to conclude the transfer of the line to the licensee may require the Company to consider alternative approaches to utilize the equipment, such as finding an alternate licensee to take over, relocating the equipment, or dismantling the line. Any one of these alternatives could have a negative economic impact on the carrying value of the equipment.

Accrued Purchase Commitment. At March 30, 1998, a certificate of deposit for $3.5 million was opened as collateral for the letter of credit related to the Company's obligations under a letter agreement between the Company's controlling stockholder, EKI, and the Company relating to a patent purchase agreement between EKI and a third party, as discussed in the Commitments note, and is classified as restricted cash on the balance sheet at December 31, 2002 and September 30, 2003. As of December 31, 2002 and September 30, 2003, the $3.5 million certificate of deposit and the related accrued purchase commitment are both classified as current in the accompanying balance sheet since the obligation will become payable on or about December 31, 2003.

Fair Value of Warrant Obligation. In connection with the March 2003 financing transactions, the Company issued to a placement agent a warrant, which expires in March 2006, that is immediately exercisable by the placement agent to purchase $1.055 million in aggregate principal amount of the 2006 Debentures and 41,667 shares of the Company common stock, except if, prior to exercise of the warrant, all of the 2006 Debentures have been redeemed, repurchased or converted, in which case the portion of the warrant exercisable into the 2006 Debentures becomes exercisable into common stock as if the 2006 Debentures included in the warrant had been converted to common stock. The exercise price of the convertible debenture portion of the warrant is $1,200 for each $1,000 of

principal and is subject to adjustment consistent with the provisions of the 2006 Debentures. The exercise price of the common stock portion of the warrant is $7.20 per share. The estimated fair value of this warrant was reflected in the financial statements as a warrant obligation and as a component of the $4.0 million aggregate discount on the 2006 Debentures and common stock issued in the March 2003 financing transaction. At September 30, 2003, the Company evaluated the current value of this warrant, considering its current cash flow projections, continued operating losses, the prospects of raising additional equity capital, the significant excess of the conversion price to the current stock price and the volatility in the Company's stock price. Based upon these factors, the Company determined that the likelihood of the warrant being exercised is remote and has written off the balance of the warrant obligation as of September 30, 2003, resulting in a $0.5 million gain in the three months ended September 30, 2003 that is reflected in "Other (income) expense" in the Statements of Operations.

Basis of Financial Statement Presentation. While the Company is continuing to reduce its operating expenses and is working to cause one or more of its licensees to purchase and install equipment to manufacture EarthShell Packaging(R) in order to generate royalty revenue to the Company, the Company will need to raise additional financing to meet its current obligations and to cover operating expenses through the year ending December 31, 2003. This additional financing could be in the form of new financing or the receipt of funds from the transfer of manufacturing lines to its operating partners. The Company cannot be certain that it will be able to raise additional financing by December 31, 2003, that additional financing will be available to it, or, if available, that the terms will be satisfactory, or that it will be able to negotiate mutually agreeable terms for the transfer of the manufacturing lines to its operating partners. If the Company is not successful in raising additional capital or transferring the manufacturing lines, it may not be able to continue as a going concern. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. (See Liquidity and Capital Resources at September 30, 2003).

Revenue recognition. The Company has been manufacturing and selling initial quantities of commercial product in cooperation with its strategic partners as it has worked to demonstrate the commercial viability of its products and manufacturing processes. During its development phase, the Company has recorded the proceeds from such sales since its inception as an offset to the cost of the demonstration manufacturing operations. As the Company transitions the commercial manufacturing of its products to its licensees and begins to earn royalties under its license agreements, it intends to reevaluate its revenue recognition policy.

The key accounting estimates and policies are reviewed with the Audit Committee of the Board of Directors.

Overview of Operations

Three Months Ended September 30, 2003 Compared with the Three Months Ended September 30, 2002.

The Company's net loss decreased $3.9 million to $2.9 million from $6.8 million for the three months ended September 30, 2003 compared to the three months ended September 30, 2002, respectively.

Total Research and Development Expenses. Total research and development expenses are comprised of Related party license fee and research and development expenses and Other research and development expenses. Total research and development expenses for the development of EarthShell Packaging(R) decreased $1.6 million to $1.6 million from $3.2 million for the three months ended September 30, 2003 compared to the three months ended September 30, 2002, respectively.

- Related party license fee and research and development expenses are comprised of the $100,000 monthly licensing fee for the use of the EarthShell Technology and technical services, both of which were payable to EKI. Related party license fee and research and development expenses increased $0.1 million to $0.4 million from $0.3 million for the three months ended September 30, 2003 compared to the three months ended September 30, 2002, respectively. This increase is entirely due to an increase in technical services provided to the Company by Biotec.

- Other research and development expenses are comprised of personnel costs, travel and direct overhead for development and demonstration production, as well as impairment charges on manufacturing property and equipment constructed for demonstration production purposes. Other research and development expenses decreased $1.6 million to $1.3 million from $2.9 million for the three months ended September 30, 2003 compared to the three months ended September 30, 2002, respectively. The decrease in other research and development expenses was primarily due to the lack of equipment impairment charges in 2003 versus $1.8 million of impairment charges in 2002. This reduction was partially offset by costs incurred in connection with testing of the Goettingen, Germany manufacturing equipment during the third quarter and various non-recurring expenses.

Other General and Administrative Expenses. Other general and administrative expenses are comprised of personnel costs, travel and direct overhead for marketing, finance and administration. Total general and administrative expenses decreased $1.0 million to $1.4 million from $2.4 million for the three months ended September 30, 2003 compared to the three months ended September 30, 2002, respectively. This was primarily the result of efforts to significantly reduce general and administrative expenses in 2003, which resulted in reductions in the following expenses: professional fees and services by $0.5 million, personnel costs by $0.1 million, travel costs by $0.1 million and insurance costs by $0.1 million. In addition, in the second quarter of 2003 the Company began a program to satisfy vendors for outstanding aged invoices. As a result of negotiations, the Company settled and paid outstanding accounts payable of approximately $0.4 million in the third quarter at a discount of approximately $0.2 million.

Depreciation and Amortization Expense. Depreciation and amortization expense decreased $0.7 million to $0.1 million from $0.8 million for the three months ended September 30, 2003 compared to the three months ended September 30, 2002, respectively. The decrease in depreciation expense is primarily attributable to the write down of fixed assets as a result of the impairment of equipment to net realizable value during 2002.

Interest Expense. Interest expense is comprised of Related party interest expense and Other interest expense.

- Related party interest expense of $0.1 million for the three months ended September 30, 2003 is interest accrued on outstanding loans made to the Company by EKI under the Loan Agreement (see

Related Party Transactions), plus accretion of the discount related to the warrants issued in conjunction with the March 2003 financing transactions.

- Other interest expense increased $0.2 million to $0.3 million from $0.1 million for the three months ended September 30, 2003 compared to the three months ended September 30, 2002, respectively. Other interest expense for the three months ended September 30, 2003 is primarily composed of accretion of the discount and interest accrued on the 2006 Debentures. Other interest expense for the three months ended September 30, 2002 was primarily composed of the accretion of the discount on the 2007 Debentures.

Gain on Sales of Property and Equipment. Gain on sales of property and equipment of $.1 million for the three months ended September 30, 2003 primarily represents the excess of proceeds received from the sale of non-essential machine shop equipment and excess office furniture and equipment over its net book value.

Other (Income) Expense. Other income of $0.5 million for the three months ended September 30, 2003 represents the gain realized in connection with the write-off of the warrant obligation as of September 30, 2003 (see Convertible Debentures).

Debenture Conversion Costs. Debenture conversion costs of $0.1 million and $0.3 million for the three months ended September 30, 2003 and 2002, respectively, represent the prorated portion of the original discount attributed to the 2007 Debentures converted during the respective periods.

Nine Months Ended September 30, 2003 Compared with the Nine Months Ended September 30, 2002.

The Company's net loss decreased $10.9 million to $13.3 million from $24.2 million for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002, respectively.

Total Research and Development Expenses. Total research and development expenses are comprised of Related party license fee and research and development expenses and Other research and development expenses. Total research and development expenditures for the development of EarthShell Packaging(R) decreased $8.6 million to $5.9 million from $14.5 million for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002, respectively.

- Related party license fee and research and development expenses are comprised of the $100,000 monthly licensing fee for the use of the EarthShell Technology and technical services, both of which were payable to EKI. Related party research and development expenses decreased $0.1 million to $1.0 million from $1.1 million for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002, respectively. This decrease is entirely due to a reduction in technical services provided to the Company by Biotec.

- Other research and development expenses are comprised of personnel costs, travel and direct overhead for development and demonstration production, as well as impairment charges on manufacturing property

and equipment constructed for demonstration production purposes. Other research and development expenses decreased $8.5 million to $4.9 million from $13.4 million for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002, respectively. The decrease in other research and development expenses was primarily due to concluding the demonstration manufacturing of hinged-lid containers in Owings Mills, Maryland at the end of the second quarter of 2002. While the majority of the expenses incurred in the nine months ended September 30, 2002 related to the Owings Mills demonstration manufacturing, it also included expenses related to the commencement of demonstration manufacturing of bowls and plates in Goleta, California. Other research and development expenses for the nine months ended September 30, 2003 related to the ongoing demonstration manufacturing in Goleta through mid-April and to the start-up in mid-May of a new manufacturing line for plates and bowls built and financed by Detroit Tool and Engineering Company (DTE) at their Lebanon, Missouri facility. In early August 2003, the Company discontinued its day-to-day support of manufacturing activities at DTE. In keeping with its business model, the Company will hereafter focus primarily on the licensing of its foam analog material and other technologies, and all future manufacturing and production will be the responsibility of current or new licensees as they install and run equipment to produce EarthShell Packaging(R) in their own facilities. The nine months ended September 30, 2003 also included expenses incurred to vacate the Goleta facility at the expiration of the lease on May 31. The nine months ended September 30, 2002 included impairment charges of $1.9 million

Other General and Administrative Expenses. Other general and administrative expenses are comprised of personnel costs, travel and direct overhead for marketing, finance and administration. Total general and administrative expenses decreased $2.6 million to $4.4 million from $7.0 million for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002, respectively. This was primarily the result of efforts to significantly reduce general and administrative expenses in 2003, which resulted in reductions in the following expenses: professional fees and services by $0.5 million, personnel costs by $0.2 million, travel costs by $0.2 million and facility costs by $0.2 million. In addition, in the second quarter of 2003 the Company began a program to satisfy vendors for outstanding invoices. As a result of negotiations, the Company settled and paid outstanding accounts payable of approximately $1.0 million at a discount of approximately $0.6 million.

Depreciation and Amortization Expense. Depreciation and amortization expense decreased $2.1 million to $0.3 million from $2.4 million for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002, respectively. The decrease in depreciation expense is primarily attributable to the write down in fixed assets as a result of the impairment of equipment to net realizable value during 2002.

Interest Expense. Interest expense is comprised of Related party interest expense and Other interest expense.

o Related party interest expense of $0.3 million for the nine months ended September 30, 2003 is primarily interest accrued on outstanding loans made to the Company by EKI under the Loan Agreement (see Related Party Transactions), plus accretion of the discount related to the warrants issued in conjunction with the March 2003 financing transactions.

  Although the outstanding loans will accrue approximately $0.3 million in annual interest expense, payment of the interest is subordinated to the 2006 Debentures. Therefore, the related party

interest expense will not be paid in cash until the 2006 Debentures have been converted or the obligation satisfied in full.

- Other interest expense increased $1.1 million to $1.2 million from $0.1 million for the nine months ended September 30, 2003 compared to the nine months ended September 30, 2002, respectively. Other interest expense for the nine months ended September 30, 2003 is primarily comprised of accretion of the discount on the 2006 Debentures and a beneficial conversion charge in the amount of $360,000 due to a change in the 2007 Debentures conversion price. In addition, Other interest expense for the nine months ended September 30, 2003 also included accretion of the discount on the 2007 Debentures and interest accrued on the 2006 and 2007 Debentures. Interest expense from accretion of the discount and accrued interest payable on the 2006 Debentures will be approximately $0.8 million per year until they expire or are converted into common stock.

Gain on Sales of Property and Equipment. Gain on sales of property and equipment of $.2 million for the nine months ended September 30, 2003 primarily represents the excess of proceeds received from the sale of non-essential machine shop equipment and excess office furniture and equipment over its net book value. As the Company continues to focus on the licensing of its foam analog material and other technologies, it will continue to liquidation non-essential product development center equipment and excess office furniture and equipment.

Other (Income) Expense. Other income of $0.4 million for the three months ended September 30, 2003 represents the net gain realized in connection with the write-off of the balance of the warrant obligation as of September 30, 2003 (see Convertible Debentures).

Loss on Extinguishment of Debentures. In connection with the March 2003 financing transactions, the Company prepaid $5.2 million of the outstanding $8.2 million principal amount of the 2007 Debentures, resulting in a prepayment penalty of $208,000. The Company also issued the holders of the 2007 Debentures 52,083 shares of common stock, valued at $237,500 based upon the closing price of the Company's common stock of $4.56 per share on March 5, 2003. In addition, one of the holders of the 2007 Debentures exchanged $2.0 million aggregate principal amount of 2007 debentures for $2.0 million aggregate principal amount of 2006 Debentures and 78,989 shares of common stock valued at approximately $360,000 based upon the closing price of the Company's common stock of $4.56 per share on March 5, 2003. In connection with the prepayment and exchange transactions, the Company incurred cash transaction costs of approximately $321,000, excluding the prepayment penalty. In addition, the Company incurred a charge of approximately $0.9 million for the prorated portion of the original discount attributed to the $7.2 million of the 2007 Debentures repaid and exchanged. Therefore, the Company recognized a $1.7 million loss upon extinguishment of the 2007 Debentures through the prepayment and exchange.

Debenture Conversion Costs. Debenture conversion costs of $0.2 million and $0.3 million for the nine months ended September 30, 2003 and 2002, respectively, represent the prorated portion of the original discount attributed to the 2007 Debentures converted during the respective periods.

Liquidity and Capital Resources at September 30, 2003

Cash Flow. The Company's principal use of cash for the nine months ended

September 30, 2003 was to fund operations. Net cash used in operations was $12.3 million for the nine months ended September 30, 2003. Net cash provided by investing activities was $0.2 million for the nine months ended September 30, 2003. Net cash provided by financing activities was $13.5 million for the nine months ended September 30, 2003. As of September 30, 2003 the Company had unrestricted cash and related cash equivalents totaling $1.5 million.

Capital Requirements. The Company paid or accrued $1,320 in capital expenditures for the nine months ended September 30, 2003. Construction of the commercial line installed in cooperation with Huhtamaki at its Goettingen, Germany facility was largely completed in 2002. Therefore the Company does not expect to make significant capital expenditures in the years 2003 or 2004.

Sources of Capital. As part of the Company's initial public offering on March 27, 1998, the Company issued 877,193 shares of common stock, for which it received net proceeds of $206 million. On April 18, 2000 and January 4, 2001, the Company filed shelf registrations statements for 416,667 and 1.25 million shares, respectively, of the Company's common stock. During the years ended December 31, 2002, 2001 and 2000 the Company sold 145,176, 1.1 million and 371,431 shares of common stock in private transactions under such registration statements and received net proceeds from such sales of approximately $2.3 million $30.5 million and $10.5 million, respectively. All shares available under such registration statements were sold as of December 2002.

In December of 2001 the Company filed a shelf registration statement providing for the sale of up to $50 million of securities, including secured or unsecured debt securities, preferred stock, common stock, and warrants. These securities may be offered, separately or together, in distinct series, and in amounts, at prices and on terms to be set forth in the prospectus contained in the registration statement, and in subsequent supplements to the prospectus. During the year ended December 31, 2002, the Company sold 1.9 million shares of common stock in negotiated transactions under such registration statement and received net proceeds from such sales of $19.6 million.

On August 12, 2002 the Company issued $10 million in aggregate principal amount of the 2007 Debentures to institutional investors. These debentures bear interest at a rate of 1.5% per annum. The holders of these debentures had the right to convert the debentures into the Company's common stock at an initial conversion price of $15.60 per share, which has been reduced to $6.00 per share as a result of anti-dilution adjustments. Based on the conversion price relative to the fair market value of the common stock at the date of issue, the debentures were deemed to have no beneficial conversion feature. The proceeds from the debentures are held in restricted accounts linked to irrevocable letters of credit in favor of the debenture holders such that unrestricted access to the proceeds from the sale of the debentures occurs only upon conversion of the debentures into shares of the Company's common stock. In addition to the holders' conversion option, under certain circumstances, the Company has the right to force conversion of up to $500,000 of the debentures per week at a 15% discount to the market price of the Company's stock. Subject to certain conditions set forth in the debentures, the Company may prepay the debentures upon twenty business days notice for 104% of the outstanding principal balance of the debentures. If during any consecutive 90 day period following August 12, 2002, the holders of the debentures or the Company have not converted more than an aggregate of $3.0 million of the original principal amount of $10.0 million or, on August 12, 2003 the holders of the debentures or the Company have not converted more that an aggregate of $7.5 million of the original principal amount of $10.0 million, the holder of the debenture may require the Company to prepay all or a portion of the debentures for an amount in cash equal to the principal amount of the debenture to be prepaid, plus all accrued and unpaid interest, such amount being payable on the 20th trading day following the Company's receipt of a prepayment notice. During the third quarter of 2002, the Company forced conversion of $1.0 million of the debentures for

166,667 shares of common stock, reducing the outstanding balance to $9.0 million. In the first quarter of 2003 the Company forced conversion of an additional $800,000 of the debentures for 139,599 shares of common stock. In March 2003, as part of a new convertible debenture financing, the Company repaid $5.2 million of the debentures, and also exchanged $2.0 million of these debentures for new 2006 Debentures which are not secured by cash, thereby releasing the related cash. In connection with this restructuring, the Company issued approximately 0.6 million shares of common stock to the original debenture holders. In the second quarter of 2003 the holders converted $491,000 of the debentures for 81,833 shares of common stock. In July 2003 the Company forced the conversion of the remaining $509,000 of the debentures for 132,552 shares of common stock.

During 2002, the Company's largest shareholder, EKI, made various simple interest working capital loans to the Company. These loans bear interest at a rate of 7% or 10% per annum, and are payable on demand. As of December 31, 2002, the outstanding principal balance of these loans was $1,745,000. In January 2003, EKI made additional working capital loans to the Company totaling $1,010,000. Some of these loans were not repaid at their stated maturity, and thereby became convertible, at EKI's election, into shares of the Company's common stock. As part of the issuance and sale of the 2006 Debentures completed in March 2003, repayment of these loans totaling $2,755,000 has been subordinated to the 2006 Debentures with strict covenants governing repayment of such loans.

In March 2003, the Company issued and sold $10.55 million in aggregate principal amount of the 2006 Debentures to a group of institutional investors. After transaction fees, the Company realized net proceeds of approximately $9.0 million, which, together with the $2.0 million realized as a result of the exchange of such amount of the 2006 Debentures for a like amount of the 2007 Debentures discussed above, means that the Company gained net proceeds of approximately $11.0 million from the two transactions. In the first quarter of 2003, $1.0 million of the 2006 Debenture principal was converted into 166,667 shares of common stock. During the second quarter ended June 30, 2003, $850,000 of the 2006 Debenture principal was converted into 141,667 shares of common stock. During the quarter ended September 30, 2003, $3,325,000 of the Debenture principal was converted into 554,167 shares of common stock. As of September 30, 2003 there was an aggregate balance of $7.375 million of the 2006 Debentures outstanding. Subsequent to September 30, 2003, $575,000 of the 2006 Debenture principal was converted into 95,833 shares of common stock.

While the Company is continuing to reduce its operating expenses and is working to cause one or more of its licensees to purchase and install equipment to manufacture EarthShell Packaging(R) in order to generate royalty revenue to the Company, the Company will need to raise additional financing to meet its current obligations and to cover operating expenses through the year ending December 31, 2003. The Company cannot be certain that it will be able to raise additional financing by December 31, 2003, that additional financing will be available to it, or, if available, that the terms will be satisfactory, or that it will be able to negotiate mutually agreeable terms for the transfer of the manufacturing lines to its operating partners. If the Company is not successful in raising additional capital or transferring the manufacturing lines, it may not be able to continue as a going concern.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's treasury function controls all decisions and commitments regarding cash management and financing arrangements. Treasury operations are conducted

within a framework that has been authorized by the board of directors.

The Company is exposed to interest rate risk on its fixed rate convertible debentures and notes payable. As of September 30, 2003, these fixed rate debt obligations totaled $10.2 million. The 2006 Debentures bear interest at a fixed rate of 2% per annum. The notes payable bear interest at a fixed rate of 10% per annum. While generally an increase in market interest rates will decrease the value of this debt, and decreases in rates will have the opposite effect, we are unable to estimate the impact that interest rate changes will have on the value of the substantial majority of this debt as there is no active public market for this debt.

Item 4. Controls and Procedures

Evaluation of disclosure controls and procedures. Based on their evaluation of the Company's disclosure controls and procedures as of the end of the period covered by this quarterly report on Form 10-Q, the Company's Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) pursuant to Rule 13a-15 of the Exchange Act. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective to ensure that the Company is able to collect, process and disclose the information it is required to disclose in the report it files with the Securities and Exchange Commission within the required time periods.

Changes in internal control over financial reporting. The Company maintains a system of internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). No significant changes in the Company's internal control over financial reporting have come to management's attention during the Company's last fiscal quarter that have materially affected, or are likely to materially affect, the Company's internal control over financial reporting.

Part II. Other Information

Item 1. Legal Proceedings

In September 2003, two lawsuits were filed against the Company by Green Packaging ("GP") and Green Earth Packaging ("GEP"), both of whom have signed license agreements with the Company permitting their use of the Company's proprietary, biodegradable-packaging technology. The first lawsuit alleges breach of an oral contract involving manufacturing equipment that GP and GEP purchased in order to manufacture biodegradable packaging using the Company's proprietary technology and seeks contract damages in excess of $2 million. The second lawsuit alleges violations of California's antitrust law and Unfair Practices Act involving the commercial viability of the biodegradable-packaging technology that the Company licensed to GP and GEP and seeks unspecified damages in excess of $10 million. Although the Company believes both lawsuits are without merit and intends to vigorously defend against them, an adverse decision in either case would materially adversely impact the financial condition of the Company.

Item 2. Changes in Securities and Use of Proceeds

Not applicable

Item 3. Defaults Upon Senior Securities

Not applicable

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable

Item 5. Other Information

Not applicable

Item 6. Exhibits and Reports on Form 8-K

The Company filed two reports on Form 8-K during the quarter ended September 30, 2003, and two reports on Form 8-K subsequent to September 30, 2003 but prior to the filing of this Form 10-Q. Information regarding the items reported on is as follows:

Date	Item Reported On
July 31, 2003	Engagement of Farber & Hass LLP as the Company's independent public accountants.
August 15, 2003	Press release of the Company dated August 15, 2003, relating to the Company's earnings for the second quarter ended June 30, 2003.
October 17, 2003	Press release of the Company dated October 20, 2003, regarding a reverse stock split.
October 30, 2003	Press release of the Company dated October 30, 2003, relating to the Company's earnings for the third quarter ended September 30, 2003.

31.1 Certification of the CEO pursuant to Rules 13a-14 and 15d-14 under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the CFO pursuant to Rules 13a-14 and 15d-14 under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned.

EarthShell Corporation

Date: November 11, 2003 By: /s/ D. Scott Houston

D. Scott Houston
Chief Financial Officer

(Principal Financial Officer and Duly Authorized Officer)

Income Security Act of 1974 (“ERISA”).

The Company has adopted the MFS Retirement Services, Inc. (“MFS”) Non-Standardized 401(k) Profit Sharing Plan and Trust and appointed MFS Heritage Trust Company as the trustee of the trust established under the Plan.

Effective February 1, 2007, MFS changed its name to Sun Life Retirement Services (U.S.), Inc. (“Sun Life”). Effective March 4, 2008, Sun Life changed its name to The Hartford Financial Services Group, Inc. (“Hartford).

Contributions

Participants may elect to contribute from 1% to 50% of their eligible compensation, subject to Internal Revenue Service (“IRS”) limitations. The Company provides discretionary matching contributions equal to a percentage of participant contributions as determined annually by the Company’s Board of Directors. Additionally, the Company may contribute discretionary profit sharing amounts to the Plan as determined each year by the Company’s Board of Directors. To be eligible to receive matching contributions and profit sharing contributions, participants must be actively employed on the last day of the Plan year and must have completed 1,000 hours of service.

Participants may elect to commence voluntary contributions or modify the amount of voluntary contributions made on the first day of each quarter within the Plan year.

Participant Accounts

A separate account is maintained for each participant and is credited with participant contributions, Company contributions, and actual earnings thereon as well as forfeitures of terminated participants’ non-vested accounts.

AZZ Incorporated Employee Benefit Plan & Trust

Notes to Financial Statements (continued)

A. Description of the Plan - continued

Forfeited Accounts

Forfeited balances of terminated participants' non-vested accounts are reallocated among the remaining participants in the proportion that each participant's compensation for the year bears to the total compensation of all participants for the year.

Investment Options

Upon enrollment in the Plan, a participant may direct contributions to their account in a variety of nine investment options, which vary in degree of risk, with the exception of AZZ incorporated common stock for which participants may only hold or sell existing shares. Participants may change their investment options at any time. Investments are held by Hartford, the record keeper, funding agent, and a party-in-interest. Under a trust agreement with the Company, MFS Heritage Trust Company is a directed trustee. The Plan's assets are invested in accordance with directions provided by the Company.

Vesting

Participant contributions to the Plan plus actual earnings or losses thereon are fully vested at all times. The participant's share of matching contributions and profit sharing contributions and earnings and losses thereon vest in accordance with the following schedule:

Years of Service	Vesting Percentage
Less than 1 year	0%
1 year	20%
2 years	40%
3 years	60%
4 years	80%
5 years	100%

Participants will vest 100% upon attainment of age 65, or in the event of death or disability while employed by the Company.

Loans

Participants may borrow from their account a minimum of $1,000 up to a maximum equal to the lesser of $50,000 or 50% of their vested account balance. Loan terms range from one to five years. The loans are secured by the balance in the participant's account and bear interest at prime. Interest rates for 2008, ranged from 4.0% to 9.25%. Principal and interest are paid ratably through payroll deductions.

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AZZ Incorporated Employee Benefit Plan & Trust

Notes to Financial Statements (continued)

A. Description of the Plan – continued

Participant Withdrawals

On termination of service, if a participant's vested benefits are less than $1,000, the benefit is payable in a lump sum. If the vested benefit is greater than $1,000, the participant may elect to receive either a lump-sum amount or annual installments over a period not to exceed the life expectancy of the participant and the participant's beneficiary. Prior to termination of service, a participant may elect to receive all or any portion of their accrued vested benefit if either the participant has participated in the Plan at least five years or has attained 59 1/2 years of age.

B. Summary of Significant Accounting Policies

The financial statements of the Plan are presented on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Accordingly, actual results may differ from these estimates.

Investment Valuation

Investments in mutual funds are stated at fair value using quoted prices in an active market, which represent the net asset values of shares held by the Plan at year end. The investments in AZZ incorporated common stock are valued at the closing price at year end on the New York Stock Exchange. Amounts invested on a short-term basis are in highly liquid assets; the fair value and cost basis of these invested funds are equal. Purchases and sales of securities are recorded on the trade dates. Gains or losses on sales of securities are calculated using the average cost of the securities sold. Interest income is recorded on the accrual basis.

All investments, earnings thereon, and uninvested cash were held by Hartford under a trust agreement. The Plan's investments are generally subject to market or credit risks customarily associated with debt and equity investments.

Contributions

Participant and employer contributions are accrued in the period in which they are deducted in accordance with salary deferral agreements and as they become obligations of the Company, as determined by the Plan's administrator.

AZZ Incorporated Employee Benefit Plan & Trust

Notes to Financial Statements (continued)

B. Summary of Significant Accounting Policies - continued

Payment of Benefits

Benefits are recorded when paid.

Plan Expenses

Employees of the Company perform certain administrative functions with no compensation from the Plan. The Company or the Plan pays administrative expenses of the Plan. Administrative expenses paid by the Plan are properly reflected in the accompanying statements of changes in net assets available for benefits. There were no administrative expenses paid by the Plan in 2008 or 2007.

C. Investments

At February 29, 2008 and February 28, 2007, individual investments that represent 5% or more of the net assets available for benefits are as follows:

	2008
MFS Total Return Fund A	$ 5,076,117
American Funds Growth Fund of America R4	4,778,143
MFS Value Fund A	4,441,670
MFS Bond Fund A	4,381,390
MFS Global Equity Fund A	4,068,120
MFS Money Market Fund	1,928,246

	2007
MFS Total Return Fund A	$ 4,464,981
MFS Value Fund A	4,311,114
MFS Bond Fund A	4,179,756
American Funds Growth Fund of America R4	3,961,367
MFS Global Equity Fund A	3,758,767
MFS Money Market Fund	1,446,887

During the years ended February 29, 2008 and February 28, 2007, net realized and unrealized gains (losses) were comprised of the following:

	2008	2007
Mutual funds	$ (2,145,296)	$ 744,886

AZZ incorporated common stock		425,312		281,493
Net realized and unrealized gains (losses)	$	(1,719,984)	$	1,026,379

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AZZ Incorporated Employee Benefit Plan & Trust

Notes to Financial Statements (continued)

D. Forfeited Accounts

Approximately $35,000 of forfeitures were allocated to remaining participants during fiscal 2007. At February 29, 2008 and February 28, 2007, net assets available for benefits include approximately $157,000 and $58,000, respectively, of unallocated forfeitures.

E. Excess Contributions Payable

The Internal Revenue Code (the "Code") attempts to ensure that employees at all levels of income share the tax advantages of the Plan proportionally. A non-discrimination test is required by the Code to determine a contribution level that makes all participant contributions, as a percentage of compensation, fall within prescribed limits. The amounts accrued as an excess contributions payable to participants, represent contributions exceeding the allowed limits and will be refunded to employees subsequent to the end of each Plan year.

F. Plan Termination

Although it has not expressed any intent to do so, the Company has the right under the Plan to discontinue its contributions at any time and to terminate the Plan subject to the provisions of ERISA. In the event of Plan termination, participants will become 100% vested in their accounts.

G. Income Tax Status

The Company has adopted the MFS Retirement Services, Inc. Non-Standardized 401(k) Profit Sharing Plan and Trust, which has a favorable opinion letter from the IRS stating that the written form of the prototype plan is acceptable under Section 401(a) of the Code and that any employer adopting this prototype plan document will be considered to have a plan qualified under section 401(a) of the Code. In March 2005, the Plan received a favorable determination letter from the IRS stating that the Plan as adopted is qualified under Section 401(a) of the Code. Once qualified, the Plan is required to operate in conformity with the Code to maintain its qualification. The Plan Administrator believes the Plan is being operated in compliance with the applicable requirements of the Code and, therefore, believes that the Plan is qualified and the related trust is tax exempt.

AZZ Incorporated Employee Benefit Plan & Trust

Notes to Financial Statements (continued)

H. Plan Amendments

Effective March 1, 2006, the Plan was amended to increase the maximum deferral limit to 50%, decrease the required period of service for eligibility from one year to 90 days, and to automatically enroll eligible employees into the Plan with an automatic enrollment provision at 3%.

I. Reconciliation of Financial Statements to Form 5500

The following is a reconciliation of net assets available for benefits, at February 29, 2008 and February 28, 2007, per the financial statements to the Form 5500:

	2008	2007
Net assets available for benefits per the financial statements	$ 31,934,439	$ 28,181,156
Amounts allocated to withdrawing participants	(83,042)	(23,006)
Net assets available for benefits per the Form 5500	$ 31,851,397	$ 28,158,150

Amounts allocated to withdrawing participants are recorded on the Form 5500 for benefit claims that have been processed and approved for payment prior to the Plan's year end but not yet paid as of that date. For financial statement purposes benefit claims are not recorded until payment is made.

AZZ incorporated Employee Benefit Plan & Trust

Form 5500, Schedule H, Line 4i - Schedule of Assets (Held at End of Year)

February 29, 2008

Plan: 001

EIN: 75-0948250

(a)	(b) Identity of Issuer	(c) Description of Investments	(d) Cost		(e) Current Value
*	MFS	MFS Total Return Fund A	**	$	5,076,117
	American Funds	Growth Fund of America R4	**		4,778,143
*	MFS	MFS Value Fund A	**		4,441,670
*	MFS	MFS Bond Fund A	**		4,381,390
*	MFS	MFS Global Equity Fund A	**		4,068,120
*	MFS	MFS Money Market Fund	**		1,928,246
	Columbia	Columbia Acorn Fund A	**		1,022,403
*	AZZ incorporated	AZZ incorporated common stock	**		750,150
	Scudder	Scudder Equity 500 Index Fund	**		611,116
*	Participant loans	Interest rates ranging from 4.0 to 9.25 percent	-0-		842,634
				$	27,899,989

* Represents a party-in-interest to the Plan.

** Cost omitted for participant-directed investments.

SIGNATURES

The Plan. Pursuant to the requirements of the Securities Exchange Act of 1934, the persons who administer the AZZ incorporated Employee Benefit Plan & Trust (the "Plan") have duly caused this annual report for the Plan year ended February 29, 2008 to be signed on its behalf by the undersigned, thereunto duly authorized.

AZZ incorporated Employee Benefit Plan & Trust

Date: August 27, 2008 By /s/ DAVID H. DINGUS
David H. Dingus
Administrative Committee Member

Date: August 27, 2008 By /s/ DANA L. PERRY
Dana L. Perry
Administrative Committee Member

EXHIBIT INDEX

Exhibit No.	Description
23.1	Consent of Independent Registered Public Accounting Firm

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