



24 Hours/day (612) 441-3440 Fax (612) 441-7174

Internet: SolarAttic@aol.com

****This is a copy of the stockholder's update letter dated: July 15, 1996****

Dear Investor:

Stockholder's Update

It has been awhile since my last update. This letter will bring you up to speed on our operations. An unaudited P&L statement and Balance Sheet are included for your review. They cover the first half of 1996.

Operations Summary

SolarAttic is still primarily in a developmental mode working in two key areas. A) We are prosecuting the fourth patent application covering our new duct technology with the U.S. Patent & Trademark Office. Initial international filing must be completed prior to October 5th if we are going to file internationally. Yes, we now expect the fourth U.S. Patent by the end of 1996! [see discussion below] B) We are working to complete the combination space heater-ventilator product that was presented at last years Minnesota State Fair. This is a product that a lot of people wanted to immediately purchase! It combines our space and duct technologies into a single year-around product! It will vent the attic in the winter & summer and grab the free solar heat in the fall & spring for space heating. Having said this about developmental issues, SolarAttic is also in a limited sales & manufacturing mode for "word-of-mouth" pool heater inquiries. And, the company is working aggressively to ramp up its marketing operations in order to "drive" our pool heater sales [see below].

Marketing & Sales Front

Inquiries Processed & Direct Sales

132 product inquiries were processed during the first six months. This compares with 316 for the first half of 1995 which benefited from the Jim Dulley pool heating article published in April of 1995. Still, twenty pool heating systems and one space heating system have been sold. This puts our 1996 sales roughly on par with last years word-of-mouth sales despite the lower number of inquiries being processed.

Marketing & Sales Filter

One of the more fascinating marketing & sales issues to think about is our experience to date and the ratio of sales that are associated with Jim Dulley's 1995 article. Jim Dulley has told me that he sent out between 2,000 - 3,000 of his utility update #955.

His article featured three types of solar pool heaters. We were only one. The other two highlighted were solar pool deck heaters and solar panel pool heaters. The graphic which was included in some papers [i.e. LA Times] was a direct benefit to us. However, there is no way of knowing which papers included the graphic and which didn't. There is also no way of knowing how many pool owners actually saw the article and were inspired to take action. For example, if 10,000 pool owners saw the information and only 3,000 took action, it means one thing (one type of filter). If, on the other hand, only 3,000 pool owners saw the article and all 3,000 took action—it would mean something entirely different.

For our analysis, we will assume that all 3,000 inquiries that Dulley received were for our product information (worse case scenario). We'll also assume that only 3,000 pool owners saw the article (a guess). To date, we have received 346 inquiries from those who received Jim Dulley's Update #955 ($346 \div 3000 = 11.5\%$). This means that 11.5% who saw our information in Dulley's utility update #955 were also motivated to contact us about the product. Of the 346 who contacted us, 36 sales were made ($36 \div 346 = 10.4\%$). This means that we are currently running a 10.4% direct mail sales rate on a \$1800 product from a relatively obscure company (us) against those inquiries whose source was update #955.

Of the 132 product inquiries received during the first six months of 1996, we have had 13 direct sales. Again, 10%. Note: The balance of the 1996 sales were from prior inquiries.

Why do I mention these percentages? Well, for openers, a 1% direct mail response rate for any product would be considered great by most direct mail marketers. What's happening with us? Are we really running 10%? What does this information mean to SolarAttic?

Stepanek Inground Pool List

On April 22, we acquired a marketing list of 600,000 inground pool addresses from Frank N. Stepanek, Jr. of Tully, New York in exchange for common stock in our company. The typed list occupies a full 4 drawer file cabinet and is organized by Nielsen's DMA markets. Frank is an accredited investor who is now retiring from the pool industry. He has over 35 years of industry marketing experience and believes that our pool heater is going to be a real winner. In addition to the inground pool list, Frank has also supplied us with a typed list of 16,000 pool industry retailers, 40,000 commercial pool addresses and industry marketing profiles of Nielsen's DMA markets. Frank's industry data provides us with a very powerful direct marketing sales tool.

Main Computer Crash Leads To Expanded System

On April 25, the main computer for the business died abruptly. I just pushed the power on button and it was gone (non-functional). After weeks of rebuilding and reorganizing the office, we are again fully operational with an expanded computer system that is ready for a full-time direct mail marketing and sales effort using the Stepanek list. None of our files were lost. Today, our computer system has built in redundancy that ensures we won't—ever again—have to go through the grief we just went through.

Computer Databases Being Built

Both the inground pool list and the dealer list are being inputted into computer databases for this upcoming direct marketing & sales effort. The inground pool database is currently growing at the rate of about 1,000 inground pool addresses per week. The dealer list is growing at the rate of about 500 retailers per week. Yes, it will take a considerable effort to get all of this information computerized. However, we plan to input the inground pool addresses selectively by geographical area and start direct marketing ASAP.

That Marketing Filter. What Percentage Direct Mail Rate Is It?

Back to that 10.4% direct mail response rate for our inquiries. It is clear that Dulley sent 3000 updates (maximum) of which we received 346 inquiries and 36 sales. (3000—346—36). This could be $36 \div 346 = 10.4\%$ sales rate or it could be $36 \div 3000 = 1.2\%$ sales rate. Or, it could be (X—3000—346—36) where X represents more pool owners who saw our information than the 3000 who asked Dulley to send information. A greater population X would decrease the overall direct mail sales rate. Or, if Dulley only sent 2000 updates, it could be interpreted as $36 \div 2000 = 1.8\%$ or an increased response rate.

One thing we know for sure is that our response rate for these types of inquiries has been historically consistent. We have an accurate database that has followed our limited sales activity closely. Jim Dulley has published an article three times over the last several years. The quality of the inquiries this third time was very high and the quantity of inquiries was actually 1/2 of the two prior times in which price was not mentioned.

So what? What does this all mean to SolarAttic? Assume for the moment that we could experience a 1.2% response rate against the population of inground pools. Since we now have on file over 600,000 inground pool addresses, it COULD mean the following:

$$\text{Unit Sales} = 600,000 \text{ Inground Pools} \times 1.2\% \text{ DM Rate} = 7200$$

$$\text{Gross Sales Revenue } \$ = 7200 \text{ Unit Sales} \times \$1800 \text{ avg. sale} = \$12.96 \text{ Million}$$

The above calculations illustrate that every time we pass through this list of inground pools we could potentially get up to 7200 unit sales. It gets more exciting then that when you realize we can also obtain over 5,000,000 pool addresses from other industry sources.

Important Detail For Pool Industry Business Plan

Almost all of the assumptions have been tested in the business plan for the pool industry. The key remaining ingredient is the actual direct mail response rate against a blind population list of inground pools. One in which we only have the address and in which we do not know who the pool owner is. For example, if we sent out 1000 direct mail pieces to blind addresses of inground pools, could we expect $1000 \times 1.2\%$ or 12 sales??? Historical sales data suggests that we could expect exactly this.

The Stepanek Pool List gives us the opportunity to test and resolve this business plan assumption. It gives us the opportunity to accurately define the response rate using direct mail techniques. Once pinpointed, we can then accurately plan the growth of our sales and our business expansion within this industry.

Direct Mail Marketing To "DRIVE BUSINESS" Starts Soon

We now expect to begin direct mail marketing efforts against the inground pool list sometime in the next few months. The direct mail materials need to be created first. And, this effort has to be intermixed with other critical business priorities. We are still "juggling" and "pacing" due to limited financial resources.

Prices & Margins

Prices were increased in February so gross profit margins on sales have risen from 49.5% to 50.2% (See enclosed P&L Statement). However, one pool heating system was provided free of charge to the individual who purchased the very first pool heater.

This was an attempt to recover the first PCS1 which was damaged during shipment in 1988 but was placed on-line for 6-7 years of service anyway. Taking into account this giveaway, our gross profit margin on sales for the first six months of 1996 was actually 55.5%.

Dealers Coming Onboard

Four of the twenty sales in the first half were installed through dealers. We now have a dealer selling product in both Oregon and Texas. In addition, a dealer is almost operational in Orlando, Florida. The Orlando operation is expected to be on-line by this Fall. There is also an active effort in the Phoenix, Arizona area and in Maryland near Washington, D.C. to establish dealer operations. I believe we have hit a critical milestone and there appears to be a more receptive attitude in potential dealers that we are talking with.

Business Opportunity Ad

Due to limited financial resources, no direct product advertising has been conducted yet. However, we had placed a 1" business opportunity ad in the marketplace section of STARTUPS magazine. It was designed to create interest from prospective dealers. It was canceled when the nature of the inquiries was determined to be different than anticipated. Instead of getting prospective dealer inquiries, we only received product or technology inquiries. Since we acquired the pool list, it is now more advantageous for us to launch into a direct mail marketing operation to pool owners Vs immediately seeking dealers. It's the fastest way to increase our revenues. The dealer network will follow later.

Locating Installer Works

We have the ability to locate a dealer in a specific area. An installer is very important for many people. Some people need an installer identified prior to purchase and others will buy and take a chance without one. We have matched buyer & installer successfully several times. A sale that needs an installer gives us a convenient excuse to contact dealers within that area. We find that dealers are very receptive to installing our product. It is a very low-risk way for them to explore our business opportunity. This is exactly how we identified our Texas installer. First, he installed a system we sold. Then he sold a system himself!

Dealer Interest Predictable

Frank Stepanek has predicted, from his 35 years of industry experience, the point at which pool industry dealers will become aggressively interested in our pool heater. It is when we have reached an annual production of 2500 units and we are moving towards 10,000.

PCS1 Now In 29 States

This year, the SolarAttic pool heater has been shipped into two new states. Washington (on the desert side) and Oregon. The PCS1 pool heater is now in 29 states.

New Product Testimonials

More product testimonials on the PCS1 have been received during 1996 from:

Phoenix, Arizona
Brooksville, Florida
Orlando, Florida
Shalimar, Florida
Titusville, Florida
Edison, New Jersey

Redding, California
Long Beach, California
Thousand Oaks, California
Slidell, Louisiana
Warren (Detroit area) Michigan

The Edison, New Jersey customer likes our pool heater so much that he has stated that he plans to take it with him when he moves. He has used the PCS1 for several years and has given us a written testimonial. The Detroit customer replaced his solar panel system with our PCS1 when he reroofed his house. Most of the above testimonials are verbal. We are tracking them and have a continuing effort towards converting them into written form.

Minnesota State Fair

SolarAttic will again be in the Home Improvement Building during the Minnesota State Fair. This is from August 22 through September 2. We expect to present our new combination space heater and ventilator product. We expect this to be the initial preproduction version and we expect to be able to immediately start selling this product. COME AND VISIT US AT THE STATE FAIR. It is a great time for you to get to meet and talk with us personally!

Space Heater-Ventilator Product

The public's reaction last year to the prototype we presented at the fair was overwhelming. It was clear that this product concept was accepted. It contrasts with the space heater by itself which was hard for the public (in Minnesota) to grasp. We expect that this product will eventually be sold in mass quantities to stores like Home Depot, etc.

Why am I telling you all of this about marketing & sales?

It's because SolarAttic is alive, well and moving in the right direction. We are still gathering a head of steam. And, we are pushing sales as hard and as fast as our limited financial & personnel resources will allow. Within the constraints of the various priorities the company has! After our main developmental efforts are out of our way later this year, we expect to accelerate marketing and sales efforts. This would be the first quarter of next year. Or, in the advent of some additional material resources (as in serious financial \$), we are prepared to accelerate these sales efforts sooner than later.

“And let us not grow weary while doing good, for in due season we shall reap if we do not lose heart.” Galatians 6:9 "And, you have persevered and have patience, and have labored for My name's sake and have not become weary.” Revelations 2:3 NKJ

Fourth U. S. Patent Is Coming

SolarAttic is actively prosecuting the fourth patent application. We have just received the second response from the Patent Office. Once again, our claims “as written” were denied—BUT—the Patent Office has acknowledged we have patentable material. The following excerpt is what the Patent Examiner has said on this “allowable” subject:

Serial Number: 08/528,720
Art Unit: 3404

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Allowable Subject Matter

7. Claim 18 would be allowable if rewritten to overcome the rejection under 35 U.S.C. 112 and to include all of the limitations of the base claim and any intervening claims.

What does this mean to SolarAttic? It means that we can now expect a “Notice of Allowance” for our fourth U.S. Patent by the end of the year. The Patent could be issued by the end of the year or during the first quarter of 1997.

However, we still have some minor obstacles to deal with. First, we have to rewrite the claim(s) to overcome the Patent Examiner’s objections. Second, we need to review closely the examiner’s arguments. Since this is an intellectual debate, it may be possible for SolarAttic to argue other new and/or additional claims language. In other words, even though the examiner has stated he would allow a certain claims language, there may be some other or additional language more favorable for SolarAttic that is acceptable.

Larry Garde, one of our directors, is the creative genius behind our patent claims language. Larry will be evaluating the examiners remarks and patent references closely. I’m confident that we can identify the most creative way to respond in order to maximize the value of this fourth patent. We now have about 2 1/2 months to respond to the examiner’s remarks.

It is this fourth patent that expands our markets in the U.S. from approximately \$600 Million to over \$3 BILLION. And, Worldwide, takes them to over \$10 BILLION in size. It is this fourth patent that gives SolarAttic the clear ability to reach \$100 Million in revenues Vs being limited to around \$30-40 Million. Hold on to your hat, we are headed in the right direction. And, in the near future, SolarAttic’s revenues can be expected to explode!

Space Issues

SolarAttic is actively reviewing industrial space options in the Elk River area. At the moment, available industrial space in the area is rather limited. We also do not have the resources to lease any substantive industrial space. However, we are looking forward to moving out of the garage and basement as soon as those resources become available.

In the interim, we have expanded and reorganized the office and manufacturing area at my residence. We have also moved some stuff into a newly built shed and a mini storage area in Elk River. The end result is more marketing production & manufacturing space.

This has been done in anticipation of a more aggressive marketing & sales efforts this fall. This is the first step towards expanding our operations and also moving them out of the garage. Feel free to call and make an appointment to visit our office and production area.

New Sheet Metal Vendor

One of the major obstacles we had to overcome earlier this year is finding a new sheet metal vendor for our sheet metal parts. Aljon Tool became a 100% AT&T vendor last year and “dumped” a few little guys like SolarAttic. We then wound up doing business with an Alexandria company but the parts were less than desirable. We found Marksman Metals, Inc. of St. Michael, Minnesota early this year. I’m happy to report that the quality of their parts are very high and SolarAttic is looking forward to a long and prosperous relationship.

IPO Analysis

SolarAttic has had its Minnesota IPO file reviewed by an attorney. In conclusion, the attorney states: “SolarAttic does appear to have a valid argument that the Agency engaged in improper rule making However, its sole remedy appears to be in the form of injunctive and/or declaratory relief”

In our IPO plan, there was no way we could have forecasted that the Minnesota Securities Registration Division would not follow the State’s written rule of law. Nor could we have forecasted that the Securities Division would actually work against our IPO in a rather aggressively bureaucratic way. But, that is exactly what happened to SolarAttic.

As we proceed towards another IPO attempt in the near future, several issues still need to be examined in order to predict with greater certainty—the State’s regulatory response. A few things are clear: A) SolarAttic cannot count on the State to obey its own securities regulations; B) Some state securities laws are not published; C) SolarAttic cannot count on the Securities Registration Division to obey the State’s Administrative Procedures Act; and, D) SolarAttic can expect to deal with state bureaucrats that have anti-business mentalities.

These were the facts that occurred during our first IPO attempt. SolarAttic, at the very least, must be prepared to seek “injunctive and/or declaratory relief” if needed. Having said this, I have been assured by the State’s Securities Director that some internal changes have been made. Further, he has offered his office’s help in our next attempt at a public offering.

SCOR IPO Being Explored

Since our failed IPO attempt, major regulatory changes have taken place. Perhaps the biggest is the SCOR U-7 IPO. SCOR stands for **S**mall **C**ompany **O**ffering **R**egistration. The SEC has developed this program which uses a standard Form U-7 for its filing. Under this new program, a company can raise up to \$1 Million without having to file anything with the SEC. There are no SEC quarterly or annual filings (unless we have 500+ stockholders) and audited financials are not required. So far, an estimated 43 of the 50 states have signed up to accept SCOR filings. I do not believe Minnesota is one of these states. In addition, if the stock is priced at \$5.00 or more per share, it can be traded on the Pacific Stock Exchange.

The SEC has also sanctioned INTERNET trading of a company’s stock. What’s it all mean to us? Well, I have all of the SCOR materials on hand for review and will be studying the issue over the next several months. It does appear, however, that we could probably “test the waters” on the INTERNET for our next IPO. In doing so, we could locate all of the investors. Kind of presell the IPO if you’d like. Then do the appropriate state filings!

IPO Timing

The earliest attempt at another IPO would probably be next spring. The issue is still being assessed and is not yet being planned. However, it is clear that we have some considerably less expensive options available at this time. I'll keep you posted.

Financial Commentary

****See the attached Unaudited Financial Statements****

Table 1: Three Key Measurements

Measurement	6/30/95	6/30/96	Change
Stockholder's Equity	\$43,837	\$148,159	Increased \$104,322 Up 338% Improvement
Total Liabilities	78,783	32,984	Decreased \$45,799 Down 58% Improvement
Officer Loan Account	33,442	45,595	Increased \$12,153

Note 1: The increase in the officer loan account over the last twelve months was loaned to Mr. Palmer who is not paid a salary. The only paid employee is Jim Kantorowicz.

Note 2: Negative cash flow is defined as YTD Loss of \$23,182.72 less paper deductions of Amortization and Depreciation. Negative cash flow during the first six months of 1996 was therefore \$16,513 or 2,752 per month which the company has been able to offset with additional equity investments.

Note 3: Some expense accounts were combined to get the income statement on one page. I.E. - Auto expenses are actually broken down in four separate accounts. Utilities are broken down into several accounts.

Note 4: The expenses shown reflect the continued developmental nature of the company.

Note 5: These are unaudited financials and they are not GAAP adjusted (not required).

If you have any questions or would like to sit down with me and review any documents or our accounting records in detail, feel free to give me a call. I'll be happy to sit down and review them with you. All of our records are available for review at our corporate offices in Elk River. **THANK YOU for being a SolarAttic shareholder!**

Sincerely yours,



Edward G. Palmer
President

Balance Sheet

June 30, 1996

<u>Assets</u>		
<u>Current Assets</u>		
Cash 1	2,959.64	
Current Inventory	37,720.38	
Leasehold Improvement	1,707.00	
Officer Loan	45,595.16	
Prepaid Expenses	<u>7,300.00</u>	
Total Current Assets		95,282.18
<u>Fixed Assets</u>		
Accumulated Amortization	(25,946.42)	
Accumulated Depreciation	(22,649.02)	
Computer Hardware	26,136.27	
New Machinery & Equipment	4,385.94	
Office Equipment & Fixtures	5,133.05	
Signs & Displays	4,301.46	
Stepanek Pool List	33,000.00	
U.S. Patent Re. 32,607	61,200.00	
Used Machinery & Equipment	<u>300.00</u>	
Total Fixed Assets		<u>85,861.28</u>
Total Assets		<u><u>181,143.46</u></u>
<u>Liabilities</u>		
<u>Current Liabilities</u>		
Accounts Payable	(409.60)	
Accrued Payroll Taxes	417.53	
Accrued Use Tax	247.68	
Accrued Interest	345.59	
Community Credit	25,568.25	
Credit Card	<u>6,811.11</u>	
Total Current Liabilities		32,984.36
<u>Long-term Liabilities</u>		<u>0.00</u>
Total Liabilities		32,984.36
<u>Owners Equity</u>		
<u>Equity Accounts</u>		
Common Stock (NO PAR)	519,722.60	
Retained Earnings	(348,380.78)	
Net Income YTD 1996	<u>(23,182.72)</u>	
Total Equity Accounts		<u>148,159.10</u>
Total Liabilities and Owners Equity		<u><u>181,143.46</u></u>

Income Statement

1st Half 1996

Net Sales		35,120.46
Cost of Goods Sold		
Opening Inventory	34,300.50	
Purchases	20,289.48	
Freight Inbound	631.70	
Cost of Goods Available for Sale	55,221.68	
Less Current Inventory	<u>37,720.38</u>	
Cost of Goods Sold		<u>17,501.30</u>
Gross Profit		17,619.16
Expenses		
Accounting	91.93	
Advertising	192.00	
Amortization	4,741.14*	
Audio/CD/Video	297.35	
Auto	1,101.03	
Book	757.75	
Computer Supplies	540.59	
Depreciation	1,928.58*	
Dues	53.00	
Insurance	1,054.92	
Interest	2,624.71	
Legal	40.00	
Maintenance & Repairs	570.24	
Marketing	356.50	
Medical	706.18	
Mfr Dept Charge	41.83	
Mfr Supplies	1,214.90	
Office Supplies	2,177.47	
Online Services	396.97	
Payroll FICA	826.20	
Payroll FUTA	54.18	
Payroll SUTA	214.20	
Postage	491.89	
Printing	350.00	
R & D	3,045.00	
Rent	1,374.00	
Salaries & Wages	10,800.00	
Sales Dept Charge	146.61	
Software	392.49	
Subscriptions	303.69	
T & E (50%)	258.00	
Telephone & Long Distance	995.38	
Training	502.00	
Utilities	1,359.64	
VISA/MC/AMEX	<u>801.51</u>	
Total Expenses		<u>40,801.88</u>
Total Income from Operations		(23,182.72)