

ADVANCED ENVIRONMENTAL RECYCLING TECHNOLOGIES INC

Form DEF 14A

May 01, 2006

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

**SCHEDULE 14A**

Proxy Statement Pursuant to Section 14(a) of the Securities  
Exchange Act of 1934 (Amendment No. 1)

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to §240.14a-12

**Advanced Environmental Recycling Technologies, Inc.**

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(Name of Registrant as Specified In Its Charter)

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(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

1) Title of each class of securities to which transaction applies:

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1) Amount Previously Paid:

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**ADVANCED ENVIRONMENTAL  
RECYCLING TECHNOLOGIES, INC.**

**914 N Jefferson Street (72764)**

**Post Office Box 1237**

**Springdale, Arkansas 72765**

**(479) 756-7400**

**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS**

**To Be Held Thursday, June 8, 2006**

To our Stockholders:

The annual meeting of stockholders of Advanced Environmental Recycling Technologies, Inc. will be held at the Northwest Arkansas Holiday Inn Convention Center, Springdale, Arkansas at 7:00 p.m., local time, Thursday, June 8, 2006, to consider and act upon the following matters, all as more fully described in the accompanying proxy statement which is incorporated herein by this reference:

1. To elect eleven members to the eleven-person board of directors to serve until the next annual meeting of stockholders and until their respective successors shall be elected and qualify.
2. To ratify the appointment of Tullius Taylor Sartain & Sartain LLP as independent public accountants of the company for the year ending December 31, 2006; and
3. To transact such other business and to consider and take action upon any and all matters that may properly come before the annual meeting or any adjournment thereof.

The board of directors has fixed the close of business on April 12, 2006, as the record date for the determination of the stockholders entitled to notice of and to vote at the annual meeting and any adjournment thereof.

Sincerely,

Marjorie S. Brooks

*Secretary*

April 28, 2006

A proxy card and annual report of the company for the year ended December 31, 2005, are enclosed. It is important that your shares be represented whether or not you attend the meeting. Registered stockholders can vote their shares via the Internet or by using a toll-free telephone number. Instructions for using these convenient services appear on the proxy card. You can also vote your shares by marking your votes on the proxy card, signing and dating it and mailing it promptly using the envelope provided. Proxy votes are tabulated by an independent agent and reported at the annual meeting. The tabulating agent maintains the confidentiality of the proxies throughout the voting process. We hope that you can attend this meeting in person, but if you cannot do so please vote your proxy now.

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**ADVANCED ENVIRONMENTAL  
RECYCLING TECHNOLOGIES, INC.  
914 N Jefferson Street (72764)  
Post Office Box 1237  
Springdale, Arkansas 72765  
(479) 756-7400  
Annual Meeting of Stockholders  
June 8, 2006  
PROXY STATEMENT**

**SOLICITATION AND REVOCABILITY OF PROXIES**

The enclosed proxy is solicited on behalf of the board of directors of Advanced Environmental Recycling Technologies, Inc., a Delaware corporation (the Company), for use at the annual meeting of stockholders to be held at the Northwest Arkansas Holiday Inn Convention Center, Springdale, Arkansas, at 7:00 p.m. local time, Thursday, June 8, 2006, and at any adjournments thereof. The notice of meeting, proxy statement, and form of proxy are being mailed to stockholders on or about May 1, 2006.

A proxy may be revoked by delivering a written notice of revocation to the principal office of the Company or in person at the meeting at any time prior to the voting thereof.

**VOTING SECURITIES AND PRINCIPAL HOLDERS THEREOF**

At April 12, 2006, the record date, there were 38,237,812 shares of Class A common stock and 1,465,530 shares of Class B common stock issued and outstanding. Each outstanding share of Class A common stock entitles the holder thereof to one vote on matters submitted to the stockholders and each share of Class B common stock entitles the holder thereof to five votes on matters submitted to the stockholders. As of April 12, 2006, the holders of the Class B common stock are entitled to an aggregate of 7,327,650 votes. The holders of record of the Class A common stock and Class B common stock outstanding on April 12, 2006, will vote together as a single class on all matters submitted to stockholders and such other matters as may properly come before the annual meeting and any adjournments.

The enclosed form of proxy provides a method for stockholders to withhold authority to vote for any one or more nominees (See Election of Directors for the method of withholding authority to vote for directors). By withholding authority, shares will not be voted either for or against a particular matter but will be counted for quorum purposes. Abstentions and brokers non-votes, if any, are counted for purposes of determining a quorum but will have no effect on the election of directors or other matters intended to be submitted to a vote of the stockholders.

As of the record date, the Company's executive officers and directors beneficially owned approximately 37.5% of the currently outstanding shares of Class A common stock and 93.9% of the shares of Class B common stock, and collectively beneficially owned shares representing approximately 44.8% of the votes entitled to be cast upon matters submitted at the annual meeting. As of the record date, Marjorie S. Brooks and corporations controlled by her beneficially owned shares representing approximately 31.1% of the votes entitled to be cast and may be in a position to control the Company.

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The following table sets forth, as of April 12, 2006, certain information with regard to the beneficial ownership of the Company's capital stock by each holder of 5% or more of the outstanding stock, by each named executive officer and director of the Company, and by all officers and directors as a group:

<b>Name and Address of Beneficial Owner</b>	<b>Title of Class(1)</b>	<b>Number of Shares of Common Stock(2)</b>	<b>Percentage of Class Outstanding(2)(17)</b>	<b>Percentage of Total Voting Power(2)(18)</b>
Marjorie S. Brooks	Class A	12,186,833(3)	26.9%	31.1%
	Class B	837,588(4)	57.2%	
Joe G. Brooks	Class A	896,772(5)	2.3%	5.1%
	Class B	284,396	19.4%	
J. Douglas Brooks	Class A	919,065(6)	2.4%	3.4%
	Class B	131,051	8.9%	
Jerry B. Burkett	Class A	325,848(7)	*	1.1%
	Class B	33,311	2.3%	
Sal Miwa	Class A	489,811(8)	1.3%	1.1%
Stephen W. Brooks	Class A	821,112(9)	2.1%	2.8%
	Class B	89,311	6.1%	
Jim Robason	Class A	221,142(10)	*	*
Melinda Davis	Class A	257,326(11)	*	*
Michael M. Tull	Class A	1,028,362(12)	2.6%	2.2%
Samuel L. Milbank	Class A	578,165(13)	1.5%	1.3%
Tim W. Kizer	Class A	26,278(14)	*	*
Edward P. Carda	Class A	26,278(14)	*	*
Robert A. Thayer	Class A	150,000(8)	*	*
Jim Precht	Class A	407,700(15)	1.1%	*
Alford Drinkwater	Class A	10,000(16)	*	*
Officers and directors as a group (fifteen persons)	Class A	18,344,692	37.5%	44.8%
P. O. Box 1237 Springdale, Arkansas 72765	Class B	1,375,657	93.9%	

\* Less than 1%

- (1) The Class B common stock is substantially identical to the Class A common stock, except that each share of Class B common stock has five votes per share and each share of Class A common stock has one vote per share. Each share of Class B common stock is convertible into one share of Class A common stock.
- (2) Beneficial ownership of shares was determined in accordance with Rule 13d-3(d)(1) of the Exchange Act and included shares underlying outstanding warrants and options which the named individual had the right to acquire within sixty days (June 11, 2006) of April 12, 2006.
- (3) Includes 4,042,323 shares owned directly, 1,121,457 in trusts or corporations controlled by Mrs. Brooks, 35,848 shares issuable pursuant to restricted stock awards, 425,000 shares issuable upon exercise of stock

options, 3,974,080 shares issuable upon exercise of Class F and Class G Warrants issued in connection with a private placement of Class A common stock in May of 1994, 1,771,792 shares issuable upon exercise of Class H Warrants, 323,000 shares issuable upon exercise of Series X and Y warrants owned directly and 493,333 shares issuable upon exercise of Series X and Series Y Warrants owned indirectly through two corporations controlled by Mrs. Brooks (Razorback Farms, Inc. and Brooks Investment Company).

- (4) Includes 403,946 shares owned directly by Mrs. Brooks and 433,642 shares owned by two corporations controlled by Mrs. Brooks. (Razorback Farms, Inc. is the record owner of 312,320 shares and Southern Mineral and Fibers, Inc. is the record owner of 121,322 shares, representing approximately 21.3% and 8.3%, respectively, of the Class B common stock). Excludes additional shares owned by adult children

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- of Mrs. Brooks, including Joe G. Brooks, Stephen W. Brooks and J. Douglas Brooks, as to which she disclaims a beneficial interest.
- (5) Includes 607,400 shares owned directly, 4,500 shares owned as custodian for Joe G. Brooks' minor child, 38,205 shares owned as custodian for Brooks' Children's Trust and 246,667 shares issuable upon exercise of stock options.
  - (6) Includes 434,324 shares owned directly, 84,741 shares owned indirectly and 400,000 shares issuable upon exercise of stock options.
  - (7) Includes 63,000 shares owned directly, 2,000 shares owned by Mr. Burkett as custodian for his minor child, 10,000 shares owned by a partnership controlled by Mr. Burkett, 35,848 shares issuable pursuant to restricted stock awards, and 215,000 shares issuable upon exercise of stock options.
  - (8) Includes 35,848 shares issuable pursuant to restricted stock awards and 453,496 shares issuable upon exercise of stock options.
  - (9) Includes 296,112 shares owned directly and 525,000 shares issuable upon exercise of stock options.
  - (10) Includes 99,494 shares owned directly, 35,848 shares issuable pursuant to restricted stock awards, 60,800 shares issuable upon exercise of Series X and Series Y warrants, and 25,000 shares issuable upon exercise of stock options.
  - (11) Represents 19,012 shares owned directly, 66,666 shares in a trust controlled by Ms. Davis, 35,848 shares issuable pursuant to restricted stock awards, 75,000 shares issuable upon exercise of stock options, and 60,800 shares issuable upon exercise of Series X and Series Y warrants.
  - (12) Includes 449,181 shares owned directly, 35,848 shares issuable pursuant to restricted stock awards, 100,000 shares issuable upon exercise of stock options, and 443,333 shares issuable upon exercise of Series X and Series Y warrants.
  - (13) Includes 281,130 shares owned directly, 35,848 shares issuable pursuant to restricted stock awards, 112,697 shares issuable upon exercise of Series X Warrants, 41,604 shares issuable upon exercise of Series Y Warrants, 31,886 shares issuable upon exercise of Class I Warrants, and 75,000 shares issuable upon exercise of stock options.
  - (14) Includes shares issuable pursuant to restricted stock awards.
  - (15) Includes 7,700 shares owned directly and 400,000 shares issuable upon the exercise of stock options.
  - (16) Includes shares owned directly.
  - (17) Class A common stock beneficial ownership was calculated by dividing the beneficial ownership of each individual by the sum of: (i) the total shares of Class A common stock outstanding at April 12, 2006, and (ii) the total shares underlying outstanding warrants and options which the named individual had the right to acquire within 60 days (June 11, 2006) of April 12, 2006. Class B common stock beneficial ownership is calculated based on 1,465,530 shares outstanding on April 12, 2006.
  - (18) Calculated by dividing the voting rights of the beneficial ownership of each individual by the sum of: (i) the total votes available to be cast at April 12, 2006, and (ii) in footnote (16) above.

At April 12, 2006, there were 38,237,812 shares of Class A common stock and 1,465,530 shares of Class B common stock issued and outstanding. The previous table indicates that those directors, officers and 5% shareholders, as a group, beneficially owned shares representing approximately 44.8% of the votes entitled to be cast upon matters submitted to a vote of the Company's stockholders, and Marjorie S. Brooks and corporations controlled by her beneficially owned shares representing approximately 31.1% of the votes entitled to be cast and may be in a position to control the Company.

Table of Contents**DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT**

The directors and executive officers of the Company as of April 12, 2006, are as follows:

<b>Name</b>	<b>Age</b>	<b>Position</b>
Joe G. Brooks	50	Chairman of the board of directors, co-chief executive officer and president
Sal Miwa	49	Vice-chairman of the board of directors
Stephen W. Brooks	49	Co-chief executive officer and director
Marjorie S. Brooks	70	Secretary, treasurer and director
J. Douglas Brooks	46	Senior vice-president raw materials
Alford Drinkwater	54	Senior vice president plastic operations
Jim Precht	60	Senior vice-president sales and marketing
Robert A. Thayer	54	Senior vice-president and chief financial officer
Eric E. Barnes	32	Controller and chief accounting officer
Jerry B. Burkett	49	Director
Edward P. Carda	65	Director
Melinda Davis	63	Director
Tim W. Kizer	40	Director
Samuel L. Milbank	65	Director
Jim Robason	68	Director
Michael M. Tull	51	Director

The Company's board of directors elected **Joe G. Brooks** as its chairman and the Company's co-chief executive officer in December 1998, and he has served as president since February 2000. Mr. Brooks has served as president or in other executive office capacities and has been a director since the Company's inception in December 1988, including service as chairman and CEO from inception until August 1993. He was a member of Clean Texas 2000, appointed by then Governor George W. Bush in 1995.

**Sal Miwa** has been an outside director of the Company since January 1994. He served as chairman of the board between December 1995 and December 1998, and as vice chairman from December 1998 through July 2005. From January 2005 to present, Mr. Miwa has been CEO and chairman of Greenstone Holdings, Inc. (OTC GSHG), a chemical technology company located in New York City primarily serving the building and construction industry. From July 2004 to December 2005, he was CEO of Greenstone Inc. of Delaware, a predecessor of Greenstone Holdings, Inc. From April 2000 to June 2004, he was COO and director of RealRead Inc., an online document service company. For more than 20 years Mr. Miwa has been engaged in various international businesses and serves on boards of several closely held family businesses around the world. He received his master's degree in Aerospace Engineering from the Massachusetts Institute of Technology in 1981.

The Company's board of directors elected **Stephen W. Brooks** as co-chief executive officer in December 1998. Mr. Brooks has served as its chief executive officer and has been a director since January 1996. Mr. Brooks has served as CEO and chairman of the board of Razorback Farms, Inc. from January 1996 to the present. Razorback Farms is a Springdale, Arkansas based firm that specializes in vegetables processing. Mr. Brooks also serves on the board of the Ozark Food Processors Association.

**Marjorie S. Brooks** has been secretary, treasurer and a director since the Company's inception in December 1988. Mrs. Brooks has served as secretary and treasurer of Brooks Investment Co., a holding company for the Brooks family investments, for more than thirty years.

**J. Douglas Brooks** has served as senior vice-president from inception to September 2003, has been in charge of raw material sourcing and strategic relationships since 1998, and has been a senior vice president since September 2003. Mr. Brooks was vice-president of plastics from 1995 through 1998, was previously



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project manager for AERT's polyethylene recycling program with The Dow Chemical Company, and is a joint inventor on several of AERT's process patents for recycling polyethylene film for composites.

**Robert A. Thayer** was named by the board of directors to succeed Edward J. Lysen as chief financial officer and senior vice-president in September 2005. Since October 2002, Mr. Thayer has served as the assistant to AERT chairman Joe G. Brooks, during which time he has had executive assignments in all aspects of AERT's business including finance, operations, and administration. From January 1997 to October 2002, Mr. Thayer was a principal at Madison Research, Denison, Texas where he conducted independent financial research under contract to banks and financial publishers. From January 2001 to July 2002 he also served as Vice President of Finance for Asia Teletech Company, Ltd., a Thailand headquartered voice-over-internet company where he was responsible for raising the company's startup capital. Prior to 1997, Mr. Thayer spent twenty-one years in the software and investment banking industries with financial, systems and executive responsibilities. He received a BA in Economics from the University of Colorado and studied graduate economics at the University of Wisconsin, Madison. Mr. Thayer is a Chartered Financial Analyst.

**Alford Drinkwater** has served as senior vice president of logistics, laboratories, and plastic operations since September 2003. Prior to joining the Company in May 2000, Mr. Drinkwater had been the Assistant Director for the Established Industries Division of the Arkansas Department of Economic Development and was on the Advocacy Team from November 1988 until January 2000. From September 1986 until July 1988, he owned and operated Town and Country Waste Services, Inc. a waste services company engaging in the development of waste recycling, energy recovery, and disposal systems. From April 1981 until January 1987, Mr. Drinkwater was the Resource Recovery Manager for Metropolitan Trust Company, and was primarily involved in waste-to-energy systems development. From July 1974 until April 1981, Mr. Drinkwater worked for the State of Arkansas as Assistant to the Chief of the Solid Waste Control Division of the Arkansas Department of Pollution Control & Ecology and as the Manager of the Biomass and Resource Recovery Program of the Arkansas Department of Energy.

**Jim Precht** has served as senior vice-president of sales and marketing for the Company since February 2001, and senior vice president since September 2003. Mr. Precht was formerly general manager of Weyerhaeuser Building Materials' Pittsburgh Customer Service Center with 32-years of industry experience.

**Eric E. Barnes** was appointed by the board of directors as chief accounting officer in September 2005. Mr. Barnes joined AERT's accounting department in November 1997 after graduating from the University of Arkansas with a BS in Accounting and an MA in Economics. He was named AERT's controller in January 2000. Mr. Barnes is a Certified Public Accountant.

**Jerry B. Burkett** has served on the board of directors of the Company since May 1993. Mr. Burkett has been a rice and grain farmer since 1979 and has been a principal in other closely held businesses. He is the past president of the Arkansas County Farm Bureau. In April 2002, Mr. Burkett was elected to serve as a director of the Ag Heritage Farm Credit Services board.

**Edward P. Carda** was elected to the board of directors in July 2005. Mr. Carda began his 37-year business career with Weyerhaeuser Company in June 1967, ending with his retirement in December 2003. While at Weyerhaeuser, he served in various management positions, including statutory reporting, heading large accounting departments, interacting with external and internal auditors and all types of management. Mr. Carda spent the last 10 years of his career as the business controller for the distribution business of Weyerhaeuser. While in this capacity, he received many awards for his performance for profit and working capital improvement initiatives. Mr. Carda attended the University of Montana and graduated with a degree in accounting. He has served for 25 years on the board of directors of the Woodstone Credit Union in Federal Way, Washington and is currently its Vice Chairman. He also serves on the credit union's audit committee.

**Melinda Davis** has served on the board of directors since July 2001. From December 2000 to the present, Ms. Davis has provided professional consulting services in the areas of financial management and cost accounting for manufacturing operations. Ms. Davis retired as senior vice-president and treasurer from Allen Canning Co. in December 2000, after serving for 39 years in various accounting and financial management positions.



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**Tim W. Kizer** was elected to the board of directors in July 2005. Since December 2004, Mr. Kizer has served as president and partner of Bentonville Global Associates, a global consultancy firm specializing in collaborative commerce. Mr. Kizer is executive director of the *Doing Business in Bentonville Series* seminar level program series in Bentonville Arkansas. From April 2001 to December 2004, Mr. Kizer was director of the Center for Management and Executive Development and the Donald W. Reynolds Center for Enterprise Development, Sam M. Walton College of Business, University of Arkansas. From January 2000 to April 2001, Mr. Kizer was managing director of Information Technology Research Center, Sam M. Walton College of Business, University of Arkansas. Mr. Kizer was a business and industry specialist for the Division of Continuing Education at the University of Arkansas from October 1996 until January 2000. He has a BA from the University of Louisville and is a member of the Board of Advisors of RFID Global Solution in Bentonville, Arkansas.

**Samuel L. Milbank** has served on the board of directors since July 2000. Mr. Milbank is a co-founder and owner of Milbank Roy and Co., LLC, an investment bank founded in February 2005 and focused on M&A, advisory as well as funding of middle market companies. Prior to that, from April 1997 to February 2005, Mr. Milbank was a managing director of Zanett Securities Corporation, a company also focusing on investment banking services to the middle market. From February 1992 to January 1996, Mr. Milbank was a senior vice-president and sales manager with Lehman Brothers, Inc. in New York, where he managed a team that provided interest rate and currency risk management for central banks and other official institutions. From March 1973 to February 1992, Mr. Milbank worked with Salomon Brothers, Inc. as a director and manager of the international department. Since January 1990, Mr. Milbank has served as chairman of Milbank Memorial Fund, a private operating foundation (established in 1905), concerned with environmental and public health issues. He has a BS from Columbia University and a MBA in Finance from The Amos Tuck School of Business Administration at Dartmouth College.

**Jim Robason** has served on the board of directors since July 2003. Since January 2005, Mr. Robason has been a consultant to and supervisor of the Company's plant operations on an interim basis. Mr. Robason joined Allen Canning Co. in 1967. Mr. Robason served as senior vice-president operations of Allen Canning Co. from 1974 until his retirement in 2002. As senior vice-president of operations with Allen Canning Co., he was responsible for the operation of twelve plants with plant managers and raw product procurement managers, as well as special projects engineering, reporting to him. He has a vast amount of knowledge in all phases of manufacturing including infrastructure, building, equipment, and engineering; with a focus on the full production arena from product procurement through the production process. Mr. Robason is a graduate of West Texas State University. He has served on Allen Canning's executive committee and profit sharing/retirement plan committee in addition to his operations responsibilities.

**Michael M. Tull** has served on the board of directors of the Company since December 1998. Mr. Tull has served since 1990 as the president and majority owner of Tull Sales Corporation, a manufacturer's representative company, which professionally represents eight manufacturing companies and is responsible for the sales and marketing of those companies' window and door related components in the southeastern United States. Mr. Tull serves on boards of several closely held family businesses and is the chairman and a board of director member of the National Wild Turkey Federation, which is one of the largest North American conservation organizations.

Joe G. Brooks, Stephen W. Brooks, and J. Douglas Brooks are brothers and sons of Marjorie S. Brooks. There are no other familial relationships between the current directors and executive officers.

Each of the Company's directors has been elected to serve until the next annual meeting of stockholders or until their successors are elected and qualified. Officers serve at the discretion of the Board of Directors.

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**CORPORATE GOVERNANCE**

**Independence of Directors**

The board of directors has determined that Jerry B. Burkett, Edward P. Carda, Melinda Davis, Tim W. Kizer, Samuel L. Milbank, and Sal Miwa are independent under the NASDAQ Stock Market's (NASDAQ) corporate governance listing standards, and that Marjorie S. Brooks, secretary and treasurer, Joe G. Brooks, chairman, co-CEO and president, Stephen W. Brooks, co-CEO, Michael M. Tull and Jim Robason are not independent under such listing standards.

During fiscal 2005, the Company held four executive sessions of the board of directors in which only independent members of the board were present. The chairpersons of the audit committee, compensation committee and nominating and corporate governance committee each presided over the meetings on a rotating basis.

The Company encourages, but does not require, directors to attend annual meetings of stockholders. All members of the board attended the Company's 2005 stockholder meeting.

**Board Meeting and Certain Committees Reports and Meetings**

During the Company's fiscal year ended December 31, 2005, the board of directors held eight meetings. All directors attended 75% or more of the total number of meetings of the board of directors and its committees on which he or she served.

From January 1, 2005 through July 28, 2005, the audit committee of the board of directors consisted of three independent directors under NASDAQ's director and audit committee independence standards: Jerry B. Burkett, Melinda Davis (chairperson), and Sal Miwa. On July 28, 2005, Edward P. Carda, also an independent director, was elected to the board of directors and joined the audit committee. The composition of the audit committee has not changed since July 28, 2005. The audit committee is directly responsible for the engagement of the Company's independent accountants and is responsible for approving the services performed by the Company's independent accountants and for reviewing and evaluating the Company's accounting principles and its system of internal accounting controls. The audit committee met four times in 2005. Melinda Davis serves as the financial expert of the audit committee.

From January 1, 2005 through July 28, 2005, the compensation committee consisted of Samuel L. Milbank (chairperson), Sal Miwa and Jim Robason. On July 28, 2005, Edward P. Carda joined the committee and Jim Robason left the committee. The compensation committee establishes and administers the Company's compensation plans on behalf of the board of directors and makes recommendations to the board of directors as to stock options, restricted stock awards or other awards granted thereunder and other compensation matters. The compensation committee met five times in 2005.

From January 1, 2005 through July 28, 2005, the nominating and corporate governance committee consisted of Jerry B. Burkett (chairperson), Melinda Davis, and Jim Robason. On June 21, 2005, the nominating and corporate governance committee was revised to consist of Jerry B. Burkett (chairperson) and Melinda Davis. On July 28, 2005, Tim W. Kizer joined the committee. The nominating and corporate governance committee evaluates the efforts of AERT and its board of directors to maintain effective corporate governance practices and identifies candidates for election to the board of directors. The nominating and corporate governance committee met two times in 2005.

The nominating and corporate governance committee believes that candidates for director should have certain minimum qualifications, including being able to read and understand basic financial statements and having the highest personal integrity and ethics. The committee also considers such factors as relevant expertise and experience, ability to devote sufficient time to the affairs of the Company, demonstrated excellence in his or her field, the ability to exercise sound business judgment and the commitment to rigorously represent the long-term interests of the Company's stockholders. Candidates for director will be reviewed in the context of the current composition of the board, the operating requirements of the Company and the long-term interests of stockholders.

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The nominating and corporate governance committee does not have a formal process for identifying and evaluating nominees for directors. Instead, it uses its network of contacts to identify potential candidates. The committee will conduct any appropriate and necessary inquiries into the backgrounds and qualifications of possible candidates after considering the function and needs of the board. The committee will meet to discuss and consider such candidates' qualifications and then select a nominee for recommendation to the board by majority vote.

Although the nominating and corporate governance committee has not established procedures for considering nominees recommended by stockholders, the committee will consider director candidates recommended by stockholders, and those candidates will receive substantially the same consideration that candidates recommended by the nominating and corporate governance committee receive. Stockholders wishing to recommend director candidates for consideration by the committee may do so in writing to the corporate secretary at least 180 days in advance of the annual meeting, giving the recommended nominee's name, biographical data, and qualifications, accompanied by the written consent of the recommended nominee.

The charters of the audit, compensation, and nominating and corporate governance committees are available on the corporate website at [www.aertinc.com](http://www.aertinc.com). The Company has implemented a Corporate Hotline through which the audit committee, the board of directors, and the corporate compliance officer may be contacted, as appropriate. This service and number is available on our corporate website.

**AUDIT COMMITTEE REPORT**

*The following report of the audit committee for fiscal year 2005 does not constitute soliciting material and should not be deemed filed or incorporated by reference into any other Company filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that the Company specifically incorporates this report by reference therein.*

The audit committee of the Company is composed of four non-employee directors, and each member of the committee is independent in accordance with the policy of the National Association of Security Dealers applicable to NASDAQ listed companies. The committee operates under a written charter adopted by the board of directors.

Management is responsible for the Company's internal controls and the financial reporting process. The independent auditors are responsible for performing an independent audit of the Company's financial statements in accordance with generally accepted auditing standards and to issue a report thereon. The committee's responsibility is to engage independent public accountants for the Company and to monitor and oversee the Company's financial reporting process and report its findings to the board of directors.

The committee fulfills its responsibilities through periodic meetings with management and independent auditors. The committee reviewed and discussed with management and independent auditors the audited financial statements in the Company's annual report on Form 10-K for the year ended December 31, 2005. The committee also discussed with the independent auditors matters required to be discussed by Statement on Auditing Standards No. 61. In addition, the committee has received and reviewed the written disclosures and the letter from the independent auditors required by Independence Standards Board Standard No. 1, Independence Discussions with Audit Committees, and has discussed with the auditors the auditor's independence.

On the basis of these reviews and discussions, the audit committee recommended to the board of directors that the board approve the inclusion of the Company's audited financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for filing with the Securities and Exchange Commission (SEC).

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The audit committee has also considered whether the provision of non-audit services by the independent registered public accounting firm, Tullius Taylor Sartain & Sartain LLP ( TTS&S ), is compatible with maintaining auditor independence. TTS&S performed tax preparation services for the Company during 2005. No other non-audit related services were provided by TTS&S during 2005.

Submitted by the audit committee,

Jerry B. Burkett

Edward P. Carda

Melinda Davis, chairperson

Sal Miwa

**COMPENSATION COMMITTEE REPORT**

*The following report of the compensation committee for fiscal year 2005 does not constitute soliciting material and should not be deemed filed or incorporated by reference into any other Company filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that the Company specifically incorporates this report by reference therein.*

The compensation committee of the board of directors is responsible for administering incentive plans and reviewing and making recommendations to the board of directors with respect to the compensation of AERT executive officers and key executives.

The following is the compensation committee's report to shareholders on the Company's executive compensation policies with respect to compensation reported for the fiscal year ended December 31, 2005.

**Compensation Committee Report on Executive Compensation**

Key compensation-related responsibilities of the Compensation Committee of the Board of Directors:

To establish and periodically review AERT's compensation philosophy and the adequacy of compensation plans and programs for directors, executive officers and other AERT employees and make recommendations to the board of directors with respect thereto;

To establish compensation arrangements and incentive goals for executive officers and to administer compensation plans and make recommendations to the board of directors with respect thereto;

To review the performance of the executive officers and award incentive compensation and adjust compensation arrangements as appropriate based upon performance;

To review and monitor management development and succession plans and activities; and

To prepare the report on executive compensation for inclusion in AERT's annual proxy statement in accordance with Securities Exchange Commission rules and regulations.

For the fiscal year ended December 31, 2005, the Committee's activity focused on the key elements of the total direct compensation program for executive officers, which included base pay, quarterly incentive awards, discretionary incentive awards, and long-term incentives. Elements reviewed as part of the long-term incentives to executive officers included type and level of award distribution.

The Company's executive compensation program is designed to:

Attract, motivate and retain executive officers who can make significant contributions to the Company's long-term success;

Align the interests of executive officers with those of shareholders; and

Place a significant portion of an executive officer's total compensation at risk by tying it to the Company's financial performance.

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The primary components of the Company's executive compensation programs are: base salary, quarterly incentive awards, discretionary awards, and long-term incentive awards:

*Base Salary*

Base salaries are generally targeted at the middle of the competitive marketplace (the median).

The market rate for an executive position is determined through an assessment by the Company's human resources personnel under the guidance and supervision of the compensation committee. This assessment considers relevant industry salary practices, the position's complexity, and level of responsibility, its importance to the Company in relation to other executive positions, and the competitiveness of an executive's total compensation.

Subject to the Committee's approval, the level of an executive officer's base pay is determined on the basis of:

Relevant comparative compensation data; and

The Chief Executive Officer's assessment of the executive's performance, experience, demonstrated leadership, job knowledge and management skills.

*Quarterly Incentive Awards*

These awards were discontinued on October 1, 2005. The awards were intended to provide a linkage among executive performance, quarterly performance measures, and long-term shareholder value.

During 2005, quarterly incentive awards were earned as the Company met specific objectives for cash flow and net income. The quarterly incentive awards were designed to reward executive performance with cash incentive awards comparable to those found in the marketplace in which the Company competes for executive talent.

*Discretionary Awards*

The compensation committee may, at its discretion, authorize periodic cash awards to executives. Discretionary awards are designed to give the compensation committee the flexibility to provide incentives that are comparable to those found in the marketplace in which the Company competes for executive talent. In determining the extent and nature of discretionary awards, the compensation committee considers the Company's cash flow, net income, progress toward short and long-term business objectives, and competitive compensation programs.

When considering discretionary awards, the compensation committee identifies the employees who are eligible to participate and computes and certifies the size of the discretionary pool based on financial information supplied by the Company's officers. The award made to each eligible participant is based on the opportunity level assigned to the participant and an assessment of his or her performance and the performance of their business unit versus corporate objectives.

*Long-Term Incentive Awards*

Long-term executive incentives are designed to promote the interests of AERT and its shareholders by attracting and retaining eligible directors, executives and other key employees.

The compensation committee has the authority to determine the participants to whom awards shall be granted. The awards under prior Company plans could be made in the form of stock options, restricted stock units, performance awards and other stock-based awards. Consistent with the views of the board of directors and compensation committee that the interests of employees and directors are more likely to be aligned with stockholders to the extent that such employees and directors are stockholders of the Company, the Company has determined for the foreseeable future to provide incentive equity compensation in the form of restricted stock awards rather than options or other forms of equity compensation. The 2005 Key Associate and

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Management Equity Incentive Plan and the 2005 Non-Employee Director Equity Incentive Plan are reflective of this shift in compensation policy.

**2005 Awards**

***Chief Executive Officer compensation***

In determining CEO compensation, the Committee considered:

The Company's financial performance and peer group compensation data; and

CEO leadership, decision-making skills, experience, knowledge, communication with the Board and strategic recommendations, as well as the Company's positioning for future performance.

The Committee considered many factors and did not place any particular relative weight on one over another, but the Company's financial performance is generally given the most weight.

The Committee's recommendations regarding CEO compensation and other related matters are reported to the Board and, in the case of each specific recommendation during 2005, were approved by the Board.

For fiscal year ended December 31, 2005, the Committee's decisions regarding CEO compensation included the following:

Co-CEO Joe G. Brooks was awarded cash bonuses totaling \$45,000 under the quarterly incentive plan.

During 2005, Co-CEO Joe G. Brooks took overall responsibility for planning and execution of the Company's strategic direction. He was awarded a cash bonus of \$125,000 under the Discretionary Awards plan. Co-CEO Stephen W. Brooks undertook primary responsibility for day-to-day operations at the Company and he was awarded a \$75,000 cash bonus under the Discretionary Awards plan.

Before arriving at its final decision regarding the amount of CEO annual incentive award, the Committee confirmed that the Company's compensation program is consistent with marketplace practices linking pay for performance.

***Deductibility of Compensation:***

Under Section 162(m) of the Internal Revenue Code, AERT may not deduct compensation in excess of \$1,000,000 paid to AERT's Chief Executive Officer or to each of the named executive officers unless the compensation meets specific criteria for performance-based compensation. Awards under the short-term incentive compensation plan do not meet the criteria of being performance-based awards under Section 162(m) of the Internal Revenue Code of 1986, as amended, and, therefore, would not qualify as a deduction to the extent in excess of Section 162(m) limits. Certain awards under the long-term incentive plan, such as stock options or restricted stock awards could satisfy the criteria of being performance based under Section 162(m) to qualify as deductible under the Internal Revenue Code of 1986, as amended. The Company's historical levels of compensation have not presented issues of deductibility under Section 162(m) of the Internal Revenue Code of 1986. The compensation committee reserves the right to approve non-deductible compensation if the Committee believes it is in the best interests of the shareholders.

**2005 Key Associate and Management Equity Incentive Plan**

The compensation committee has reviewed and approved a compensation plan for the Company's management and associates that is designed to reward focus on increasing throughputs, reducing costs, and increasing efficiencies. The Key Associate and Management Equity Incentive plan, which is administered by the committee, gives the Company flexibility to provide incentives that are comparable to those found in the marketplace in which the Company competes for management and associate talent. In determining the extent and nature of awards, the compensation committee considers the Company's cash flow, net income, progress toward short and long term business objectives, and competitive compensation programs.

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**Conclusion Regarding Executive Compensation:**

Based upon its review of the Company's executive compensation program, the Committee has concluded that the program's basic structure is appropriate, competitive, and effective to serve the purposes for which it was established.

**MEMBERS OF THE COMMITTEE:**

Edward P. Carda

Samuel L. Milbank, chairperson

Sal Miwa

**Employment Agreements**

The Company has no written employment agreements with its key executives.

**DIRECTOR COMPENSATION**

Directors who are also employees of the Company are not entitled to any additional compensation by virtue of service as a director, except for reimbursement of any specific expenses attributable to such service. Non-employee directors receive annual compensation for board service of \$15,000 in cash plus annual restricted stock awards of shares with a market value of \$30,000 measured on an average closing sale price basis over a 50-business day period preceding the award. Newly elected directors are initially granted restricted stock equal to a prorated portion of the yearly \$30,000 award based on their period of service in their initial fiscal year as a director. Such restricted stock awards vest over a three-year period, with 20% of a particular award vesting on the first anniversary thereof, an additional 30% of such award (50% cumulatively) vesting on the second anniversary of the award, and the 50% balance of the award vesting on the third anniversary of the award. In addition, non-employee board committee members receive annual cash compensation as follows: audit committee: \$8,000 (chairperson) and \$3,000 (other members); compensation committee: \$5,000 (chairperson) and \$3,000 (other members); and nominating committee: \$4,000 (chairperson) and \$2,000 (other members). Directors are also reimbursed for out-of-pocket expenses in connection with their attendance at meetings.

**Table of Contents****EXECUTIVE OFFICER COMPENSATION**

The following table sets forth the aggregate compensation paid by the Company during the three years ended December 31, 2005, to the co-chief executive officers and to each of the next four most highly compensated executive officers of the Company whose aggregate annual salary and bonus in 2005 exceeded \$100,000.

**Summary Compensation Table**

(a) Name and Principal Position	(b) Year	Annual Compensation		(e) Other Annual Compensation\$(1)
		(c) Salary(\$)	(d) Bonus(\$)	
Stephen W. Brooks Co-ceo	2005	76,423	75,000	
	2004	52,000(2)	0	
	2003	52,000(2)	0	
Joe G. Brooks Co-ceo	2005	165,625	170,000	12,786(8)
	2004	157,500	193,500(3)	48,775(4)
	2003	157,500	15,000	
Robert A. Thayer Senior-vice president and chief financial officer	2005	132,500	85,000	
	2004	124,423	30,000	
	2003	119,123	25,000	
Jim Precht Senior-vice president - sales and marketing	2005	122,500	70,000	18,697(9)
	2004	102,521	30,000	20,188(6)
	2003	73,750(5)	10,000	16,590(7)
J. Douglas Brooks Senior-vice president - raw materials	2005	102,500	15,000	
	2004	87,288	16,570	
	2003	84,000	5,000	
Alford Drinkwater Senior-vice president - administration	2005	100,000	7,000	
	2004	81,731	16,570	
	2003	75,000	5,000	

- (1) Excludes perquisites less than \$50,000 and that do not exceed 10% of salary and bonus.
- (2) Paid pursuant to a non-employee consulting agreement with the Company.
- (3) Includes \$130,000 awarded to Mr. Brooks by the Board of Directors and \$63,500 awarded in quarterly performance incentives which Mr. Brooks voluntarily did not take until 2004.
- (4) Includes 48 months of \$1,000 for a non-accountable expense allowance which Mr. Brooks voluntarily did not take until 2004.
- (5) In the first six months of 2003 there was an agreement between AERT and Weyerhaeuser where each paid one-half of Mr. Precht's salary. The amounts above account for AERT's portion of the annual salary.
- (6) Includes \$14,000 for a non-accountable expense allowance and \$6,188 for the value of a company-provided vehicle.
- (7)

Includes \$12,000 for a non-accountable expense allowance and \$4,590 for the value of a company-provided vehicle.

(8) Includes \$12,000 for a non-accountable expense allowance.

(9) Includes \$12,000 for a non-accountable expense allowance and \$6,697 for the value of a company-provided vehicle.

**Table of Contents****Aggregated Option/SAR Exercises in Last Fiscal Year  
and FY-End Option/SAR Values**

Name	Shares Acquired on Exercise(#)	Value Realized(\$)	Number of Securities Underlying Unexercised Options/SAR at December 31, 2005(#)		Value of Unexercised In-the-Money Options/SAR at December 31, 2005(\$)	
			Exercisable/Unexercisable	Exercisable/Unexercisable	Exercisable/Unexercisable	Exercisable/Unexercisable
Stephen W. Brooks	0	0	525,000/0		589,050/0	
Joe G. Brooks	0	0	246,667/0		287,425/0	
Robert A. Thayer	0	0	150,000/50,000		90,000/30,000	
Jim Precht	0	0	400,000/0		46,000/0	
J. Douglas Brooks	100,000	104,100	400,000/0		487,125/0	
Alford Drinkwater	0	0	0/0		0/0	

**Equity Compensation Plan Information**

The following table provides information as of December 31, 2005, regarding shares outstanding and available for issuance under the Company's existing stock option plans.

Plan Category	Number of Securities to Be Issued Upon Exercise of Outstanding Options, Warrants and Rights (a)	Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights (b)	Number of Securities Remaining Available for Future Issuance (c)
Equity compensation plans approved by security holders	3,688,130	\$ 1.01	2,026,045
Equity compensation plans not approved by security holders			
<b>Total</b>	<b>3,688,130</b>	<b>\$ 1.01</b>	<b>2,026,045</b>

**Compensation Committee Interlocks and Insider Participation**

The board of directors, as a whole, reviews, and acts upon personnel policies and executive compensation matters, based upon recommendations of the compensation committee. Joe G. Brooks and Stephen W. Brooks serve as executive officers of the Company; however, such individuals do not participate in compensation decisions or in forming compensation policies in which they have a personal interest or in any deliberations of the board of directors concerning such matters, nor do they vote on any such matters, although Messrs Joe G. and Stephen W. Brooks did participate in compensation deliberations and decisions with respect to other executive officers.

**Limited Liability of Officers and Directors**

The Delaware Supreme Court has held that a directors' duty of care to a corporation and its stockholders requires the exercise of an informed business judgment. Having become informed of all material information reasonably available to them, directors must act with requisite care in the discharge of their duties. The Delaware general corporation law permits a corporation through its certificate of incorporation to exonerate its directors from personal liability to the corporation or its stockholders for monetary damages for breach of the fiduciary duty of care as a director, with certain exceptions. The exceptions include a breach of the directors' duty of loyalty, acts or omissions not in good faith or which involve intentional misconduct or knowing violations of law, improper declarations of dividends and transactions from which the directors derived an improper personal benefit. The Company's certificate of incorporation exonerates its directors, acting in such capacity, from monetary liability to the extent permitted by this statutory provision. The limitation of liability provision does not eliminate a stockholder's right to seek non-monetary, equitable remedies such as injunction

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or rescission to redress an action taken by directors. However, as a practical matter, equitable remedies may not be available in all situations and there may be instances in which no effective remedy is available.

**SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Securities Exchange Act of 1934 requires AERT's executive officers and directors, and persons who own more than ten-percent of a registered class of the Company's securities to file reports of ownership and changes in ownership with the Securities and Exchange Commission and National Association of Securities Dealers. Officers, directors and greater than ten-percent shareholders are required by SEC regulation to furnish the Company with copies of all forms filed pursuant to Section 16(a). Based on a review of the copies of such forms received by it and written representations from certain reporting persons that no Forms 4 or Forms 5 were required for those persons, the Company believes that during the fiscal year ended December 31, 2005; all Section 16(a) filing requirements were met, except as described below. Marjorie Brooks, director, filed two late Form 4 reports for two transactions related to a stock option exercise and an issuance of common stock in payment of the yearly premium on preferred stock. Melinda Davis, director, filed one late Form 4 report for one transaction related to an issuance of common stock in payment of the yearly premium on preferred stock. Samuel L. Milbank, director, filed two late Form 4 reports for six transactions related to an issuance of common stock in payment of the yearly premium on preferred stock and sales of common stock. Sal Miwa, director, filed one late Form 4 report for two transactions related to a stock option exercise and the a sale of common stock. Jim Robason, director, filed one late Form 4 report for one transaction related to an issuance of common stock in payment of the yearly premium on preferred stock. Robert Thayer, senior vice-president and chief financial officer, failed to file until 2006 one Form 3 to report his initial ownership of Company securities. Michael Tull, director, failed to file until 2006 one Form 4 report for one transaction related to an issuance of common stock in payment of the yearly premium on preferred stock. The Company was authorized and given the responsibility by its directors and officers to file for each of them the necessary Form 3 and Form 4 reports with the SEC, and the Company was at fault for the late filings listed above. The Company has put procedures in place to prevent such late filings in the future.

**CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

During 2005 and the first quarter of 2006, the Company had an agreement with Brooks Investment Co., controlled by Marjorie S. Brooks, which allowed the Company to transfer as collateral certain of its trade receivables, which Brooks Investment Co. deemed acceptable, up to \$4.0 million at any one time. Upon acceptance of a transfer of a receivable, Brooks Investment Co. remitted to the Company 85% of the receivable, as defined in the agreement. Upon collection of the receivable, the Company remitted to Brooks Investment Co. 1.25% of the receivable as a factoring charge, and the remaining receivable, less interest costs, which were based on the time period over which the receivable was outstanding, was remitted to the Company. The Company indemnified Brooks Investment Co. for any loss arising out of rejections or returns of any merchandise, or any claims asserted by the Company's customers.

During 2005, the Company transferred an aggregate of approximately \$89.5 million in receivables under this agreement, of which \$3.0 million remained to be collected as of December 31, 2005. During 2004 and 2003, the Company transferred an aggregate of approximately \$65.9 million and \$45.0 million, respectively, in receivables under this agreement, none of which remains to be collected. During 2005, Brooks Investment Co. provided a rebate of factoring costs in the amount of \$450,000, resulting in total factoring costs of \$669,718, which were included in selling and administrative costs at December 31, 2005. Cost of \$826,248 and \$512,233 associated with the factoring agreement were included in selling and administrative costs at December 31, 2004 and 2003, respectively. Accounts payable to related parties at December 31, 2005 and 2004, included \$2,450,788 and \$2,097,553, respectively, as a result of this agreement. The Company terminated this agreement on April 1, 2006, and has put in its place a \$15 million asset-based bank line of credit.

The Company employs the services of a related party, Tull Sales, Inc., as an outside sales representative. Tull Sales is owned by Michael M. Tull, one of our directors. Commissions paid to Tull Sales were \$677,794 in 2005, \$643,570 in 2004 and \$351,032 in 2003.

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In addition to the related transactions discussed above, members of the Brooks family provide the following to the Company without receiving any financial consideration:

Marjorie S. Brooks personally guaranteed repayment of up to \$4 million of the 2003 bonds and \$15 million of the bank line of credit;

Joe G. Brooks personally guarantees repayment of the Company's American Express account, the outstanding balance of which is sometimes in excess of \$100,000; and,

Joe G. Brooks personally guarantees repayment of the Company's automobile loans, which had a balance of \$71,068 at December 31, 2005.

At December 31, 2005, accounts payable-related parties included the following amounts:

Advances on factored receivables of approximately \$2.45 million assigned to Brooks Investment Co.,

Sales commissions of approximately \$84,000 owed to Tull Sales Co., which is owned by Michael M. Tull, one of our directors, and director compensation of \$3,750 owed to Mr. Tull,

Deferred compensation of \$90,500 owed to Stephen W. Brooks, one of our co-ces,

Deferred compensation of \$169,622 and out-of-pocket expenses of \$15,000 owed to Joe G. Brooks, our chairman and co-ceo,

Director compensation of \$3,750 and consulting fees of \$112,000 owed to Jim Robason, one of our directors, and

Other items owed to related parties of approximately \$77,000.

**Table of Contents****STOCKHOLDER RETURN PERFORMANCE GRAPH**

This graph shows the Company's cumulative total stockholder return during the last five fiscal years ended December 31, 2005, with the cumulative total returns of the Hemscoff Industry Group 63-Materials and Construction and the Nasdaq Market Index. The comparison assumes \$100 was invested on December 31, 2000 in AERT common stock and in each of the indices shown and assumes that all of the dividends were reinvested.

**COMPARE 5-YEAR CUMULATIVE TOTAL RETURN  
AMONG ADVANCED ENVIRONMENTAL RECYCLING TECHNOLOGIES, INC.,  
NASDAQ MARKET INDEX AND PEER GROUP INDEX  
ASSUMES \$100 INVESTED DECEMBER 31, 2000  
ASSUMES DIVIDEND REINVESTED  
FISCAL YEAR ENDING DECEMBER 31, 2005**

	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>
Advanced Environmental	\$ 100.00	153.33	160.00	209.33	169.33	238.67
Materials and Construction	\$ 100.00	112.60	97.91	146.29	184.49	215.00
Nasdaq Market Value Index	\$ 100.00	79.71	55.60	83.60	90.63	92.62

**Table of Contents****INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM****Fees**

The information below sets forth the fees charged by Tullius Taylor Sartain & Sartain LLP during 2005 and 2004 for services provided to the Company in the following categories and amounts:

	2005	2004
Audit fees	\$ 119,250	\$ 81,500
Audit-related fees	24,500	8,500
Tax fees	7,805	
All other fees		
<b>Total</b>	<b>\$ 151,555</b>	<b>\$ 90,000</b>

**Pre-Approval Policy**

All of TTS&S's fees for 2005 and 2004 were pre-approved by the audit committee through a formal engagement letter with TTS&S. The audit committee's policy is to pre-approve all services by AERT's independent accountants.

**Item 1: Election of Directors**

The Company currently has eleven directors that are to be elected by the holders of shares of outstanding Class A and Class B common stock and Series B preferred stock voting together as a single class. To be elected, each director must receive a plurality of the votes cast at the annual meeting. All directors serve for a term of one year and until their successors are duly elected and qualified. Each outstanding share of Class A common stock entitles the holder thereof to one vote with respect to the election of each of the eleven director positions to be filled, each outstanding share of Class B common stock entitles the holder thereof to five votes with respect to the election of each of the eleven director positions to be filled.

The enclosed form of proxy provides a method for stockholders to withhold authority to vote for any one or more of the nominees for director while granting authority to vote for the remaining nominees. If you wish to grant authority to vote for all nominees, check the box marked **FOR**. If you wish to withhold authority to vote for all nominees, check the box marked **WITHHOLD**. If you wish your shares to be voted for some nominees and not for one or more of the others, check the box marked **FOR** and indicate the names(s) of the nominee(s) for whom you are withholding the authority to vote by drawing a line through the name(s) of such nominee(s). If you withhold authority to vote your shares, such vote will be treated as an abstention and, accordingly, your shares will neither be voted for or against a director but will be counted for quorum purposes.

The eleven nominees for director are: Joe G. Brooks, Marjorie S. Brooks, Stephen W. Brooks, Jerry B. Burkett, Edward P. Carda, Melinda Davis, Tim W. Kizer, Samuel L. Milbank, Sal Miwa, Jim Robason and Michael M. Tull. Currently, Joe G. Brooks is chairman, co-chief executive officer and president, Sal Miwa is vice-chairman of the board, Stephen W. Brooks is co-chief executive officer and Marjorie S. Brooks is secretary and treasurer.

**THE BOARD UNANIMOUSLY RECOMMENDS THAT THE STOCKHOLDERS VOTE IN FAVOR OF THE ELEVEN NOMINEES NAMED ABOVE. PROXY CARDS EXECUTED AND RETURNED WILL BE SO VOTED UNLESS CONTRARY INSTRUCTIONS ARE INDICATED THEREON.**

In the event one or more nominees become unavailable for election, votes will be cast, pursuant to authority granted by the enclosed proxy, for such substitute nominees as may be designated by the board of directors. The board of directors has no reason to believe that any nominee will be unable to serve, if elected.

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**Item 2: *Ratification of Appointment of Independent Registered Public Accounting Firm***

**Introduction**

Subject to ratification by the stockholders, the board's audit committee has selected Tullius Taylor Sartain & Sartain LLP to be AERT's independent registered public accounting firm for the Company's fiscal year ending December 31, 2006. TT&S has acted as the Company's independent registered public accounting firm since 2001. The audit committee may terminate the appointment of TTS&S as independent registered public accounting firm without stockholder approval whenever the audit committee deems necessary or appropriate.

Representatives of TTS&S are expected to attend the annual meeting. They will have the opportunity to make a statement if they desire to do so and will be available to respond to appropriate questions from stockholders.

**Required Vote**

Ratification of the appointment of the independent registered public accounting firm requires the affirmative vote of a majority of the voting power present (in person or by proxy) and entitled to vote at the meeting. In the event that the Company's stockholders fail to ratify the appointment of TTS&S, the selection of the Company's independent registered public accounting firm will be submitted to the Company's audit committee for reconsideration.

THE BOARD UNANIMOUSLY RECOMMENDS A VOTE FOR RATIFICATION OF THE APPOINTMENT OF THE INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM. PROXY CARDS EXECUTED AND RETURNED WILL BE SO VOTED UNLESS CONTRARY INSTRUCTIONS ARE INDICATED THEREON.

**COST AND METHOD OF PROXY SOLICITATION**

The Company will pay the cost of proxy solicitation. In addition to solicitation by mail, arrangements will be made with brokers and other custodians, nominees and fiduciaries to send proxies and proxy material to their principals and the Company will, upon request, reimburse them for their reasonable expenses in so doing. Officers and other regular employees of the Company may, if necessary, request the return of proxies by mail, telephone, Internet or in person.

**ADDITIONAL INFORMATION AVAILABLE**

Upon written request of any stockholder, the Company will furnish, without charge, a copy of the Company's 2005 annual report on Form 10-K, as filed with the SEC, including the financial statements and schedules. The written request should be sent to the secretary, at the Company's executive office. The written request must state that, as of April 12, 2006, the person making the request was a beneficial owner of capital stock of the Company.

The SEC has adopted rules that permit companies and intermediaries such as brokers to satisfy delivery requirements for proxy statements with respect to two or more stockholders sharing the same address by delivering a single proxy statement addressed to those stockholders. This process, which is commonly referred to as "householding," potentially provides extra convenience for stockholders and cost savings for companies. The Company and some brokers household proxy materials, delivering a single proxy statement to multiple stockholders sharing an address unless contrary instructions have been received from the affected stockholders. Once you have received notice from your broker or the Company that they or the Company will be householding materials to your address, householding will continue until you are notified otherwise or until you revoke your consent. If, at any time, you no longer wish to participate in householding and would prefer to receive a separate proxy statement, please notify your broker if your shares are held in a brokerage account or the Company if you hold registered shares. You can notify the Company by sending a written request to

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Marjorie S. Brooks, secretary of the Company, Post Office Box 1237, Springdale, Arkansas 72765, by registered, certified, or express mail.

**STOCKHOLDER PROPOSALS FOR THE ANNUAL MEETING IN 2006**

If you want to present a proposal for possible inclusion in the Company's proxy statement for the annual meeting of stockholders in 2007, you may do so by following the procedures described in SEC Rule 14a-8 by sending the proposal to Marjorie S. Brooks, secretary of the Company, Post Office Box 1237, Springdale, Arkansas 72765, by registered, certified or express mail. Proposals must be received on or before December 28, 2006. **This date is determined by the board and is based on SEC Rule 14a-8, which states proposals for a regularly scheduled annual meeting must be received at the Company's principal executive offices not less than 120 calendar days before the release date of the previous year's annual meeting proxy statement.**

**OTHER MATTERS**

The board does not intend to present any items of business other than those stated in the Notice of Annual Meeting of Stockholders. If other matters are properly brought before the meeting, the persons named in the proxy will vote the shares represented by it in accordance with their best judgment. Discretionary authority to vote on other matters is included in the proxy.

The foregoing Notice and Proxy Statement are sent by order of the board of directors.

Joe G. Brooks  
*Chairman*

Dated: April 28, 2006

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**ADVANCED ENVIRONMENTAL RECYCLING TECHNOLOGIES, INC.  
THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS  
FOR THE ANNUAL MEETING OF STOCKHOLDERS ON JUNE 8, 2006**

The undersigned hereby appoints Joe G. Brooks, as proxy, with full power to appoint his substitute, and hereby authorizes such proxy to represent and vote, as designated on this proxy, all shares of common stock of Advanced Environmental Recycling Technologies, Inc. held of record by the undersigned on the record date April 12, 2006 at the annual meeting of stockholders of the Company to be held at the Northwest Arkansas Holiday Inn Convention Center, Springdale, Arkansas on Thursday, June 8, 2006 at 7:00 p.m., local time, and at any adjournment thereof. **This proxy, when properly executed, will be voted in the manner directed herein. If no direction is made, this proxy will be voted FOR Items 1 and 2. In his discretion, the proxy is authorized to vote upon such other business as may properly come before the meeting.**

**(Continued and to be signed on reverse side)**

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**ANNUAL MEETING OF STOCKHOLDERS OF  
Advanced Environmental Recycling Technologies, Inc.  
June 8, 2006  
PROXY VOTING INSTRUCTIONS**

**MAIL** Date, sign and mail your proxy card in the envelope provided as soon as possible.

-OR-

**TELEPHONE** Call toll-free **1-800-PROXIES** from any touch-tone telephone and follow the instructions.

Have your control number and proxy card available when you call.

-OR-

**INTERNET** Access www.voteproxy.com and follow the on-screen instructions.

Have your proxy card available when you access the web page.

You may enter your voting instructions at 1-800-PROXIES or www.voteproxy.com up until 11:59 PM Eastern Time the day before the cut-off or meeting date.

Please detach along perforated line and mail in the envelope provided **IF** you are not voting via telephone or Internet. **PLEASE SIGN, DATE AND RETURN PROMPTLY IN THE ENCLOSED ENVELOPE. PLEASE MARK YOUR VOTE IN BLUE OR BLACK INK AS SHOWN HERE X**

1. Election of Directors
  - o FOR ALL NOMINEES
  - o WITHHOLD AUTHORITY  
FOR ALL NOMINEES
  - o FOR ALL EXCEPT  
(See Instructions below)

Nominees:

- o Joe G. Brooks
- o Marjorie S. Brooks
- o Stephen W. Brooks
- o Jerry B. Burkett
- o Edward P. Carda
- o Melinda Davis
- o Tim W. Kizer
- o Samuel L. Milbank
- o Sal Miwa
- o Jim Robason
- o Michael M. Tull

INSTRUCTION: To withhold authority to vote for any individual nominee(s), mark **FOR ALL EXCEPT** and fill in the circle next to each nominee you wish to withhold, as shown here: o

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- 2. Ratification of Tullius Taylor Sartain & Sartain LLP, independent registered public accountants, as the Company's auditors.

For	Against	Abstain
<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

The undersigned acknowledges receipt of the formal notice of such meeting and the 2005 Annual Report of the Company.

New Address: \_\_\_\_\_

To change the address on your account, please check the box at right and indicate your new address in the address space above. Please note that changes to the registered name(s) on the account may not be submitted via this method.

Signature: \_\_\_\_\_ Date: \_\_\_\_\_, 2006      Signature: \_\_\_\_\_ Date: \_\_\_\_\_, 2006

Note: Please sign above exactly as name appears on this proxy. When shares are held by jointly, each holder should sign. When signing as attorney, administrator, trustee, or guardian, please give full name as such. If the signer is a corporation, please sign full corporate name by duly authorized officer, giving full title as such. If signer is a partnership, please sign in partnership name by authorized person.