

Edgar Filing: TSET INC - Form 10QSB

TSET INC  
Form 10QSB  
November 15, 2002

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-QSB

Quarterly Report Pursuant to Section 13 or 15(d)  
of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2002

Transition Report under Section 13 or 15(d)  
of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

COMMISSION FILE NO. 000-30191

TSET, INC.  
-----

(Exact name of registrant as specified in its charter)

NEVADA  
-----

(State of other jurisdiction of  
incorporation or organization)

464 Common Street, Suite 301, Belmont, MA  
-----

(Address of principal executive offices)

87-0440410  
-----

(I.R.S. Employer Identification  
Number)

02478  
-----

(Zip Code)

Registrant's telephone number, including  
area code:  
-----

(617) 993-9965  
-----

(1) Registrant 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. X Yes No

As of November 10, 2002, there were 46,891,296 shares outstanding of the issuer's common stock.

PART I

FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

The following comprise our condensed (unaudited) consolidated financial statements for the three months ended September 30, 2002.

Edgar Filing: TSET INC - Form 10QSB

2

TSET, INC  
CONSOLIDATED BALANCE SHEETS

	SEPTEMBER 30, 2002	JUNE 30, 2002
	-----	-----
ASSETS		
Current Assets		
Cash	\$ 24	\$ 21,510
Accounts receivable, net	26,650	700
Prepays	66,649	101,029
	-----	-----
TOTAL CURRENT ASSETS	93,322	123,239
	-----	-----
PROPERTY AND EQUIPMENT	62,723	62,723
Less: Accumulated Depreciation	(38,143)	(33,348)
	-----	-----
NET PROPERTY AND EQUIPMENT	24,580	29,375
	-----	-----
OTHER ASSETS		
Intangibles	2,146,076	2,213,917
	-----	-----
TOTAL OTHER ASSETS	2,146,076	2,213,917
	-----	-----
TOTAL ASSETS	\$ 2,263,979	\$ 2,366,531
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 1,324,419	\$ 956,684
Accrued expenses	403,962	284,761
Notes payable, current portion	463,165	535,700
	-----	-----
TOTAL CURRENT LIABILITIES	2,191,546	1,777,145
	-----	-----
LONG TERM LIABILITIES		
Notes payable	210,000	225,466
	-----	-----
TOTAL LONG TERM LIABILITIES	210,000	225,466
	-----	-----
TOTAL LIABILITIES	2,401,546	2,002,610
	-----	-----
REDEEMABLE WARRANTS	748,500	748,500
	-----	-----
SHAREHOLDERS' EQUITY		
Common stock, authorized 500,000,000 shares of \$.001 par value	45,141	43,938

Edgar Filing: TSET INC - Form 10QSB

Capital in excess of par value	14,443,929	14,371,113
Deferred equity compensation	(26,044)	(41,668)
Retained earnings (Accumulated deficit)	(15,349,093)	(14,757,963)
	-----	-----
TOTAL SHAREHOLDERS' EQUITY	(886,067)	(384,579)
	-----	-----
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 2,263,979	\$ 2,366,531
	=====	=====

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

3

TSET, INC  
CONSOLIDATED STATEMENTS OF OPERATIONS

	FOR THE QUARTER ENDED SEPTEMBER		
	2002	2001	
	-----	-----	-----
Sales	\$ 108,617	\$ 25,014	\$
Cost of sales	92,125	10,014	
Gross Profit	----- 16,492	----- 15,000	-----
Selling, General and Administrative expenses			
Compensation and benefits	134,790	176,218	2
Research and development	30,274	90,191	
Professional services	284,076	644,817	
Depreciation and amortization	72,636	71,674	
Facilities	19,205	25,665	
Other selling general & administrative expenses	32,871	41,047	
Total Selling, General and Administrative expenses	----- 573,850	----- 1,049,612	5
Net Operating Income (Loss)	(557,358)	(1,034,612)	(5)
Other Income / (expense)	-	269	
Interest Expense	(33,773)	(18,292)	
Net Income (Loss) Before Taxes	----- (591,130)	----- (1,052,634)	(5)
Provision for Taxes	-	-	
Net Income (Loss) from continuing operations	(591,130)	(1,052,634)	(5)
Income (Loss) from discontinued operations,			

Edgar Filing: TSET INC - Form 10QSB

net of income tax of \$0	-	-	(3)
Net Income (Loss)	\$ (591,130)	\$ (1,052,634)	\$ (8)
Basic Earnings (Loss) Per Share			
Income (loss) from continuing operations	(0.01)	(0.03)	
Loss from discontinued operations	-	-	
Net Income (loss)	\$ (0.01)	\$ (0.03)	\$
Diluted Earnings (Loss) Per Share			
Income (loss) from continuing operations	(0.01)	(0.03)	
Loss from discontinued operations	-	-	
Net Income (loss)	\$ (0.01)	\$ (0.03)	\$

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

4

TSET, INC  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	FOR THE QUARTER ENDED SEPTEMBER	
	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
NET LOSS FROM CONTINUING OPERATIONS	\$ (591,130)	\$ (1,052,634)
ADJUSTMENTS TO RECONCILE NET LOSS TO NET CASH (USED IN) PROVIDED BY OPERATIONS		
Depreciation and amortization	72,636	71,674
Common stock issued for compensation/services	5,674	274,513
CHANGE IN		
Inventory Assets	-	-
Accounts receivable	(25,950)	-
Prepaid expenses and other assets	34,380	(97,427)
Accounts Payable	268,703	462,312
Accrued Expenses and other liabilities	119,201	(34,538)
NET CASH (USED IN) PROVIDED BY CONTINUING OPERATIONS	(116,486)	(376,100)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	-	-
Investment in patent protection	-	(36,740)
Investment in discontinued operations	-	82,545
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES	-	45,805

Edgar Filing: TSET INC - Form 10QSB

CASH FLOWS FROM FINANCING ACTIVITIES			
Issuance of common stock	183,000	80,000	1,
Proceeds from short-term borrowings		315,321	
Repayments of short-term borrowings	(88,001)	-	
NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES	----- 94,999	----- 395,321	----- 1,
NET (DECREASE) INCREASE IN CASH	(21,486)	65,026	
CASH			
BEGINNING OF PERIOD	21,510	32,619	
END OF PERIOD	----- \$ 24	----- \$ 97,645	----- \$
Supplemental schedule of non-cash investing and financing activities:			
Debt satisfied with stock	\$ -	\$ -	\$
	=====	=====	=====

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THIS FINANCIAL STATEMENT.

5

TSET, INC  
STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

	COMMON STOCK			
	-----			
	SHARES	AMOUNT	CAPITAL IN EXCESS OF PAR VALUE	RETA EAR (ACCU DEF
	-----	-----	-----	-----
BALANCE at June 30, 2002	43,937,907	\$ 43,938	\$ 14,371,113	\$ (14,7
Shares issued in July 2002 for cash	150,000	150	26,100	
Shares issued in August 2002 for cash	790,248	790	116,928	
Shares issued in September 2002 for cash	263,141	263	38,769	
Stock options granted at Sept 30, 2002 for consulting services			5,674	
Costs associated with equity financing			(114,655)	
Amortization of deferred equity compensation				
Net loss for the year ended June 30, 2002				(5
	-----	-----	-----	-----

Edgar Filing: TSET INC - Form 10QSB

BALANCE at September 30, 2002	45,141,296	\$ 45,141	\$ 14,443,929	\$ (15,3
	=====			

The accompanying notes are an integral part of this financial state

6

TSET, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)

NOTE 1 - ACCOUNTING MATTERS

The accompanying unaudited financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information. Accordingly, they do not include all the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments necessary to present fairly the information set forth therein have been included. Operating results for the three-month period ended September 30, 2002 are not necessarily indicative of the results that may be experienced for the fiscal year ending June 30, 2003.

These financial statements are those of the Company and its wholly-owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in the preparation of the consolidated financial statements. Aperion Audio, Inc. is disclosed as discontinued operations in these financial statements.

The accompanying financial statements should be read in conjunction with the TSET, Inc. Form 10-KSB for the fiscal year ended June 30, 2002 filed on September 28, 2002.

RECENT ACCOUNTING PRONOUNCEMENTS. On July 20, 2001, the FASB issued Statement of Financial Accounting Standard (SFAS) No. 142, "Goodwill and Other Intangible Assets." This statement makes significant changes to the accounting for business combinations, goodwill, and intangible assets.

SFAS No. 142 establishes new standards for goodwill acquired in a business combination, eliminates amortization of goodwill and instead sets forth methods to periodically evaluate goodwill for impairment. Intangible assets with a determinable useful life will continue to be amortized over that period. The Company adopted this statement during the quarter ending September 30, 2002. Goodwill and intangible assets acquired after June 30, 2001 will be subject immediately to the non-amortization and amortization provisions of the statement. The Company does not currently have any goodwill recorded on its financial statements and it is expected that there will be no immediate impact on the Company's financial statements as a result of the adoption of this statement.

In June 2001, the Financial Accounting Standards Board issued SFAS No. 143, "Accounting for Asset Retirement Obligations." This statement addresses the financial accounting and reporting for the retirement of tangible long-lived assets and the associated asset retirement costs. The Company believes the adoption of SFAS 143 will have no significant impact on its financial statements. This statement is effective for financial statements issued in fiscal years beginning after June 15, 2002.

In August 2001, the Financial Accounting Standards Board issued SFAS No. 144,

Edgar Filing: TSET INC - Form 10QSB

"Accounting for the Impairment or Disposal of Long-Lived Assets." This statement addresses the financial accounting and reporting for the impairment or disposal of long-lived assets. The Company believes the adoption of SFAS 144 will have no significant impact on its financial statements. This statement is effective for financial statements issued in fiscal years beginning after June 15, 2002.

In April 2002, the Financial Accounting Standards Board issued SFAS No. 145, "Recission of FASB Statements 4, 44, 64, Amendment of FASB Statement 13, and Technical Corrections." This Statement rescinds FASB Statement No. 4, REPORTING GAINS AND LOSSES FROM EXTINGUISHMENT OF DEBT, and an amendment of that Statement, FASB Statement No. 64, EXTINGUISHMENTS OF DEBT MADE TO SATISFY SINKING-FUND REQUIREMENTS. This Statement also rescinds FASB Statement No. 44, ACCOUNTING FOR INTANGIBLE ASSETS OF MOTOR CARRIERS. This Statement amends FASB Statement No. 13, ACCOUNTING FOR LEASES, to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. This Statement also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. The Company believes the adoption of SFAS 145 will have no significant impact on its financial statements. This statement is effective for financial statements issued on or after May 15, 2002.

In August 2002, the Financial Accounting Standards Board issued SFAS No. 146, "Accounting for Costs Associated with Exit, or Disposal Activities." This Statement addresses financial accounting and reporting for costs associated with exit or disposal activities. The Company believes the adoption of SFAS 145 will

7

have no significant impact on its financial statements. This statement is effective for exit or disposal activities initiated after December 31, 2002.

NOTE 2 -- INCOME TAXES

The composition of deferred tax assets and the related tax effects at September 30, 2002 and June 30, 2002 are as follows:

	SEPTEMBER 30, 2002 (UNAUDITED)	JUNE 30, 2002
	-----	-----
Benefit from carryforward of capital and net operating losses	\$2,872,231	\$2,685,915
Other temporary differences	220,332	220,332
Less:		
Valuation allowance	(3,052,963)	(2,906,247)
	-----	-----
Net deferred tax asset	\$ -	\$ -
	=====	=====

The other temporary differences shown above relate primarily to gain and loss on discontinued operations, impairment reserves for intangible assets, accrued expenses, and accrued and deferred compensation. The difference between the income tax benefit in the accompanying statements of operations and the amount that would result if the U.S. Federal statutory rate of 34% were applied to pre-tax loss is as follows:

SEPTEMBER 30, 2002

## Edgar Filing: TSET INC - Form 10QSB

	(UNAUDITED)		JUNE 30, 2002	
	AMOUNT	% OF PRE-TAX LOSS	AMOUNT	% OF PRE-TAX LOSS
Benefit for income tax at federal statutory rate	\$ 200,984	34.0%	\$ 946,620	34.0%
Benefit for income tax at state statutory rate	11,782	2.0%	55,494	2.0%
Non-deductible expenses	(26,445)	(4.5)%	(111,274)	(4.0)%
Acquired NOL and other	-	0.0%	248,489	8.9%
Increase in valuation allowance	(186,316)	(31.5)%	(1,139,325)	(40.9)%
	\$ -	0.0%	\$ -	0.0%
	=====	=====	=====	=====

The non-deductible expenses shown above related primarily to the amortization of intangible assets and to the accrual of stock options for compensation using different valuation methods for financial and tax reporting purposes.

The Company has filed all of its federal and state income tax returns for all years through June 30, 2001. The Company is current on all income tax filings. At September 30, 2002, for federal income tax and alternative minimum tax reporting purposes, the Company has approximately \$6.4 million of unused Federal net operating losses, \$1.0 million of capital losses and \$3.3 million of unused State net operating losses available for carryforward to future years. The benefit from carryforward of such losses will expire in various years between 2006 and 2022 and could be subject to limitations if significant ownership changes occur in the Company.

### NOTE 3 - SEGMENTS OF BUSINESS

The Company operates principally in one segment of business: The Kronos segment licenses, manufactures and distributes air movement and purification devices utilizing the Kronos™ technology. All other segments have been disposed of or discontinued. In the three months ended September 30, 2002, the Company operated only in the U.S.

8

### NOTE 4 - EARNINGS PER SHARE

Weighted average shares outstanding used in the earnings per share calculation were 44,526,735, 34,224,405, and 25,950,780 for the periods ended September 30, 2002, 2001, and 2000, respectively.

As of September 30, 2002, there were outstanding options to purchase 7,641,975 shares of the Company's common stock. These options have been excluded from the earnings per share calculation as their effect is anti-dilutive. As of September 30, 2001, there were outstanding options to purchase 1,557,075 shares of the Company's common stock. These options have been excluded from the earnings per share calculation as their effect is anti-dilutive.

### NOTE 5 - DISCONTINUED OPERATIONS

As of September 30, 2002, the Company had no discontinued operations. In early January 2001, management committed to a formal plan of action to sell or otherwise dispose of Atomic Soccer. Agreement was reached with a buyer group, that included current and former Atomic Soccer management, to sell them the



## Edgar Filing: TSET INC - Form 10QSB

outstanding shares of common stock of Atomic Soccer. The transaction was effective on April 11, 2001. On September 14, 2001 the board approved a formal plan of action to sell or otherwise dispose of Aperion Audio (formerly EdgeAudio). The Company accrued \$150,000 for anticipated operating losses during the phase-out period. At June 30, 2001, the Company recognized an impairment loss on the intangible asset related to its acquisition of Aperion Audio of \$2,294,000. The sale of TSET-owned shares of Aperion Audio common stock was completed on June 7, 2002, pursuant to a Settlement Agreement and Mutual Release. At June 30, 2001, the Company wrote down to \$0 the intangible asset associated with its investment in Aperion Audio creating a negative book value for this investment of approximately \$800,000. The sale will resulted in a gain of approximately \$682,000. For tax purposes, there was no write down in the Aperion Audio intangible asset, therefore, there will be no tax effect on this gain. As a result, both Atomic Soccer and Aperion are included in the financial statements as discontinued operations.

The Company's consolidated financial statements for all periods have been reclassified to report separately results of operations and operating cash flows from continuing operations and the discontinued operations. The net revenues are included in the financial statements under Net Income (Loss) from Discontinued Operations. Operating results of discontinued operations for the three-months ended September 30, are as follows:

### OPERATING RESULTS OF DISCONTINUED OPERATIONS:

OPERATING RESULTS OF DISCONTINUED OPERATIONS:				
-----				
FOR THE THREE MONTHS ENDED SEPTEMBER 30,				
-----				
	2001		2000	
	APERION AUDIO	ATOMIC	APERION AUDIO	TOTAL
	-----	-----	-----	-----
Sales	\$175,265	\$ 365,848	\$ 22,990	\$388,838
Cost of sales	(63,509)	(230,117)	(11,810)	(241,927)
Depreciation and amortization	(3,309)	(71,798)	(64,934)	(136,732)
General and administrative	(208,331)	(150,895)	(233,483)	(384,378)
	-----	-----	-----	-----
Operating income (loss)	(99,883)	(86,962)	(287,237)	(374,199)
Other income	5,090	-	-	-
Interest expense	(7,744)	(28,526)	(2,615)	(31,141)
Provision for future operating losses	82,030	-	-	-
Minority interest	20,507	-	44,984	44,984
	-----	-----	-----	-----
Income (Loss) pre-tax	0	(115,488)	(244,868)	(360,356)
Income taxes (benefits)	-	-	-	-
	-----	-----	-----	-----
Loss from discontinued operations	\$0	\$ (115,488)	\$ (244,868)	\$ (360,356)
	=====	=====	=====	=====

#### NOTE 6 - NOTES PAYABLE

The Company had the following obligations at September 30 and June 30, 2000:

## Edgar Filing: TSET INC - Form 10QSB

	September 30, 2002	June 30, 2002
	-----	-----
(1) Obligations to Fusion Capital	\$ 49,999	\$ 123,000
(2) Obligation to Aperion Audio	185,466	200,466
(3) Obligation to Jeff Wilson	360,000	360,000
(4) Eagle Rock	70,000	70,000
Obligations to stockholders	7,700	7,700
	-----	-----
Total Notes Payable	673,165	761,166
Current portions:		
Obligations to Fusion Capital	49,999	123,000
Obligation to Aperion Audio	185,466	205,000
Obligation to Jeff Wilson	150,000	130,000
Eagle Rock	70,000	70,000
Obligations to stockholders	7,700	7,700
	-----	-----
Total current portion	463,165	535,700
	-----	-----
Total long term obligations net of current portion	210,000	225,466
	=====	=====

- (1) This is a non-interest bearing demand obligation and is only outstanding until Fusion Capital purchases enough common stock from the Company to eliminate the advance position.
- (2) This is a non-interest bearing note with monthly payments of \$15,000.
- (3) This note is to a director of the Company and bears interest at 4.59%. The note calls for quarterly payments of \$20,000 until the principal and interest are paid in full.
- (4) This note bears interest at a rate of 12%. The payment terms are interest only with the principal due on March 1, 2003.

### NOTE 7 - CONSULTING AGREEMENTS

In July 2001, the Company signed a six-month agreement to utilize the strategic planning and business plan execution services of The Eagle Rock Group, LLC. The Eagle Rock Group will work with the Kronos Air Technologies team to fully develop and capitalize the Kronos(TM) technology.

Pursuant to the agreement that the Company entered into with The Eagle Rock Group, the Company issued to The Eagle Rock Group a ten-year warrant granting them the right to purchase 1,400,000 shares of the Company's common stock at an exercise price of \$0.68 per share. The warrants were immediately vested and non-forfeitable. The warrant was valued at \$686,000 using the Black-Scholes option valuation model and was initially recorded as deferred equity compensation and amortized into current period professional services expense at a rate of \$137,200 per month over the term of the agreement. Amortization for the year ended June 30, 2002 was \$686,000. The shares underlying the warrant have subscription rights in the event that the Company issues any rights to all of its stockholders to subscribe for shares of the Company's common stock. In addition, the warrant contains redemption rights in the event that the Company enters into a transaction that results in a change of control of the Company.

On October 1, 2001, the Company entered into a 15-month consulting agreement with Joshua B. Scheinfeld and Steven G. Martin, principals of Fusion Capital, for consulting services with respect to operations, executive employment issues, employee staffing, strategy, capital structure and other matters as specified from time to time. As consideration for their services, the Company issued

## Edgar Filing: TSET INC - Form 10QSB

360,000 shares of its common stock. In accordance with EITF 96-18, the measurement date was established as the contract date of October 1, 2001 as the share grant was non-forfeitable and fully vested on that date. The stock was valued on that date at \$0.28 a share (the closing price for the Company's common stock on the measurement date). The stock issuance has been recorded as a prepaid consulting fee and is being amortized to Professional Fee Expense ratably over the 15 month term of the contract.

10

On March 1, 2002, the Company entered into a 12-month consulting agreement with The Eagle Rock Group. Pursuant to the agreement, the Company issued a note for the outstanding balance of \$120,000 due to The Eagle Rock Group. The note is due on March 1, 2003 and bears interest at the rate of 12% per annum. The Company also granted The Eagle Rock Group a 10 year warrant for up to 2,000,000 shares. The warrant contains redemption rights in the event that the Company enters into a transaction that results in a change of control of the Company. Of this, 500,000 shares will be earned over a period of 12 months. The exercise price of the initial 500,000 warrants is \$0.42 for 250,000 warrants and \$0.205 (the closing price of the Company's common stock on March 1, 2002) for 250,000 warrants. These warrants are irrevocable and are fully vested. The measurement date is March 1, 2002 as the warrants are fully vested and non-forfeitable on that date. The value assigned to these warrants is \$62,500 and was determined using the Black-Scholes option valuation model. The 500,000 warrants are for general consulting services for a 12 month period. The \$62,500 will be expensed ratably over the term of the consulting contract. The remainder of the shares may be earned contingent upon the occurrence of various events including a successful capital raise equal to or greater than \$1.5 million, securing contracts with the U.S. military, securing contracts with consumer-oriented distribution organizations, and the adoption of a branding/marketing campaign which has been principally developed by The Eagle Rock Group. The remaining potential 1,500,000 shares covered by the warrant will be valued if and when earned under the terms of the contract. The exercise price for the remaining shares will be the market price on the date the grant is earned.

### NOTE 8 - SUBSEQUENT EVENTS

In October 2002, the Company received a Notice of Allowance from the United States Patent and Trademark Office indicating that its application entitled Electrostatic Fluid Accelerator has been examined and allowed for issuance as a U.S. patent. It is expected that the patent will issue in due course, providing protection for key aspects of Kronos' technology until late in 2019. A number of corresponding applications have been filed and are pending outside of the United States. Kronos' Chief Technology Officer, Dr. Igor Krichtafovitch, is the lead inventor of this proprietary technology.

In October 2002, Kronos Air Technologies, Inc., and HoMedics USA, Inc. executed a multiyear, multi-million-dollar Licensing Agreement to bring Kronos(TM) proprietary technology to the consumer. The agreement provides for exclusive North American, Australian and New Zealand retail distribution rights for next generation consumer air movement and purification products based on patented KronosTM technology.

The initial term of the agreement is three and one half years with the option to extend the agreement for six additional years. Kronos will be compensated through an initial royalty payment and ongoing quarterly royalty payments based on a percentage of sales. HoMedics will pay minimum royalty payments of at least \$2 million during the initial term and on-going royalty payments to extend the agreement. Kronos will retain full rights to all of its intellectual property.

In November 2002, Kronos Air Technologies, Inc. and the United States Navy

## Edgar Filing: TSET INC - Form 10QSB

executed a Small Business Innovation Research Phase II contract to develop and demonstrate an advanced distributive air management system based on the patented Kronos(TM) technology. The 24-month contract is worth \$585,000 with an option for an additional \$144,000 in funding.

This Phase II contract is an extension of the Phase I and Phase I Option work that began last year and represents further validation of the Kronos(TM) technology by the U.S. Department of Defense. The work and funding on Phase II will begin immediately. During Phase II, Kronos shall develop and demonstrate a set of fully controlled devices that represent a "cell" of an advanced distributive air management system with medium capacity airflow in a U.S. Navy unique environment. The "cell" will be designed to be easily adjustable to a variety of applications, such as duct size, airflow requirements, and air quality. The goal of this development work is to significantly reduce or replace altogether the current HVAC air handling systems on naval ships.

### NOTE 9 - REALIZATION OF ASSETS

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplate continuation of the Company as a going concern. The Company has sustained losses from operations in recent years, and such losses have continued through the current year ended June 30, 2002. In addition, the Company has used, rather than provided cash in its operations. The Company is currently using its resources to raise capital necessary to complete research and development work, and to provide for its working capital needs.

In view of the matters described in the preceding paragraph, recoverability of a major portion of the asset amounts shown in the accompanying balance sheet is dependent upon continued operations of the Company, which in turn is dependent upon the Company's ability to meet its financing requirements on a continuing basis, to maintain present financing and to succeed in its future operations.

11

The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts and classification of liabilities that might be necessary should the Company be unable to continue in existence.

Management has taken the following steps with respect to its operating and financial requirements, which it believes are sufficient to provide the Company with the ability to continue in existence:

1. In May 2001, Kronos Air Technologies was awarded a Small Business Innovation Research contract. This contract is sponsored by the United States Navy and is potentially worth up to \$816,000 in product development and testing support for Kronos Air Technologies. The first phase of the contract was worth up to \$87,000 in funding for manufacturing and testing a prototype device for air movement and ventilation onboard naval vessels. In April 2002, the U.S. Navy and Kronos mutually agreed to exercise the option on the first phase of the U.S. Navy SBIR contract. The option was to provide incremental funding to Kronos to further test and evaluate Kronos(TM) devices built during the initial SBIR funding. Testing included demonstrating the ability of these U.S. Navy Kronos(TM) devices to capture and destroy biological hazards and to effectively manage

## Edgar Filing: TSET INC - Form 10QSB

electrical magnetic interference. In November 2002, Kronos Air Technologies, Inc. and the United States Navy executed a Small Business Innovation Research Phase II contract to develop and demonstrate an advanced distributive air management system based on the patented Kronos(TM) technology. The 24-month contract is worth \$585,000 with an option for an additional \$144,000 in funding.

2. In December 2001, Kronos Air Technologies was awarded an SBIR contract sponsored by the U.S. Army. This contract is potentially worth up to \$850,000 in product development and testing support for Kronos Air Technologies. Phase One of the contract is worth up to \$120,000 in funding to investigate and analyze the feasibility of the Kronos(TM) technology to reduce humidity in heating, ventilation and air conditioning (HVAC) systems. Dehumidification is essential to making HVAC systems more energy efficient. Phase Two of the contract is worth up to \$730,000 in additional funding for product development and testing. We are currently under contract for and working on phase One. In August 2002, the U.S. Army requested the company resubmit a detailed Phase Two proposal for review in 2003.
3. On July 2, 2001, we signed a six month agreement to utilize the strategic planning and business plan execution services of The Eagle Rock Group, LLC. The Eagle Rock Group will work with the Kronos Air Technologies team to fully develop and capitalize on the Kronos(TM) technology. We believe that The Eagle Rock Group can assist us in unlocking the potential value of the Kronos(TM) technology. The Eagle Rock Group's multi-disciplined approach, which uses seasoned business executives and leverages relationships and networks, can accelerate the Kronos(TM) opportunity versus the timing and development if we were to continue on a go-it-alone strategy or if we were to work and coordinate with the myriad of groups necessary to duplicate The Eagle Rock Group team. Specifically, The Eagle Rock Group is working to augment and enhance our efforts in the following areas (i) capital raising and allocation, (ii) strategic partner introduction and evaluation, (iii) distribution channel development, (iv) product focus and brand development, (v) human resource placement, and (vi) capital market introduction and awareness. Pursuant to the agreement that we entered into with The Eagle Rock Group, we issued to The Eagle Rock Group a ten-year warrant granting them the right to purchase 1,400,000 shares of our common stock at an exercise price of \$0.68 per share. The shares underlying the warrant have piggy-back and demand registration rights, as well as subscription rights in the event that we issue any rights to all of our stockholders to subscribe for shares of our common stock. In addition, the warrant contains redemption

## Edgar Filing: TSET INC - Form 10QSB

rights in the event that we enter into a transaction that results in a change of control of our company.

4. On March 1, 2002, the Company entered into a 12-month consulting agreement with The Eagle Rock Group. Pursuant to the agreement, the Company granted The Eagle Rock Group a 10 year warrant for up to 2,000,000 shares of our common stock. Of this, 500,000 shares will be earned over a period of 12 months. The 500,000 warrants are for general consulting services for a 12 month period. The remainder of the warrants may be earned contingent upon the occurrence of various events including a successful capital raise equal to or greater than \$1.5 million, securing contracts with the U.S. military, securing contracts with consumer-oriented distribution organizations, and the adoption of a branding/marketing campaign which has been principally developed by The Eagle Rock Group.
5. On May 7, 2002, we completed a private placement of our common stock pursuant to which we sold 1,971,176 shares of our common stock at \$0.17 per share to seven accredited investors for consideration of \$335,100 cash and 1,429,695 shares of our common stock at \$0.17 per share to six members of our management team for consideration of \$39,987 cash and commitments to convert \$203,061 of debt.
6. In July 2002, Kronos Air Technologies executed a Memorandum of Understanding with Access Business Group International L.L.C. for the production of a limited number of Kronos(TM) devices and for the potential licensing of Kronos(TM) based air movement and treatment technologies. Access Business Group is the product development, manufacturing and logistics subsidiary of Alticor Inc. and an affiliate of the Amway Corporation and Quixtar Inc. Under the proposed arrangement, Kronos will retain full rights to all of our intellectual property, as well as manufacturing of our proprietary power-supply. The final agreement is subject to negotiations between the parties.
7. During our year ended June 30, 2002, we sold 5,059,752 shares of our common stock to Fusion Capital for \$1,194,608 under the terms of a Common Stock Purchase Agreement dated June 19, 2001. On August 12, 2002, we entered into a new Common Stock Purchase Agreement with Fusion.
8. In October 2002, Kronos Air Technologies, Inc., and HoMedics USA, Inc. executed a multiyear, multi-million-dollar Licensing Agreement to bring Kronos(TM) proprietary technology to the consumer. The agreement provides for exclusive North American, Australian and New Zealand retail distribution rights for next generation consumer air movement and purification products based on patented Kronos(TM) technology. The initial term of the agreement is three and one half years with the option to extend the agreement for six additional years. Kronos will be compensated through an initial royalty payment and ongoing quarterly royalty payments based on a

## Edgar Filing: TSET INC - Form 10QSB

percentage of sales. HoMedics will pay minimum royalty payments of at least \$2 million during the initial term and on-going royalty payments to extend the agreement. Kronos will retain full rights to all of its intellectual property.

### NOTE 10 - COMMITMENTS AND CONTINGENCIES

LITIGATION. On June 6, 2002, Dutchess Advisors Ltd. initiated legal proceedings in Middlesex County, Massachusetts, against TSET. The complaint alleges, among other things, breach of contract, QUANTUM MERUIT, unjust enrichment and conversion with respect to a letter agreement, dated June 19, 2001, between TSET and Dutchess Advisors Ltd., and seeks, among other things, a judgment in the amount of \$75,000, exclusive of pre-judgment interest, costs and attorneys' costs. TSET contested the allegations made by Dutchess by serving a motion to dismiss all claims. Dutchess subsequently filed an amended complaint with the court on August 16, 2002. Dutchess seeks to recover up to three times its actual damages as well as its costs and attorneys' fees. TSET filed a motion

13

to dismiss all counts in the amended complaint. TSET believes that it has meritorious defenses and intends to vigorously defend this matter.

On February 2, 2001, we initiated, together with Kronos Air Technologies, legal proceedings in Clackamas County, Oregon against W. Alan Thompson, Ingrid T. Fuhriman, and Robert L. Fuhriman II, each of whom were formerly executive officers and members of the Board of Directors of Kronos Air Technologies. This suit alleges, among other things, breach of fiduciary duties and breach of contract by these individuals, and seeks, among other things, an order from the court referring the dispute to arbitration in accordance with the terms of these individuals. We have agreed to a change of venue of this matter to King County, Washington, and arbitrators have been selected. The parties are in the process of exchanging and complying with requests for discovery.

14

### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### INTRODUCTORY STATEMENTS

#### FORWARD-LOOKING STATEMENTS AND ASSOCIATED RISKS

This filing contains forward-looking statements, including statements regarding, among other things: (a) the growth strategies of TSET, Inc., d/b/a Kronos Advanced Technologies (the "Company" or "Kronos"); (b) anticipated trends in our Company's industry; (c) our Company's future financing plans; and (d) our Company's ability to obtain financing and continue operations. In addition, when used in this filing, the words "believes," "anticipates," "intends," "in anticipation of," and similar words are intended to identify certain forward-looking statements. These forward-looking statements are based largely on our Company's expectations and are subject to a number of risks and

## Edgar Filing: TSET INC - Form 10QSB

uncertainties, many of which are beyond our Company's control. Actual results could differ materially from these forward-looking statements as a result of changes in trends in the economy and our Company's industry, reductions in the availability of financing and other factors. In light of these risks and uncertainties, there can be no assurance that the forward-looking statements contained in this filing will in fact occur. Our Company does not undertake any obligation to publicly release the results of any revision to these forward-looking statements that may be made to reflect any future events or circumstances.

### GENERAL

TSET, Inc., through its wholly subsidiary, Kronos Air Technologies, Inc., is focused on the development and commercialization of an air movement and purification technology known as Kronos(TM) that is more fully described below. The Kronos(TM) technology operates through the application of high-voltage management across paired electrical grids that creates an ion exchange which moves air and gases at high velocities while removing odors, smoke, and particulates, as well as killing pathogens, including bacteria. We believe the technology is cost-effective and is more energy-efficient than current alternative fan and filter technologies. The Kronos(TM) technology has been patented by the United States Patent and Trademark Office. The Kronos(TM) technology has been patented by the United States Patent and Trademark Office. Additional U.S. and international patents are pending.

The Kronos(TM) device is comprised of state-of-the-art high-voltage electronics and electrodes attached to one or more sets of corona and target electrodes housed in a self-contained casing. The device can be flexible in size, shape and capacity and can be used in embedded electronic devices, standalone room devices, and integrated HVAC and industrial applications. The Kronos(TM) device has no moving parts or degrading elements and is composed of cost-effective, commercially available components.

The Kronos(TM) technology combines the benefits of silent air movement, air cleaning, and odor removal. Because the Kronos(TM) air movement system is a silent, non-turbulent, and energy-efficient air movement and cleaning system, we believe that it is ideal for air circulation, cleaning and odor removal in all types of buildings as well as compact, sealed environments such as airplanes, submarines and cleanrooms. Additionally, because it has no moving parts or fans, a Kronos(TM) device can instantly block or reverse the flow of air between adjacent areas for safety in hazardous or extreme circumstances.

On January 18, 2002, we began trading shares of our common stock under a new ticker symbol (KNOS). At the same time, we announced that our company will be doing business under the name of Kronos Advanced Technologies. We have asked our shareholders to vote for the approval of an amendment to our articles of incorporation for a name change of our company to Kronos Advanced Technologies, Inc. At our annual meeting on November 20, 2002.

**PATENT AND INTELLECTUAL PROPERTY.** In October 2002, Kronos received a Notice of Allowance from the United States Patent and Trademark Office indicating that its application entitled Electrostatic Fluid Accelerator has been examined and allowed for issuance as a U.S. patent. It is expected that the patent will issue in due course, providing protection for key aspects of Kronos' technology until late in 2019. A number of corresponding applications have been filed and are pending outside of the United States. Kronos' Chief Technology Officer, Dr. Igor Krichtafovitch, is the lead inventor of this proprietary technology.



## Edgar Filing: TSET INC - Form 10QSB

This allowance is for the first of a series of patent applications now pending with the U.S. Patent and Trademark Office addressing various aspects of the Kronos' platform. In addition to the Electrostatic Fluid Accelerator patent application, three additional patent applications have been filed for, among other things, the control and management of Electrostatic Fluid Acceleration. These additional patent applications are awaiting examination by the Patent Office. Each of these patent applications is directed towards Kronos' innovative technology used to move, control and filter air electronically, without the use of fans or moving parts.

Kronos(TM) device can be either used as a standalone product or can be embedded. Standalone products are self-contained; the user would simply need to plug the Kronos device into a wall outlet to obtain air filtration for their home, office or hotel room. Embedded applications of the Kronos technology require the technology be added into another device or become part of a larger system such as a piece of medical equipment to replace the cooling fan or building ventilation system for more efficient air movement and filtration.

### STANDALONE PLATFORM.

HOMEDICS CONTRACT. In October 2002, Kronos Air Technologies, Inc., and HoMedics USA, Inc. executed a multiyear, multi-million-dollar Licensing Agreement to bring the Kronos(TM) proprietary technology to the consumer. The agreement provides for exclusive North American, Australian and New Zealand retail distribution rights for next generation consumer air movement and purification products based on patented Kronos(TM) technology.

The initial term of the agreement is three and one half years with the option to extend the agreement for six additional years. Kronos will be compensated through an initial royalty payment and ongoing quarterly royalty payments based on a percentage of sales. HoMedics will pay minimum royalty payments of at least \$2 million during the initial term and on-going royalty payments to extend the agreement. Kronos will retain full rights to all of its intellectual property.

HoMedics commitment includes a multi-million-dollar marketing and advertising campaign to promote the Kronos(TM)-based product line. The products will be manufactured and distributed by HoMedics. HoMedics currently distributes their products through major domestic retailers, including Wal-Mart, Home Depot, Sears, Bed Bath & Beyond, and Linens 'N Things. Kronos will manufacture and provide HoMedics with Kronos' proprietary electronics.

### EMBEDDED PLATFORM

U.S. NAVY SBIR CONTRACTS. The U.S. Department of Defense and Department of Energy have provided Kronos Air Technologies with various grants and contracts to develop, test and evaluate the Kronos(TM) technology for embedded applications. Since May 2001, the total potential value of Small Business Innovation Research (SBIR) contracts awarded to Kronos Air Technologies has been \$1.7 million. In May 2001, Kronos Air Technologies was awarded its first SBIR contract sponsored by the U.S. Navy. That contract is potentially worth \$816,000 in product development and testing support. The first phase of the contract was worth up to \$87,000 in funding for manufacturing and testing prototype devices for air movement and ventilation onboard naval vessels. The second phase of the contract is worth up to \$729,000 in additional funding.

In April 2002, the U.S. Navy and Kronos mutually agreed to exercise the option on the first phase of the U.S. Navy SBIR contract. The option is to provide incremental funding to Kronos to further test and evaluate the Kronos(TM) devices built during the initial SBIR funding. Testing will include demonstrating the ability of these U.S. Navy Kronos(TM) devices to capture and

## Edgar Filing: TSET INC - Form 10QSB

destroy biological hazards and to effectively manage electrical magnetic interference ("EMI").

In November 2002, Kronos Air Technologies, Inc. and the United States Navy executed a Small Business Innovation Research Phase II contract to develop and demonstrate an advanced distributive air management system based on the patented Kronos(TM) technology. The 24-month contract is worth \$585,000 with an option for an additional \$144,000 in funding.

This Phase II contract is an extension of the Phase I and Phase I Option work that began last year and represents further validation of the Kronos(TM) technology by the U.S. Department of Defense. The work and funding on Phase II will begin immediately. During Phase II, Kronos shall develop and demonstrate a set of fully controlled devices that represent a "cell" of an advanced distributive air management system with medium capacity airflow in a U.S. Navy unique environment. The "cell" will be designed to be easily adjustable to a variety of applications such as duct size, airflow requirements, and air quality. The goal of this development work is to significantly reduce or replace altogether the current HVAC air handling systems on naval ships.

As part of its air management system, Kronos will develop and test an air filtration mechanism capable of performing to HEPA quality standards. Kronos(TM) devices will replace all current HEPA filters with a permanent, easily cleaned, low-cost solution. The U.S. Navy unique environment includes shock exposure, vibration, Electromagnetic Interference/Compatibility (EMI/EMC), and salt spray. Kronos(TM) devices will be tested and built to meet specific Navy standards. Testing shall include assessments for system performance, including control techniques, noise levels, acquisition and lifecycle costs.

During the option portion of the contract, Kronos(TM) technology's ability to kill bacteria and other pathogens will be confirmed and expanded to a wide range of pathogens for space disinfection and bio-terrorist attacks. A unique ability of the Kronos(TM) technology is to kill all or almost all airborne pathogens regardless of their nature, genetic structure, robustness, or method of delivery.

U.S. ARMY SBIR CONTRACT. In December 2001, Kronos Air Technologies was awarded an SBIR contract sponsored by the U.S. Army. This contract is potentially worth up to \$850,000 in product development and testing support for Kronos Air Technologies. Phase One of the contract is worth up to \$120,000 in funding to investigate and analyze the feasibility of the Kronos(TM) technology to reduce humidity in heating, ventilation and air conditioning (HVAC) systems. Dehumidification is essential to making HVAC systems more energy efficient. Phase Two of the contract is worth up to \$730,000 in additional funding for

16

product development and testing. In August 2002, the U.S. Army requested the Company resubmit a detailed Phase Two proposal for review in 2003.

### CRITICAL ACCOUNTING POLICIES

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

ALLOWANCE FOR DOUBTFUL ACCOUNTS. We provide a reserve against our

## Edgar Filing: TSET INC - Form 10QSB

receivables for estimated losses that may result from our customers' inability to pay. These reserves are based on potential uncollectible accounts, aged receivables, historical losses and our customers' credit-worthiness. Should a customer's account become past due, we generally will place a hold on the account and discontinue further shipments and/or services provided to that customer, minimizing further risk of loss.

VALUATION OF GOODWILL, INTANGIBLE AND OTHER LONG-LIVED ASSETS. We use assumptions in establishing the carrying value, fair value and estimated lives of our long-lived assets and goodwill. The criteria used for these evaluations include management's estimate of the asset's ability to generate positive income from operations and positive cash flow in future periods compared to the carrying value of the asset, the strategic significance of any identifiable intangible asset in our business objectives, as well as the market capitalization of TSET. We have used certain key assumptions in building the cash flow projections required for evaluating the recoverability of our intangible assets. We have assumed revenues from the following applications of the Kronos technology: consumer stand-alone devices, assisted care/skilled nursing stand-alone devices, embedded devices in the hospitality industry and in specialized military applications. Expenses/cash out flows in our projections include sales and marketing, production, distribution, general and administrative expenses, research and development expenses and capital expenditures. These expenses are based on management estimates and have been compared with industry norms (relative to sales) to determine their reasonableness. We use the same key assumptions for our cash flow evaluation as we do for internal budgeting, lenders and other third parties, therefore, they are internally and externally consistent with financial statement and other public and private disclosures. We are not aware of any negative implications resulting from the projections used for purposes of evaluating the appropriateness of the carrying value of these assets. If assets are considered to be impaired, the impairment recognized is the amount by which the carrying value of the assets exceeds the fair value of the assets. Useful lives and related amortization or depreciation expense are based on our estimate of the period that the assets will generate revenues or otherwise be used by TSET. Factors that would influence the likelihood of a material change in our reported results include significant changes in the asset's ability to generate positive

17

cash flow, loss of legal ownership or title to the asset, a significant decline in the economic and competitive environment on which the asset depends, significant changes in our strategic business objectives, and utilization of the asset.

VALUATION OF DEFERRED INCOME TAXES. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized. The likelihood of a material change in our expected realization of these assets is dependent on future taxable income, our ability to deduct tax loss carryforwards against future taxable income, the effectiveness of our tax planning and strategies among the various tax jurisdictions that we operate in, and any significant changes in the tax treatment received on our business combinations.

ESTIMATED LOSSES FROM DISCONTINUED OPERATIONS. We provided for an accrual for the estimated loss on our discontinued Aperion Audio business based upon management's estimates of the estimated operating losses to be incurred by Aperion Audio from the date we adopted our plan to dispose of Aperion Audio in September 2001, through the ultimate disposal date, as well as estimated cost related to the disposal.

REVENUE RECOGNITION. We recognize revenue in accordance with SAB 101.

## Edgar Filing: TSET INC - Form 10QSB

Further, Kronos Air Technologies recognizes revenue on the sale of custom-designed contract sales under the percentage-of-completion method of accounting in the ratio that costs incurred to date bear to estimated total costs. For uncompleted contracts where costs and estimated profits exceed billings, the net amount is included as an asset in the balance sheet. For uncompleted contracts where billings exceed costs and estimated profits, the net amount is included as a liability in the balance sheet. Revenue from government grants for research and development purposes is recognized as revenue when received. Sales are reported net of applicable cash discounts and allowances for returns.

### RESULTS OF OPERATIONS

The Company's net loss from continuing operations for the three months ended September 30, 2002 was \$0.6 million, compared with a net loss of \$1.1 million for the corresponding period for the prior year. The decrease in the net loss was primarily the result of a reduction in professional fees and consulting services and a reduction in compensation expense.

**REVENUE.** Revenues are generated through sales of Kronos(TM) devices at Kronos Air Technologies, Inc. Revenue for the three months ended September 30, 2002 was \$109,000. Revenue of \$25,000 was recorded during the corresponding period of the prior year. These revenues were primarily from our U.S. Navy and U.S. Army Small Business Innovative Research contracts and from our contract with Access Business Group.

**COST OF SALES.** Cost of sales for the three months ended September 30, 2002 was \$92,000, compared to \$10,000 for the corresponding period in the prior year. Cost of sales is primarily research and development costs associated with our U.S. Navy and U.S. Army Small Business Innovative Research contracts and from our contract with Access Business Group.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES.** Selling, General and Administrative expenses for the three months ended September 30, 2002 was \$0.6 million, compared to \$1.0 million for the corresponding period in the prior year. The decrease is attributable to a reduction in professional fees and consulting services of \$360,000 and a reduction in compensation expenses of \$40,000.

### CONSOLIDATED BALANCE SHEET AS OF SEPTEMBER 30, 2002

Our total assets at September 30, 2002 were \$2.3 million, compared with \$2.4 million at June 30, 2002. Total assets at September 30, 2002 were comprised primarily of \$2.1 million of patents/intellectual property. Total assets at June 30, 2002 were comprised primarily of \$2.2 million of patents/intellectual property. Total current assets at September 30, 2002 and June 30, 2002 were \$93,000 and \$123,000, respectively, while total current liabilities for those same periods were \$2.2 million and \$1.8 million, respectively, creating a working capital deficit of \$2.1 million and \$1.7 million at each respective period end. This working capital deficit is primarily due to accrued expenses for compensation, management consulting and other professional services. Shareholders' equity as of September 30, 2002 and June 30, 2002 were \$(0.9) million and \$(0.4) million, respectively, representing a decrease of \$0.5 million. The decrease in shareholders' equity is primarily the result of incurring a \$0.6 million loss from continuing operations for the three months ended September 30, 2002, partially offset through the sale and issuance of \$.02 million of common stock.

### LIQUIDITY AND CAPITAL RESOURCES

## Edgar Filing: TSET INC - Form 10QSB

Historically we have relied principally on the sale of common stock to finance our operations. We have recently signed a multi-million dollar, multi-year licensing agreement with HoMedics as well as a Small Business Innovative Research Phase II contract with the U.S. Navy. Going forward, in addition to continued sales of common stock, we plan to rely on the proceeds from Small Business Innovation Research (SBIR) contracts with the U.S. Navy and Army, as well as other government contracts and grants, and cash flow generated from the sale of Kronos(TM) devices and the execution of licensing agreements and other contracts with commercial customers. We have also entered into a common stock purchase agreement with Fusion Capital under which we have the right, subject to certain conditions, to draw down approximately \$10,000 per day from the sale of common stock to Fusion Capital.

Net cash flow used on operating activities was \$0.1 million for the current year three months. We were able to satisfy our cash requirements for this period through the issuance and sale of our common stock as well as from revenue on our U.S Army and Navy SBIR contracts and our contract with Access Business Group.

In May 2002, we completed a private placement of our common stock pursuant to which we sold 2,559,412 shares of our common stock at \$0.17 per share to eight accredited investors for consideration of \$435,100 in cash and 841,459 shares of our common stock at \$0.17 per share to five members of our management team for consideration of commitments to convert \$143,048 of debt.

In July 2002, we entered into a Memorandum of understanding with Access Business Group under the terms of which we were to provide them with three working prototype Kronos(TM) devices for testing and evaluation for \$45,000.

On August 12, 2002, we entered into a common stock purchase agreement with Fusion Capital. Pursuant to the common stock purchase agreement, Fusion Capital has agreed to purchase on each trading day during the term of the agreement, \$10,000 of our common stock or an aggregate of \$6.0 million. The \$6.0 million of our common stock is to be purchased over a 30-month period, subject to a six-month extension or earlier termination at our sole discretion and subject to certain events. The purchase price of the shares of common stock will be equal to the lesser of (i) the lowest price of our common stock on the purchase date; or (ii) the average of the three (3) lowest closing sale prices of our common stock during the twelve (12) consecutive trading days prior to the date of a purchase by Fusion Capital. However, there can be no assurance of how much cash we will receive, if any, under the common stock purchase agreement with Fusion Capital.

In October 2002, Kronos Air Technologies, Inc., and HoMedics USA, Inc. executed a multiyear, multi-million-dollar Licensing Agreement to bring Kronos(TM) proprietary technology to the consumer. The initial term of the agreement is three and one half years with the option to extend the agreement for six additional years. Kronos has been compensated through an initial royalty payment and will receive ongoing quarterly royalty payments based on a percentage of sales. HoMedics will pay minimum royalty payments of at least \$2 million during the initial term and on-going royalty payments to extend the agreement. Kronos and HoMedics have agreed to execute a Development Agreement to provide additional funding to Kronos for the development of unique Kronos-based products that will be marketed and distributed by HoMedics. HoMedics has made a multi-million dollar commitment to the marketing and advertising of their Kronos product line over the initial 42 months of the agreement.

In November 2002, Kronos Air Technologies, Inc. and the United States Navy executed a Small Business Innovation Research Phase II contract to develop and demonstrate an advanced distributive air management system based on the patented Kronos(TM) technology. The 24-month contract is worth \$585,000 with an option

## Edgar Filing: TSET INC - Form 10QSB

for an additional \$144,000 in funding. Funding on Phase II will begin in December 2002.

### GOING CONCERN OPINION

Our independent auditors have added an explanatory paragraph to their audit opinion issued in connection with the 2002, 2001 and 2000 financial statements that states that we do not have significant cash or other material assets to cover our operating costs. Our ability to obtain additional funding will largely determine our ability to continue in business. Accordingly, there is substantial doubt about our ability to continue as a going concern. Our financial statements do not include any adjustments that might result from the outcome of this uncertainty.

We can make no assurance that we will be able to successfully transition from research and development to manufacturing and selling commercial products on a broad basis. While attempting to make this transition, we will be subject to all the risks inherent in a growing venture, including, but not limited to, the need to develop and manufacture reliable and effective products, develop marketing expertise and expand our sales force.

19

### CERTAIN RISK FACTORS

Our Company is subject to various risks which may materially harm our business, financial condition and results of operations. Certain risks are discussed below.

WE HAVE A LIMITED OPERATING HISTORY WITH SIGNIFICANT LOSSES AND EXPECT LOSSES TO CONTINUE FOR THE FORESEEABLE FUTURE

We have only recently begun implementing our plan to prioritize and concentrate our management and financial resources to fully capitalize on our investment in Kronos Air Technologies and have yet to establish any history of profitable operations. We incurred a net operating loss of \$0.6 million for the three months ended September 30, 2002. We have incurred net losses from continuing operations of \$3.5 million and \$3.6 million for the fiscal years ended June 30, 2002 and 2001. We have incurred annual operating losses of \$2.8 million, \$9.9 million and \$2.0 million, respectively, during the past three fiscal years of operation. As a result, at September 30, 2002 and June 30, 2002, we had an accumulated deficit of \$15.3 million and \$14.8 million, respectively. Our revenues have not been sufficient to sustain our operations. We expect that our revenues will not be sufficient to sustain our operations for the foreseeable future. Our profitability will require the successful commercialization of our Kronos(TM) technology. No assurances can be given when this will occur or that we will ever be profitable.

WE HAVE BEEN SUBJECT TO A GOING CONCERN OPINION FROM OUR INDEPENDENT AUDITORS

Our independent auditors have added an explanatory paragraph to their audit opinion issued in connection with the financial statements for the years ended June 30, 2002 and June 30, 2001 relative to our ability to continue as a going concern. Our ability to obtain additional funding will determine our ability to continue as a going concern. Our financial statements do not include any adjustments that might result from the outcome of this uncertainty.

WE WILL REQUIRE ADDITIONAL FINANCING TO SUSTAIN OUR OPERATIONS AND WITHOUT IT WE WILL NOT BE ABLE TO CONTINUE OPERATIONS

At September 30, 2002, we had a working capital deficit of \$2.1 million.

## Edgar Filing: TSET INC - Form 10QSB

At June 30, 2002, we had a working capital deficit of \$1.7 million. The independent auditor's report for the years ended June 30, 2002 and June 30, 2001, includes an explanatory paragraph to their audit opinion stating that our recurring losses from operations and working capital deficiency raise substantial doubt about our ability to continue as a going concern. For the years ended 2002, 2001 and 2000, we had an operating cash flow deficit of \$1.5 million, \$1.6 million and \$0.3 million, respectively. We do not currently have sufficient financial resources to fund our operations or pay certain existing obligations or those of our subsidiary. Therefore, we need additional funds to continue these operations and pay certain existing obligations.

Subject to the condition that Fusion Capital is not obligated and will not be permitted to purchase shares of our common stock if the per-share price of our common stock is below the floor price of \$0.10, we have the right to receive \$10,000 per trading day under the common stock purchase agreement unless our stock price equals or exceeds \$3.00, in which case the daily amount may be increased at our option. The extent to which we rely on Fusion Capital as a source of funding will depend on a number of factors including, the prevailing market price of our common stock and the extent to which we are able to secure working capital from other sources, such as through the sale of our Kronos((TM)) air movement and purification systems. If obtaining sufficient financing from Fusion Capital were to prove prohibitively expensive and if we are unable to commercialize and sell the products or technologies of our subsidiaries, we will need to secure another source of funding in order to satisfy our working capital needs. Even if we are able to access the funds available under the common stock purchase agreement, we may still need additional capital to fully implement our business, operating and development plans. Should the financing we require to sustain our working capital needs be unavailable, or prohibitively expensive when we require it, we would be forced to curtail our business operations. Additional financing could be prohibitively expensive due to the recent economic downturn in the U.S. economy and the possibility of reduced investor confidence generally in the financial markets and in emerging growth and technology companies. In addition, additional financing could be prohibitively expensive because (i) we have limited assets that have value to pledge as collateral; (ii) we have negative cash flows with

20

an accumulated deficit; and (iii) and we currently have no definitive contractual revenue stream from any customers.

THE SALE OF OUR COMMON STOCK TO FUSION CAPITAL MAY CAUSE DILUTION AND THE SALE OF THE SHARES OF COMMON STOCK ACQUIRED BY FUSION CAPITAL COULD CAUSE THE PRICE OF OUR COMMON STOCK TO DECLINE

The purchase price for the common stock to be issued to Fusion Capital pursuant to the common stock purchase agreement will fluctuate based on the price of our common stock. All shares issued to Fusion Capital will be freely tradable. Fusion Capital may sell none, some or all of the shares of common stock purchased from us at any time. We expect that the shares sold to Fusion Capital will be sold over a period of up to 30 months from the date of the common stock purchase agreement. Depending upon market liquidity at the time, a sale of shares by Fusion Capital at any given time could cause the trading price of our common stock to decline. The sale of a substantial number of shares of our common stock by Fusion Capital, or anticipation of such sales, could make it more difficult for us to sell equity or equity-related securities in the future at a time and at a price that we might otherwise wish to effect sales.

21

## Edgar Filing: TSET INC - Form 10QSB

COMPETITION IN THE MARKET FOR AIR MOVEMENT AND PURIFICATION DEVICES MAY RESULT IN THE FAILURE OF THE KRONOS(TM) PRODUCTS TO ACHIEVE MARKET ACCEPTANCE

Kronos Air Technologies presently faces competition from other companies that are developing or that currently sell air movement and purification devices. Many of these competitors have substantially greater financial, research and development, manufacturing, and sales and marketing resources than we do. Many of the products sold by Kronos Air Technologies' competitors already have brand recognition and established positions in the markets that we have targeted for penetration. In the event that the Kronos(TM) products do not favorably compete with the products sold by our competitors, we would be forced to curtail our business operations.

OUR FAILURE TO OBTAIN INTELLECTUAL PROPERTY AND ENFORCE PROTECTION WOULD HAVE A MATERIAL ADVERSE EFFECT ON OUR BUSINESS

Our success depends in part on our ability to obtain and defend our intellectual property, including patent protection for our products and processes, preserve our trade secrets, defend and enforce our rights against infringement and operate without infringing the proprietary rights of third parties, both in the United States and in other countries.

We presently have one patent that we have received a notice of allowance. We have three additional U.S. and four foreign patent applications pending. The validity and breadth of our intellectual property claims in ion wind generation and electrostatic fluid acceleration and control technology involve complex legal and factual questions and, therefore, may be highly uncertain. Despite our efforts to protect our intellectual proprietary rights, existing copyright, trademark and trade secret laws afford only limited protection.

POSSIBLE FUTURE IMPAIRMENT OF INTANGIBLE ASSETS WOULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FINANCIAL CONDITION

Our net intangible assets of approximately \$2.1 million and \$2.2 million as of September 30 and June 30, 2002 relate only to the acquisition of Kronos Air Technologies, Inc. and consists principally of purchased patent technology and marketing intangibles. They comprise 95% and 94% of our total assets as of September 30 and June 30, 2002, respectively. Intangible assets are subject to periodic review and consideration for potential impairment of value. Among the factors that could give rise to impairment include a significant adverse change in legal factors or in the business climate, an adverse action or assessment by a regulator, unanticipated competition, a loss of key personnel, and projections or forecasts that demonstrate continuing losses associated with these assets. In the case of our tangible assets, specific factors that could give rise to impairment would be, but are not limited to, an inability to obtain patents, the untimely death or other loss of Dr. Igor Krichtafovitch, the inventor of the

22

Kronos(TM) technology, or the ability to create a customer base for the sale or licensing of the Kronos(TM) technology.

Although no events have occurred that would indicate that an impairment may exist with respect to these intangible assets, should an impairment occur, we would be required to recognize it in our financial statements. Since the intangible assets comprise 95% and 94% of our total assets as of September 30 and June 30, 2002, respectively, a write-down of these intangible assets could have a material adverse impact on our total assets, net worth and results of operations.



## Edgar Filing: TSET INC - Form 10QSB

WE RELY ON MANAGEMENT AND KRONOS AIR TECHNOLOGIES RESEARCH PERSONNEL, THE LOSS OF WHOSE SERVICES COULD HAVE A MATERIAL ADVERSE EFFECT UPON OUR BUSINESS

We rely principally upon the services of our Board of Directors, senior executive management, and certain key employees, including the Kronos Air Technologies research team, the loss of whose services could have a material adverse effect upon our business and prospects. Competition for appropriately qualified personnel is intense. Our ability to attract and retain highly qualified senior management and technical research and development personnel are believed to be an important element of our future success. Our failure to attract and retain such personnel may, among other things, limit the rate at which we can expand operations and achieve profitability. There can be no assurance that we will be able to attract and retain senior management and key employees having competency in those substantive areas deemed important to the successful implementation of our plans to fully capitalize on our investment in Kronos Air Technologies and the Kronos(TM) technology, and the inability to do so or any difficulties encountered by management in establishing effective working relationships among them may adversely affect our business and prospects. Currently, we do not carry key person life insurance for any of our directors, executive management, or key employees.

### ITEM 3. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES. Within the 90 days prior to the filing date of this report, the Company carried out an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. This evaluation was done under the supervision and with the participation of the Company's President and Chief Financial Officer. Based upon that evaluation, they concluded that the Company's disclosure controls and procedures are effective in gathering, analyzing and disclosing information needed to satisfy the Company's disclosure obligations under the Exchange Act.

CHANGES IN INTERNAL CONTROLS. There were no significant changes in the Company's internal controls or in other factors that could significantly affect those controls since the most recent evaluation of such controls.

23

## PART II

### ITEM 1. LEGAL PROCEEDINGS

On June 6, 2002, Dutchess Advisors Ltd. initiated legal proceedings in Middlesex County, Massachusetts, against TSET. The complaint alleges, among other things, breach of contract, QUANTUM MERUIT, unjust enrichment and conversion with respect to a letter agreement, dated June 19, 2001, between TSET and Dutchess Advisors Ltd., and seeks, among other things, a judgment in the amount of \$75,000, exclusive of pre-judgment interest, costs and attorneys' costs. TSET contested the allegations made by Dutchess by serving a motion to dismiss all claims. Dutchess subsequently filed an amended complaint with the court on August 16, 2002. Dutchess seeks to recover up to three times its actual damages as well as its costs and attorneys' fees. TSET to filed a motion to dismiss all counts in the amended complaint. TSET believes that it has meritorious defenses and intends to vigorously defend this matter.

On February 2, 2001, we initiated, together with Kronos Air Technologies, legal proceedings in Clackamas County, Oregon against W. Alan Thompson, Ingrid T. Fuhriman, and Robert L. Fuhriman II, each of whom were formerly executive officers and members of the Board of Directors of Kronos Air Technologies. This

## Edgar Filing: TSET INC - Form 10QSB

suit alleges, among other things, breach of fiduciary duties and breach of contract by these individuals, and seeks, among other things, an order from the court referring the dispute to arbitration in accordance with the terms of these individuals. We have agreed to a change of venue of this matter to King County, Washington, and arbitrators have been selected. The parties are in the process of exchanging and complying with requests for discovery.

### ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

There were no sales of unregistered securities of the Company.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

### ITEM 5. EXHIBITS

EXHIBIT NO.	DESCRIPTION	LOCATION
2.1	Articles of Merger for Technology Selection, Inc. with the Nevada Secretary of State	Incorporated by reference to Exhibit 2.1 to the Registrant's Registration Statement on Form S-1 filed on August 7, 2001 (the "Registration Statement")
3.1	Articles of Incorporation	Incorporated by reference to Exhibit 3.1 to the Registration Statement on Form S-1 filed on August 7, 2001
3.2	Bylaws	Incorporated by reference to Exhibit 3.2 to the Registration Statement on Form S-1 filed on August 7, 2001
4.1	2001 Stock Option Plan	Incorporated by reference to Exhibit 4.1 to Registrant's

24

EXHIBIT NO.	DESCRIPTION	LOCATION
		Form 10-Q for the quarterly period ended March 31, 2002 filed on May 15, 2002
10.1	Employment Agreement, dated April 16, 1999, by and between TSET, Inc. and Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.1 to the Registration Statement on Form S-1 filed on

Edgar Filing: TSET INC - Form 10QSB

August 7, 2001

- |      |   |   |
|------|---|---|
| 10.2 | Deal Outline, dated December 9, 1999, by and between TSET, Inc. and Atomic Soccer, USA, Ltd.  | Incorporated by reference to Exhibit 10.2 to the Registration Statement on Form S-1 filed on August 7, 2001         |
| 10.3 | Letter of Intent, dated December 27, 1999, by and between TSET, Inc. and Electron Wind Technologies, Inc.   | Incorporated by reference to Exhibit 10.3 to the Registration Statement on Form S-1 filed on August 7, 2001         |
| 10.4 | Agreement, dated February 5, 2000, by and between DiAural, EdgeAudio, LLC   | Incorporated by reference to LLC and Exhibit 10.4 to the Registration Statement on Form S-1 filed on August 7, 2001 |
| 10.5 | Stock Purchase Agreement, dated March 6, 2000, by and among TSET, Inc., Atomic Soccer USA, Ltd., Todd P. Ragsdale, James Eric Anderson, Jewel Anderson, Timothy Beglinger and Atomic Millennium Partners, LLC | Incorporated by reference to Exhibit 10.5 to the Registration Statement on Form S-1 filed on August 7, 2001         |
| 10.6 | Acquisition Agreement, dated March 13, 2000, by and among TSET, Inc., High Voltage Integrated, LLC, Ingrid Fuhriman, Igor Krichtafovitch, Robert L. Fuhriman and Alan Thompson                                | Incorporated by reference to Exhibit 10.6 to the Registration Statement on Form S-1 filed on August 7, 2001         |
| 10.7 | Letter of Intent, dated April 18, 2000, by and between TSET, Inc. and EdgeAudio.com, Inc.   | Incorporated by reference to Exhibit 10.7 to the Registration Statement on Form S-1 filed on August 7, 2001         |
| 10.8 | Lease Agreement, dated May 3, 2000, by and between Kronos Air Technologies, Inc. and TIAA Realty, Inc.  | Incorporated by reference to Exhibit 10.8 to the Registration Statement on Form S-1 filed on August 7, 2001         |
| 10.9 | Agreement and Plan of Reorganization, dated May 4, 2000, by and among TSET, Inc., EdgeAudio.com, Inc., LYNK Enterprises, Inc., Robert Lightman, J. David Hogan,   | Incorporated by reference to Exhibit 10.9 to the Registration Statement on Form S-1 filed on August 7, 2001         |

25

EXHIBIT

NO.	DESCRIPTION	LOCATION
-----	-------------	----------

-----

Eric Alexander and  
Eterna Internacional, S.A.  
de C.V.

## Edgar Filing: TSET INC - Form 10QSB

10.10	Letter Agreement, dated May 4, 2000, by and between TSET, Inc. and Cancer Detection International, LLC	Incorporated by reference to Exhibit 10.10 to the Registration Statement on Form S-1 filed on August 7, 2001
10.11	Employment Agreement, dated May 19, 2000, by and between TSET, Inc. and Richard A. Papworth	Incorporated by reference to Exhibit 10.11 to the Registration Statement on Form S-1 filed on August 7, 2001
10.12	Finders Agreement, dated August 21, 2000, by and among TSET, Inc., Richard F. Tusing and Daniel R. Dwight	Incorporated by reference to Exhibit 10.12 to the Registration Statement on Form S-1 filed on August 7, 2001
10.13	Contract Services Agreement, dated June 27, 2000, by and between Chinook Technologies, Inc. and Kronos Air Technologies, Inc.	Incorporated by reference to Exhibit 10.13 to the Registration Statement on Form S-1 filed on August 7, 2001
10.14	Letter of Intent, dated July 17, 2000, by and between Kronos Air Technologies, Inc. and Polus Technologies, Inc.	Incorporated by reference to Exhibit 10.14 to the Registration Statement on Form S-1 filed on August 7, 2001
10.15	Consulting Agreement, dated August 1, 2000, by and among TSET, Inc., Richard F. Tusing and Daniel R. Dwight	Incorporated by reference to Exhibit 10.15 to the Registration Statement on Form S-1 filed on August 7, 2001
10.16	Preferred Stock Purchase Agreement, dated September 12, 2000, by and between EdgeAudio.com, Inc. and Bryan Holbrook	Incorporated by reference to Exhibit 10.16 to the Registration Statement on Form S-1 filed on August 7, 2001
10.17	Shareholders Agreement, dated September 12, 2000, by and among TSET, Inc., Bryan Holbrook and EdgeAudio.com, Inc.	Incorporated by reference to Exhibit 10.17 to the Registration Statement on Form S-1 filed on August 7, 2001
10.18	Amendment to Agreement and Plan of Reorganization dated September 12, 2000, by and among TSET, Inc., EdgeAudio.com, Inc., LYNK Enterprises, Inc., Robert Lightman, J. David Hogan, Eric Alexander and Eterna Internacional, S.A. de C.V.	Incorporated by reference to Exhibit 10.18 to the Registration Statement on Form S-1 filed on August 7, 2001
10.19	Agreement Regarding Sale of Preferred Stock, dated November 1, 2000, by Exhibit 10.19 to the and between EdgeAudio.com, Inc. and Bryan Holbrook	Incorporated by reference to Registration Statement on Form S-1 filed on August 7, 2001

EXHIBIT

NO.	DESCRIPTION	LOCATION
-----	-------------	----------

-----

## Edgar Filing: TSET INC - Form 10QSB

10.20	Amendment to Subcontract, dated December 14, 2000, by and between Bath Iron Works and High Voltage Integrated	Incorporated by reference to Exhibit 10.20 to the Registration Statement on Form S-1 filed on August 7, 2001
10.21	Consulting Agreement, dated January 1, 2001, by and between TSET, Inc. and Dwight, Tusing & Associates	Incorporated by reference to Exhibit 10.21 to the Registration Statement on Form S-1 filed on August 7, 2001
10.22	Employment Agreement, dated March 18, 2001, by and between TSET, Inc. and Alex Chriss	Incorporated by reference to Exhibit 10.22 to the Registration Statement on Form S-1 filed on August 7, 2001
10.23	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.23 to the Registration Statement on Form S-1 filed on August 7, 2001
10.24	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.24 to the Registration Statement on Form S-1 filed on August 7, 2001
10.25	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Daniel R. Dwight	Incorporated by reference to Exhibit 10.25 to the Registration Statement on Form S-1 filed on August 7, 2001
10.26	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Richard F. Tusing	Incorporated by reference to Exhibit 10.26 to the Registration Statement on Form S-1 filed on August 7, 2001
10.27	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Charles D. Strang	Incorporated by reference to Exhibit 10.27 to the Registration Statement on Form S-1 filed on August 7, 2001
10.28	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Richard A. Papworth	Incorporated by reference to Exhibit 10.28 to the Registration Statement on Form S-1 filed on August 7, 2001
10.29	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Richard A. Papworth	Incorporated by reference to Exhibit 10.29 to the Registration Statement on Form S-1 filed on August 7, 2001
10.30	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Exhibit 10.30 to the Erik W. Black	Incorporated by reference to Registration Statement on Form S-1 filed on August 7, 2001

EXHIBIT NO.	DESCRIPTION	LOCATION
----------------	-------------	----------

## Edgar Filing: TSET INC - Form 10QSB

---

10.31	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and J. Alexander Chriss	Incorporated by reference to Exhibit 10.31 to the Registration Statement on Form S-1 filed on August 7, 2001
10.32	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Charles H. Wellington	Incorporated by reference to Exhibit 10.32 to the Registration Statement on Form S-1 filed on August 7, 2001
10.33	Stock Option Agreement, dated April 9, 2001, by and between TSET, Inc. and Igor Krichtafovitch	Incorporated by reference to Exhibit 10.33 to the Registration Statement on Form S-1 filed on August 7, 2001
10.34	Letter Agreement, dated April 10, 2001, by and between TSET, Inc. and Richard A. Papworth	Incorporated by reference to Exhibit 10.34 to the Registration Statement on Form S-1 filed on August 7, 2001
10.35	Letter Agreement, dated April 12, 2001, by and between TSET, Inc. and Daniel R. Dwight and Richard F. Tusing	Incorporated by reference to Exhibit 10.35 to the Registration Statement on Form S-1 filed on August 7, 2001
10.36	Finders Agreement, dated April 20, 2001, by and between TSET, Inc. and Bernard Aronson, d/b/a Bolivar International Inc.	Incorporated by reference to Exhibit 10.36 to the Registration Statement on Form S-1 filed on August 7, 2001
10.37	Indemnification Agreement, dated May 1, 2001, by and between TSET, Inc. and Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.37 to the Registration Statement on Form S-1 filed on August 7, 2001
10.38	Indemnification Agreement, dated May 1, 2001, by and between TSET, Inc. and Daniel R. Dwight	Incorporated by reference to Exhibit 10.38 to the Registration Statement on Form S-1 filed on August 7, 2001
10.39	Indemnification Agreement, dated May 1, 2001, by and between TSET, Inc. and Richard F. Tusing	Incorporated by reference to Exhibit 10.39 to the Registration Statement on Form S-1 filed on August 7, 2001
10.40	Indemnification Agreement, dated May 1, 2001, by and between TSET, Inc. and Charles D. Strang	Incorporated by reference to Exhibit 10.40 to the Registration Statement on Form S-1 filed on August 7, 2001
10.41	Indemnification Agreement, dated May 1, 2001, by and between TSET, Inc. and Richard A. Papworth	Incorporated by reference to Exhibit 10.41 to the Registration Statement on Form S-1 filed on August 7, 2001
10.42	Indemnification Agreement, dated	Incorporated by reference to

## Edgar Filing: TSET INC - Form 10QSB

EXHIBIT NO.	DESCRIPTION	LOCATION
	May 1, 2001, by and between TSET, Inc. and Erik W. Black	Exhibit 10.42 to the Registration Statement on Form S-1 filed on August 7, 2001
10.43	Stock Option Agreement, dated May 3, 2001, by and between TSET, Inc. and Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.43 to the Registration Statement on Form S-1 filed on August 7, 2001
10.44	Common Stock Purchase Agreement, dated June 19, 2001, by and between TSET, Inc. and Fusion Capital Fund II, LLC	Incorporated by reference to Exhibit 10.44 to the Registration Statement on Form S-1 filed on August 7, 2001
10.45	Registration Rights Agreement, dated June 19, 2001, by and between TSET, Inc. and Fusion Capital Fund II, LLC	Incorporated by reference to Exhibit 10.45 to the Registration Statement on Form S-1 filed on August 7, 2001
10.46	Mutual Release and Settlement Agreement, dated July 7, 2001, by and between TSET, Inc. and Foster & Price Ltd.	Incorporated by reference to Exhibit 10.46 to the Registration Statement on Form S-1 filed on August 7, 2001
10.47	Letter Agreement, dated July 9, 2001, by and between TSET, Inc. and The Eagle Rock Group, LLC	Incorporated by reference to Exhibit 10.47 to the Registration Statement on Form S-1 filed on August 7, 2001
10.48	Finders Agreement, dated July 17, 2001, by and between TSET, Inc. and John S. Bowles	Incorporated by reference to Exhibit 10.48 to the Registration Statement on Form S-1 filed on August 7, 2001
10.49	Warrant Agreement, dated July 16, 2001, by and between TSET, Inc. and The Eagle Rock Group, LLC	Incorporated by reference to Exhibit 10.49 to the Registration Statement on Form S-1 filed on August 7, 2001
10.50	Agreement and Release, dated October 10, 2001, by and between TSET, Inc. and Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.50 to the Registrant's Form 10-K for the year ended June 30, 2001 filed on October 15, 2001
10.51	Promissory Note dated October 10, 2001 payable to Mr. Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.51 to the Registrant's Form 10-K for the year ended June 30, 2001 filed on October 15, 2001
10.52	Consulting Agreement, dated October 10, 2001, by and between TSET, Inc. and Jeffrey D. Wilson	Incorporated by reference to Exhibit 10.52 to the Registrant's Form 10-K for the year ended June 30, 2001 filed

Edgar Filing: TSET INC - Form 10QSB

29

EXHIBIT NO.	DESCRIPTION	LOCATION
		on October 15, 2001
10.53	Consulting Agreement effective October 1, 2001, by and among TSET, Inc., Steven G. Martin and Joshua B. Scheinfeld	Incorporated by reference to Exhibit 10.53 to the Registrant's Form 10-Q for the quarterly period ended September 30, 2001 filed on November 19, 2001
10.54	Letter Agreement dated November 13, 2001 by and between TSET, Inc. and Fusion Capital Fund II, LLC	Incorporated by reference to Exhibit 10.54 to the Registrant's Form 10-Q for the quarterly period ended September 30, 2001 filed on November 19, 2001
10.55	Employment Agreement, effective November 15, 2001 by and between TSET, Inc. and Daniel R. Dwight	Incorporated by reference to Exhibit 10.55 to the Registrant's Form 10-Q for the quarterly period ended March 31, 2002 filed on May 15, 2002
10.56	Agreement, dated November 13, 2001 by and between TSET, Inc. and Fusion Capital Fund II, LLC	Incorporated by reference to Exhibit 10.56 to the Registrant's Amendment No. 1 to Form S-1 filed on August 2, 2002
10.57	Common Stock Purchase Agreement, dated August 12, 2002 by and between TSET, Inc. and Fusion Capital Fund II, LLC	Incorporate by reference to Exhibit 10.57 to the Registrant's Form S-1 filed on August 13, 2002
10.58	Registration Rights Agreement, dated August 12, 2002 by and between TSET, Inc. and Fusion Capital Fund II, LLC	Incorporated by reference to Exhibit 10.58 to the Registrant's Form S-1 filed on August 13, 2002
10.59	Termination Agreement, dated August 12, 2002 by and between TSET, Inc. and Fusion Capital Fund II, LLC	Incorporated by reference to Exhibit 10.59 to the Registrant's Amendment No. 1 to Form S-1 filed on September 16, 2002
11.1	Statement re: Computation of Earnings	Not applicable
12.1	Statement re: Computation of Ratios	Not applicable
15.1	Letter re: Unaudited Interim Financial Information	Not applicable
18.1	Letter re: Change in Accounting Principals	Not applicable
24.1	Power of Attorney	Not applicable



Edgar Filing: TSET INC - Form 10QSB

27.1 Financial Data Schedule Not applicable

30

SIGNATURES

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.

DATED: NOVEMBER 14, 2002 TSET, INC.

By: /s/ Daniel R. Dwight

-----  
Daniel R. Dwight  
President and Chief Executive Officer

By: /s/ Richard A. Papworth

-----  
Richard A. Papworth  
Chief Financial Officer

31

CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of TSET, Inc. (the "Company") on Form 10-QSB for the quarter ended September 30, 2002 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned, in the capacities and on the dates indicated below, hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operation of the Company.

/s/ Daniel R. Dwight

-----  
Daniel R. Dwight  
President and Chief Executive Officer

/s/ Richard A. Papworth

-----  
Richard A. Papworth  
Chief Financial Officer

CERTIFICATION  
PURSUANT TO SECTION 302

I, Daniel R. Dwight, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of TSET, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal

## Edgar Filing: TSET INC - Form 10QSB

controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

By: /s/ Daniel R. Dwight

-----  
Daniel R. Dwight  
Chief Executive Officer

33

### CERTIFICATION PURSUANT TO SECTION 302

I, Richard A. Papworth, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of TSET, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's

Edgar Filing: TSET INC - Form 10QSB

auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

By: /s/ Richard A. Papworth

-----  
Richard A. Papworth  
Chief Financial Officer and  
Principle Accounting Officer