

EMVELCO CORP.
Form 10KSB
May 30, 2007

**United States
Securities and Exchange Commission**

Washington, D.C. 20549

Form 10-KSB

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

For the fiscal year ended December 31, 2006

OR

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

For the transition period from _____ to _____

Commission File Number 001-12000

EMVELCO CORP.

(Name of small business issuer as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

13-3696015
(I.R.S. Employer
Identification No .)

468 N. Camden Drive, Suite 315, Beverly Hills, CA 90210
(Address of principal executive offices)

Issuer's telephone number, including area code: (310) 285-5350

Securities registered under Section 12(g) of the Exchange Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on which Registered</u>
Common Stock, par value \$.001 per share	NASDAQ CAPITAL MARKET

Check whether the issuer is not required to file reports pursuant to Section 13 or 15 (d) of the Exchange Act.

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirement for the past 90 days. Yes No

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements

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incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)
Yes o No x

The registrant's total revenues for the year ended December 31, 2006 were \$22,594.

The aggregate market value of the registrant's common stock (the only class of voting stock) held by non-affiliates of the Company as of March 26, 2007 was \$3,039,579 based on the closing price of the registrant's common stock on such date of \$1.61 as reported by the Nasdaq Capital Market.

At March 19, 2007, 4,705,546 shares of common stock (the only class of voting stock) were outstanding of which 1,887,937 were held by non-affiliates of the Company.

Transitional Small Business Disclosure Format (check one): Yes o No x

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ITEM 1.

DESCRIPTION OF BUSINESS

History of Business

Emvelco Corp., formerly known as (“f/k/a”) Euroweb International Corp., is a Delaware corporation and was organized on November 9, 1992. It was a development stage company through December 1993. Emvelco Corp. and its consolidated subsidiaries are collectively referred to herein as “Emvelco” or the “Company”.

In 1997, Emvelco entered the Internet field in Hungary and grew through various acquisitions not only in Hungary, but also in the Czech Republic, Slovakia and Romania.

In December 2004, Emvelco disposed of its 100% interest in its subsidiary in Czech Republic and in April 2005, Emvelco sold its 100% interest in its subsidiary in Slovakia.

In October 2005, the Company entered into the information technology (“IT”) sector by acquiring 100% ownership of Navigator Informatika Rt. (“Navigator”), a Hungary-based provider of IT outsourcing, applications development and IT consulting services.

On December 19, 2005, the Company entered into a definitive Share Purchase agreement with Invitel Tavkozlesi Szolgaltato Rt. (“Invitel”) for the sale of its two Internet and telecommunication related operating subsidiaries, Euroweb Internet Szolgaltato Rt. (“Euroweb Hungary”) and Euroweb Romania S.A. (“Euroweb Romania”). Pursuant to the Agreement, the Company sold and, Invitel purchased, 100% of its interest in Euroweb Hungary and Euroweb Romania. The closing occurred on May 23, 2006 and the Company exited the internet service provider (“ISP”) industry. The purchase price was \$30.0 million.

On June 11, 2006, the Board of Directors of Emvelco, as part of its strategy to redirect the Company into new markets, voted to pursue an investor role in real estate business opportunities through focusing on the financial aspects of developing majority or minority owned affiliates, providing loans for the development of property, engaging in the financing segments for development of property and the construction of various types of facilities and investing in real estate opportunities. The Company commenced its investments in the real estate industry through its former wholly-owned subsidiary, Emvelco RE Corp (“ERC”), f/k/a Euroweb RE Corp. in June 2006.

In September 2006, ERC formed Lorraine Properties, LLC (“Lorraine”), a Nevada limited liability company. In October 2006, ERC acquired majority ownership in non-operational asset holding companies as follows: 66.67% of Stanley Hills LLC (“Stanley”), a Nevada limited liability company and 51% of 846 AR Huntley, LLC (“Huntley”), a California limited liability company,

On December 31, 2006, Emvelco and its wholly owned subsidiary ERC entered into an Agreement and Plan of Exchange (“Exchange Agreement”) with Verge Living Corporation (“Verge”), a Nevada corporation and its sole shareholder and unaffiliated third party, The International Holdings Group Ltd. (“TIHG”), a corporation formed and registered in the Marshall Islands. The Exchange Agreement closed on December 31, 2006. Pursuant to the Exchange Agreement, ERC issued new shares to TIHG in exchange for 100% of the outstanding securities of Verge. After the exchange, Emvelco owned 43.33% of ERC and TIHG owned 56.67% of ERC. Verge became a wholly-owned subsidiary of ERC.

Based on the operations of ERC throughout the year and as a result of the Exchange Agreement, the Company's ownership structure as of December 31, 2006, which is discussed further below, was as follows:

- Emvelco directly owns 43.33% of ERC, a real estate development company, 25.1% of Micrologic, Inc. ("Micrologic"), a software development company incorporated in Nevada, and 50% of an investment holding company EA Emerging Ventures Corp. ("EVC"), through a joint venture with Ashfield Finance LLC ("Ashfield").
- ERC directly owns real estate development companies as follows: 100% of Verge, 51% of Huntley, 66.67% of Stanley and 100% of Lorraine. Stanley is a related party as its minority owner is D'vora Attia, sister of Yossi Attia, the Company's CEO.
- ERC directly owns 33.33% of AP Holdings Limited ("AP Holdings"), a Jersey Company. AP Holdings is a related party, as its majority owner is Shalom Atia, the brother of Yossi Attia, the Company's CEO. AP Holdings is a non-operational holding company which owns 100% of Atia Projekt d.o.o, a Croatian Company ("Atia Project"), a real estate development company.

On February 16, 2007, the Company completed the disposal of Navigator and exited from the IT outsource industry, which has been classified as a discontinued operation as of December 31, 2006. Accordingly, the Company's principal operations are solely for financial investment in real estate development.

On May 14, 2007, the Company entered into a Stock Transfer and Assignment of Contract Rights Agreement (the "Stock Transfer Agreement") with ERC, ERC's principal shareholder TIHG, and ERC's wholly owned subsidiary Verge. Pursuant to the Agreement, the Company transferred and conveyed its 1,000 Shares (representing a 43.33% interest) (the "Shares") in ERC to TIHG to submit to ERC for cancellation and return to Treasury. ERC, TIHG and Verge agreed to assign (the "Assignment") to the Company all rights in and to that certain Investment Agreement, dated as June 19, 2006, and all Amendments thereto (collectively, the "Investment Agreement") wherein ERC (from funds available to ERC from the Company) agreed to provide secured loans to Verge for the construction of a multi-use condominium and commercial property in Las Vegas, Nevada (the "Verge Property") and for other projects and properties as provided therein.

The consideration payable to the Company under the Stock Transfer Agreement is \$500,000, which in TIHG's discretion, may be added to the outstanding loan amount owing to the Company by ERC pursuant to the secured line of credit agreement (the "Line of Credit") with ERC, entered into on June 14, 2006, pursuant to which the Company agreed to loan ERC up to \$10.0 million. In December 2006, the Board of Directors and Audit Committee of the Company approved an increase of the Line of Credit up to \$20.0 million. ERC can use this line for the various different projects they are engaged in. The loans are payable on demand and accrue interest at 12% per annum.

As of December 31, 2006, the outstanding Line of Credit owing to the Company is approximately \$12 million. Under the Stock Transfer Agreement, in no event shall the Line of Credit exceed eighty percent (80%) of the fair market value of the Verge Property. As a condition precedent to the Stock Transfer Agreement, a current appraisal of the Verge Property shall be presented and delivered to the Company within two weeks of the date of the Stock Transfer Agreement.

The effective date of the Stock Transfer Agreement is January 1, 2007 (the "Effective Date"). All rights assigned to the Company under the Investment Agreement will be considered to be assigned as of the Effective Date. Accordingly, as of the Effective Date, the Company shall be the sole secured and primary beneficiary under the Investment Agreement, and the Company shall have no ownership interest in ERC.

As of the Effective Date, under the Investment Agreement, each loan made to Verge is due on demand or upon maturity on January 14, 2008. If the Company requests that the funds be paid on demand prior to maturity, then Verge shall be entitled to reduce the amount requested to be prepaid by 10%. The 10% discount will be paid in the form of shares of common stock of the Company, which will be computed by dividing the dollar amount of the 10% discount by the market price of the Company's shares of common stock. The terms of the loans require that the Company, be paid-off the greater of (i) the principal including 12% interest per annum or (ii) 33% of all gross profits derived from the Verge Property. In addition, the Company has the right to acquire the Verge Property for a purchase price of \$15,000,000 through January 1, 2015. The purchase is payable in \$10,000,000 in cash and \$5,000,000 in shares of common stock of the Company.

Currently, the Company does not have operations in Hungary. The Company's headquarters are now located in Beverly Hills, California.

Emvelco Strategy

REAL ESTATE DEVELOPMENT IN THE UNITED STATES OF AMERICA

In June 2006, the Company commenced its financial investments in the real estate industry through the acquisition of ERC. ERC was a shell corporation with no operations seeking opportunities in the real estate industry. Based on the parameters set by the Board of Directors, ERC's opportunities are limited as follows:

- any investment in the real estate opportunity (the "Proposed RE Investment"), including loans, shall not exceed a planned period of three years;
- the expected return on investment on the Proposed real estate Investment must be a minimum of 15% per year;
- the Proposed RE Investment shall not be leveraged in excess of more than \$1.50 for each \$1.00 invested in equity; and
- each Proposed RE Investment shall have a clear exit strategy (i.e. purchase, development and sale) and no Proposed RE Investment will be intended to acquire income producing real estate.

On June 14, 2006, the Company entered into a secured line of credit agreement (the "Line of Credit") with ERC, pursuant to which the Company agreed to loan ERC up to \$10.0 million. In December 2006, the Board of Directors and Audit Committee of the Company approved an increase of the Line of Credit up to \$20.0 million. ERC can use this line for the various different projects they are engaged in. The loans are payable on demand and accrue interest at 12% per annum. At December 31, 2006, the balance on the secured Line of Credit was \$11.3 million.

On June 19, 2006, ERC entered into the Investment Agreement with Verge, f/k/a The Aquitania Corp. and AO Bonanza Las Vegas, Inc., pursuant to which ERC, within its sole discretion, agreed to provide secured loans to Verge, as part of the Line of Credit described above, which is not to exceed the amount of \$10.0 million. Verge is developing the Verge Property in downtown Las Vegas, Nevada, where it intends to build approximately 296 condominiums plus commercial space. Verge obtained entitlements to the Verge Property, and has advised that it expects to break ground and commence sales during 2007. Each loan provided to Verge is due on demand or upon maturity on January 14, 2008. All loans are secured by a first deed of trust, assignment of rents and security agreement with respect to the property, along with American Land Title Association ("ALTA") title policy issued by a title company.

In October 2006, as part of developing the Company's financial real estate development business, ERC acquired a majority ownership in two real estate companies, Huntley and Stanley, which are planning for the development of two to three unit residences. In September, ERC also formed Lorraine, which are lots designated for an apartment or condominium complex containing 14 multi-family units. ERC is also developing single family homes in Los Angeles known as the Harper, Edinburgh and Laurel projects.

On December 31, 2006, Emvelco and its wholly-owned subsidiary ERC entered into an Exchange Agreement with Verge and its sole shareholder, TIHG an unaffiliated third party. The Exchange Agreement closed on December 31, 2006. Pursuant to the Exchange Agreement, ERC issued new shares to TIHG in exchange for 100% of the outstanding securities of Verge. After the exchange, Emvelco owned 43.33% of ERC and TIHG owned and control 56.67% of ERC. Verge became a wholly-owned subsidiary of ERC.

On May 14, 2007, pursuant to the Stock Transfer Agreement, the Company transferred and conveyed its 1,000 Shares (representing a 43.33% interest) in ERC to TIHG to submit to ERC for cancellation and return to Treasury. ERC, TIHG and Verge agreed to assign to the Company all rights in and to the Investment Agreement.

The consideration payable to the Company under the Stock Transfer Agreement is \$500,000, which in TIHG's discretion, may be added to the outstanding loan amount owing to the Company by ERC pursuant to the secured line of credit agreement (the "Line of Credit") with ERC, entered into on June 14, 2006, pursuant to which the Company agreed to loan ERC up to \$10.0 million. In December 2006, the Board of Directors and Audit Committee of the Company approved an increase of the Line of Credit up to \$20.0 million. ERC can use this line for the various different projects they are engaged in. The loans are payable on demand and accrue interest at 12% per annum.

As of December 31, 2006, the outstanding Line of Credit owing to the Company is approximately \$12 million. Under the Stock Transfer Agreement, in no event shall the Line of Credit exceed eighty percent (80%) of the fair market value of the Verge Property. As a condition precedent to the Stock Transfer Agreement, a current appraisal of the Verge Property shall be presented and delivered to the Company within two weeks of the date of the Stock Transfer Agreement.

OTHER INVESTMENTS

(a) EA Emerging Ventures Corp. ("EVC").

On August 30, 2006, the Company entered into an agreement by and between the Company and Ashfield Finance LLC ("Ashfield"), a Delaware limited liability company to form, develop and initially fund EVC, a Nevada Corporation. The agreement was developed for the purpose of identifying Electronic Design Automation ("EDA") and IT development projects, as well as potential financing of real estate properties related thereto and other business ventures and investments. EVC is owned 50% by the Company and 50% by Ashfield. The Company shall provide the initial funds for implementation of the business purposes of the joint venture and shall be entitled to a first priority return on any proceeds or income received by EVC. Ashfield shall provide services in the area of business, finance and taxation advice and has entered into a Consulting Agreement with EVC regarding these services. In consideration

for such services, Ashfield shall receive its 50% interest as well as a payment of \$10,000 per month. EVC is evaluating various projects, although at the present time, has not presented the Company with a specific project for consideration. EVC is a shell company as of the date of this filing.

(b) Micrologic, Inc.

On October 11, 2006, as the first transaction in connection with the agreement with Ashfield (where Ashfield and EVC accepted no consideration) (see above), the Company entered into a Term Sheet that will be formally documented in a contract with associated exhibits, License Agreement and Warrants by and between the Company and Dr. Danny Rittman - a third party, in connection with the formation and initial funding of Micrologic, Inc. ("Micrologic"), a Nevada corporation, for the design and production of EDA applications and Integrated Circuit ("IC") design processes; specifically, the development and production of the NanoToolBox™ tools suite which shortens the time to market factor. NanoToolBox™ is a smart platform that is designed to accelerate IC's design time and shrink time to market factor. The Term Sheet provides for an initial investment by the Company of up to \$1.0 million, with warrants to purchase additional equity for additional investment. Initially, the Company owns 25.1% and Dr. Rittman owns 74.9% of Micrologic, Inc. but such equity positions would be revised depending upon the exercise of the warrants as follows: (1) Warrant A - the Company shall be granted a two year option to acquire an additional 10% of Micrologic for \$1.0 million (2) Warrant B - the Company shall be granted a three year option to acquire an additional 15% of Micrologic for \$3.0 million. The consideration of warrants A and B can be paid at the discretion of the Company, 50% in cash and 50% in the Company's shares. As of December 31, 2006, \$50,000 was transferred by the Company as part of this commitment and no warrants were purchased. Micrologic will enter into a License Agreement with Dr. Danny Rittman, which grants Micrologic the right to technology invented, owned and registered by Dr. Rittman. Parties agreed that this investment will be handled directly between Micrologic and Emvelco without the involvement of EVC or Ashfield, however, the Company has no influence over the operation of Micrologic. The Company and Dr. Rittman are working on finalizing these agreements, which have not been signed as of the date of this report.

(C) AP Holdings Limited - A Jersey Corporation ("AP Holdings")

As a result of the Exchange Transaction entered into on December 31, 2006, ERC, through Verge, acquired a 33.33% equity investment in AP Holdings Limited, a Jersey Company for \$3.0 million which was paid in cash at closing. AP Holdings, a non-operational holding Company owns 100% of Atia Projekt d.oo. ("Atia Project"), a Croatian company engaged in real estate development. The Company has no influence over the operation of AP Holdings. The majority owner (66.67%) of AP Holdings is Shalom Atia, the brother of the Company's Chief Executive Officer. During the accounting related to the Exchange Transaction, it was determined that there is no accounting value associated with this investment and therefore, the fair value of AP Holdings is its cost as of December 31, 2006.

The Company may invest in other unidentified industries that the Company deems profitable. If the opportunity presents itself, the Company will consider implementing its consolidation strategy with its subsidiaries and any other business that it enters. However, the Company does not presently have any plans, proposals or arrangements to redeploy its remaining capital funds or engage in any specific acquisitions. The Company has not yet identified any additional specific industries in which to invest.

History of Acquisitions and Dispositions - ISP and IT industry

Over the past nine years, Emvelco participated in the ISP market in Central Europe through various acquisitions of companies in that geographic area. In 2005, the scope of the Company's business activity was changed by the decision to sell the Company's operations in the ISP market and furthermore by the acquisition of Navigator, a company active in the IT services industry. In 2007, the Board also approved the exit from IT service industry, and completed the exit with the sale of Navigator. Currently, the Company has no operations in Hungary. A history of the Company's acquisitions and disposals within the ISP and IT industry are presented below.

Hungary

On January 2, 1997, the Emvelco acquired all of the outstanding stock of three Hungarian ISPs for a total purchase price of approximately \$1,785,000, consisting of 28,800 shares of common stock of the Company and \$1,425,000 in cash (collectively, the "1997 Acquisitions"). The 1997 Acquisitions included the following:

- EUNET (Hungary Ltd.) for a cost of \$1,000,000 in cash, and the assumption of \$128,000 in liabilities;
- E-Net Hungary Telecommunications and Multimedia for a cost of \$200,000 in cash and \$150,000 in stock (12,000 shares); and
- MS Telecom Rt. for a cost of \$225,000 in cash and \$210,000 in stock (16,800 shares).

Subsequent to completion of these acquisitions, all three Hungarian companies were combined and merged into a new Hungarian entity, Euroweb Hungary. On November 22, 1998, the Company sold 51% of the outstanding shares of Euroweb Hungary to Pantel Rt. ("Pantel") for \$2,200,000 in cash and an agreement to increase the share capital of Euroweb Hungary by \$300,000 without changing the ownership ratio. In February 2004, the Company acquired the 51% of Euroweb Hungary that it had sold to Pantel. The consideration paid by the Company for the 51% interest comprised \$2,105,000 in cash and a guarantee that Euroweb Hungary will purchase at least \$3,000,000 worth of services from Pantel in each of the three years ending December 31, 2006. The purchase commitment was fulfilled by Euroweb Hungary.

On June 9, 2004, the Company acquired all of the outstanding shares of Elender, an ISP located in Hungary that provides Internet access to the corporate and institutional (public) sector and, amongst others, 2,300 schools in Hungary. Consideration paid in the amount of \$9,350,005 consisted of \$6,500,000 in cash and 677,201 of the Company's shares of common stock, valued at \$2,508,353 excluding registration cost, and \$391,897 in transaction costs (consisting primarily of professional fees incurred related to attorneys, accountants and valuation advisors).

Under the terms of this agreement, the Company placed 248,111 unregistered shares of newly issued stock (in the name of the Company) with an escrow agent as security for approximately \$1.5 million loans payable to former shareholders of Elender. The shares will be returned to the Company from escrow once the outstanding loans have been fully repaid. However, if there is a default on the outstanding loan, then the shares will be issued to the other party and the Company is then obliged to register the shares. As of December 31, 2005, the Company repaid all of the loans that were outstanding. In January 2006, the Company acquired and subsequently cancelled the shares that were put into escrow.

On October 7, 2005, the Company acquired all of the outstanding shares of Navigator, a Hungary-based provider of IT outsourcing, applications development and IT consulting services. Consideration paid in the amount of \$10,760,772 consisted of \$8,500,000 in cash and 441,566 shares of the Company's common stock valued at \$1,752,134 excluding registration cost, and \$508,638 in transaction costs (consisting primarily of professional fees incurred related to attorneys, accountants and valuation advisors).

On December 19, 2005, Emvelco entered into a share purchase agreement with Invitel for the sale of Euroweb Hungary and Euroweb Romania. The purchase price for the subsidiaries specified in the share purchase agreement was approximately \$30 million. As part of the closing, approximately \$6 million of the cash proceeds paid by Emvelco were paid to Euroweb Hungary in exchange for the 85% ownership of Navigator currently held by Euroweb Hungary. This cash was used by Euroweb Hungary for the repayment of an approximately \$6 million bank loan obtained for the acquisition of Navigator. The closing of the sale of Euroweb Hungary and Euroweb Romania occurred on May 23, 2006.

On February 16, 2007, the Company completed the disposal of Navigator. The purchase price paid to the Company is \$3,200,000 in cash and the transfer to the Company of 622,531 shares of the Company. On May 3, 2007 the Company surrendered 622,531 stock certificates together with stock powers to American Stock Transfer & Trust Company, the Company's transfer agent for cancellation and return to Treasury.

Romania

On May 19, 2000, the Company purchased all of the Internet related assets of Sumitkom Rokura, S.R.L., an ISP in Romania, for \$1,561,125 in cash. The acquisition was accounted for as an asset purchase with a value of \$1,150,000 being assigned to the customer lists acquired.

On June 14, 2000, the Company acquired all of the outstanding shares of capital stock of Mediator S.A., an ISP in Romania for \$2,040,000 in cash and the assumption of a \$540,000 liability to the former owner payable in annual installments of \$180,000, commencing on June 1, 2001. Goodwill arising on this purchase was \$2,455,223. Immediately after the purchase, the name of this company was changed to Euroweb Romania. This acquisition was effective as of July 1, 2000.

On December 19, 2005, Emvelco entered into a share purchase agreement with Invitel for the sale of Euroweb Hungary and Euroweb Romania. The purchase price for the subsidiaries specified in the share purchase agreement was approximately \$30 million. As part of the closing, approximately \$6 million of the cash proceeds paid by Emvelco were paid to Euroweb Hungary in exchange for the 85% ownership of Navigator currently held by Euroweb Hungary. This cash was used by Euroweb Hungary for the repayment of an approximately \$6 million bank loan obtained for the acquisition of Navigator. The closing of the sale of Euroweb Hungary and Euroweb Romania occurred on May 23, 2006.

Czech Republic

On June 11, 1999, the Company acquired all of the participating interests of Luko CzechNet, an ISP in the Czech Republic, for a total cost of \$1,862,154, including 90,000 shares of the Company's common stock and 50,000 options valued at \$2.00 per share; the balance paid in cash. This acquisition was effective as of June 1, 1999.

On August 25, 2000, the Company, through its subsidiary, Luko Czech, acquired all of the outstanding capital stock of Stand s.r.o., an ISP in the Czech Republic, for \$280,735 in cash. Stand s.r.o. was merged into Luko Czech under the name of Euroweb Czech Republic. This acquisition was effective as of September 1, 2000.

On December 16, 2004, the Company sold all of its shares in its wholly-owned subsidiary, Euroweb Czech for cash of \$500,000. Additionally, as a part of the transaction, the Company forgave \$400,000 of loans receivable from Euroweb Czech.

Slovakia

On July 15, 1999, the Company acquired all of the outstanding shares of capital stock of EUNet Slovakia, an ISP in the Slovak Republic, for a total cost of \$813,299 including 47,408 shares of the Company's common stock valued at \$400,005 issued August 9, 1999; the balance was paid in cash. This acquisition was effective as of August 1, 1999.

The Company made another acquisition of a Slovak ISP on July 15, 1999 with the purchase of 70% of the outstanding shares of Dodo s.r.o.'s subsidiary, R-Net, for a total cost of \$630,234, including 29,091 shares of the Company's common stock valued at \$200,000 issued August 13, 1999; the balance was paid in cash. This acquisition was effective as of August 1, 1999.

On September 23, 1999 and November 16, 1999, the Company acquired from Slavia Capital o.c.p., a.s. 70% and 30%, respectively, of the issued and outstanding stock of Global Network Services a.s.c., a Slovakian corporation providing Internet service primarily to businesses located in Bratislava and other major cities in Slovakia for a total purchase price of \$1,633,051, including 71,114 shares of the Company's common stock valued at \$499,929 issued on September 23, 1999; the balance was paid in cash. The acquisition of 70% of Global Network Services a.s.c. was effective as of October 1, 1999.

On April 21, 2000, the Company acquired all of the outstanding capital stock of Iinternet SR, s.r.o., an ISP in the Slovak Republic, for \$1,029,299 in cash. Goodwill arising on this purchase was \$945,200. This acquisition was effective May 1, 2000.

On May 22, 2000, the Company acquired the remaining 30% of R-Net (the initial 70% being acquired in 1999) for \$355,810 in cash. Goodwill arising on this purchase was \$357,565.

All of the Company's Slovakian operations were then merged into one company under the name of Euroweb Slovakia. On April 15, 2005, Emvelco sold 100% of its interest in its wholly-owned subsidiary Euroweb Slovakia to DanubiaTel a.s. The purchase price was \$2,700,000.

Euroweb Hungary, Euroweb Slovakia, Euroweb Czech, Euroweb Romania and Navigator are classified as discontinued operations in the Company's financial statements for all periods presented.

History of Acquisitions and Dispositions - Financial Investment in Real Estate Industry

On June 11, 2006, the Company commenced operations in the financial aspects of the real estate industry through the acquisition of a non-operational, wholly-owned subsidiary, ERC, which was acquired for a stock purchase price totally \$1,000. The primary activity of ERC includes development and subsequent sale of real estate, as well as investment in the form of loans provided to, or ownership acquired in, property development companies, directly or via majority or minority owned affiliates.

In the third quarter of 2006, ERC acquired the following non-operational asset holding companies: 51% in Huntley for a purchase price of \$510, 66.67% of Stanley for a purchase price \$667 and 100% of Lorraine for a capital contribution of \$1,000.

On December 31, 2006, Emvelco and its wholly-owned subsidiary ERC entered into an Exchange Agreement with Verge and its sole shareholder, TIHG. The Exchange Agreement closed on December 31, 2006. Pursuant to the Exchange Agreement, ERC issued 1,308 new shares to TIHG in exchange for 100% of the outstanding securities of Verge, resulting in TIHG having voting control over ERC. Subsequent to the exchange, Emvelco owned 43.33% of ERC, while TIHG owned the remaining 56.67%. Verge became a wholly-owned subsidiary of ERC.

On May 14, 2007, pursuant to the Stock Transfer Agreement, the Company transferred and conveyed its 1,000 Shares (representing a 43.33% interest) in ERC to TIHG to submit to ERC for cancellation and return to Treasury. ERC, TIHG and Verge agreed to assign to the Company all rights in and to the Investment Agreement.

Products and Services

Upon completion of the sale of Navigator in February 2007, which is presented as discontinued operations for the year ended December 31, 2006, the Company no longer operates within the IT outsourcing industry.

Since June 2006, the Company is engaged in the financial aspects of acquisition, development, management, rental and sale of commercial, multi-family and residential real estate properties located primarily the United States of America ("US"). The Company is also engaged in investment and financing activities, as well as conducting real estate operations on its own properties. Currently, all of the real estate properties are in the initial phase of development, and therefore no sales of property have occurred.

Organization

Project management

The Company employs five full-time professionals including management, in its Beverly Hills, California headquarters. Headquarter personnel are responsible for project management, bid-management and operations service management activities. Their main tasks involve creating business and interaction with subsidiaries and vendors. Post the Exchange Agreement with TIHG, the Company currently employs one full time employee.

Employees

As of March 31, 2007, the Company employed a total of 5 full-time employees.

Government Regulations

The Company's subsidiary or affiliate operations are subject to building, environmental and other codes, ordinances, zoning, building design and regulations of various federal, state, and local governing authorities to comply with building permit, as well as on-going-inspections, including local regulations which impose restrictive zoning and density requirements in order to limit the number of homes that can eventually be built within the boundaries of a particular property or locality. We must satisfy valuation standards and site, material and construction requirements of those authorities. More stringent requirements could be imposed in the future on homebuilders and developers, thereby increasing the cost of compliance.

In addition, the Company is subject to various licensing, registration and filing requirements in connection with the construction, advertisement and sale of homes in its communities. Although these laws have increased our overall costs, they have not had a material effect on the Company.

Competition

The real estate development business is highly competitive and fragmented. We compete with numerous real estate developers of varying sizes, ranging from local to national in scope, some of which have greater sales and financial resources than we have.

Our dedication to customer satisfaction is evidenced by our consumer and value-based brand approach to product development, and we believe that this dedication distinguishes us in the homebuilding industry and will contribute to our long-term competitive advantage. The real estate industry in the United States, however, is highly competitive. In each of our market areas, there are numerous real estate developers with which we compete. We also compete with the resale of existing house inventory. Any provider of housing units, for-sale or to rent, including apartment builders, may be considered a competitor. Conversion of apartments to condominiums further provides certain segments of the population an alternative to traditional housing, as well as manufactured housing. We compete primarily on the basis of price, reputation, design, location and quality of our homes. The real estate industry is affected by a number of economic and other factors including: (1) significant national and world events, which impact consumer confidence; (2) changes in the costs of building materials and labor; (3) changes in interest rates; (4) changes in other costs associated with home ownership, such as property taxes and energy costs; (5) various demographic factors; (6) changes in federal income tax laws; (7) changes in government mortgage financing programs, and (8) availability of sufficient mortgage capacity. In addition to these factors, our business and operations could be affected by shifts in demand for new homes.

Risk Factors

In addition to the other information contained in this Annual Report on Form 10-KSB, the following risk factors should be considered carefully in evaluating our business. Our business, financial condition, or results of operations or future prospects could be materially adversely affected by operating results, and could cause our actual results to differ materially from our plans, projections, or other forward-looking statements included in "Item 6. Management's Discussion and Analysis of Financial Condition and Results of Operations" below and elsewhere in this Report on Form 10-KSB.

We have incurred a loss from continuing operations for the prior periods and we will again incur net losses if we are unable to generate sufficient revenue and control costs.

We incurred a loss from continuing operations of \$2,279,285 for the year ended December 31, 2006 and \$1,703,466 for the year ended December 31, 2005. We may not achieve profitability on a quarterly or annual basis in the future. If revenues grow more slowly than we anticipate, or if operating expenses exceed our expectations or cannot be adjusted

accordingly, we will continue to incur losses. Our future performance is dependent upon the successful development and marketing of our services and products and additional acquisition about which there is no assurance. Any future success that we might enjoy will depend upon many factors, including factors out of our control or which cannot be predicted at this time. These factors may include changes in or increased levels of competition, including the entry of additional competitors and increased success by existing competitors, changes in general economic conditions, increases in operating costs, including costs of supplies, personnel and equipment, reduced margins caused by competitive pressures and other factors. These conditions may have a materially adverse effect upon us or may force us to reduce or curtail operations.

Our common stock may be delisted by the Nasdaq Capital Market

(1,075

)

(52,271

)

5,426

Other revenues

3,516

2,651

13,005

11,499

Total revenues

89,626

107,521

374,326

439,224

Benefits and expenses

Policyholder benefits

43,894

39,823

178,749

166,458

Interest credited to policyholder

account balances

21,780

23,096

86,899

91,215

Amortization of deferred acquisition costs

and value of business acquired

12,620

10,873

42,084

40,333

Operating expenses

21,966

22,543

92,808

88,307

Total benefits and expenses

100,260

	96,335
	400,540
	386,313
Income (loss) before income tax expense (benefit)	
)	(10,634
	11,186
)	(26,214
	52,911
Income tax expense (benefit)	
)	(3,483
	4,774

	(9,164
)	
	17,250
<i>Net income (loss)</i>	
\$	
	(7,151
)	
\$	
	6,412
\$	
	(17,050
)	
\$	
	35,661

Other comprehensive income (loss), net of taxes:

Change in net unrealized gains and losses on

securities available for sale

\$

	(16,157
)	
\$	
	16,991
\$	
	(89,921
)	
\$	
	6,396
Change in minimum pension liability	
	(21,067
)	
	(1,089
)	
	(21,067
)	
	(1,089
)	
Other comprehensive income (loss)	

	(37,224
)	
	15,902
	(110,988
)	
	5,307
Comprehensive income (loss)	
\$	
	(44,375
)	
\$	
	22,314
\$	
	(128,038
)	
\$	
	40,968

Per common share:

Net income (loss), basic and diluted

\$ (0.62

)
\$ 0.54

\$ (1.47

)
\$ 3.01

Cash dividends

\$ 0.27

\$ 0.27

\$ 1.08

\$

**Consolidated
Statements of Cash Flows
(Thousands)**

	Year ended December 31	
	<u>2008</u>	<u>2007</u>
Operating activities		
Net cash provided	\$ 12,337	\$ 32,897
Investing activities		
Purchases of investments:		
Fixed maturity securities	(251,136)	(313,080)
Equity securities	(8,300)	(15,249)
Mortgage loans	(49,273)	(54,816)
Real estate	(30,138)	(4,507)
Sales of investments:		
Fixed maturity securities	33,499	168,259
Equity securities	8,811	4,583
Real estate	30,613	22,457
Other investment assets	5,883	7,930
Maturities and principal paydowns of investments	308,981	259,435
Net dispositions (additions) to property and equipment	3	(969)
Proceeds from sale of non insurance affiliate	—	10,104
Net cash provided	48,943	84,147
Financing activities		
Proceeds from borrowings	100,962	122,830
Repayment of borrowings	(108,462)	(127,130)
Deposits on policyholder account balances	200,465	205,767
Withdrawals from policyholder account balances	(240,508)	(294,799)
Net transfers from separate accounts	8,556	11,706
Change in other deposits	4,525	13,703
Cash dividends to stockholders	(12,483)	(36,420)
Net acquisition of treasury stock	(16,773)	(4,451)
Net cash used	(63,718)	(108,794)
Increase (decrease) in cash	(2,438)	8,250
Cash at beginning of year	12,158	3,908

Cash at end of period	\$	9,720	\$	12,158
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Notes

- Net income per common share was based upon the average number of shares outstanding of 11,446,029 and 11,795,878 for the fourth quarters and 11,566,805 and 11,836,213 for the years ended December 31, 2008 and 2007, respectively.
- Cash dividends include a one-time special dividend of \$2.00 per share, paid on February 13, 2007.
- These financial statements should be read in conjunction with the Company's Form 10-K. Please refer to the Company's Form 10-K as filed with the U.S. Securities and Exchange Commission.
- Certain immaterial amounts in prior years have been reclassified to conform with the current year presentation.

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 thereunto duly authorized.

KANSAS CITY LIFE INSURANCE COMPANY

(Registrant)

By: /s/ James F. Aldrich

James F. Aldrich,
Associate General Counsel

March 11, 2009

(Date)