BROOKFIELD HOMES CORP
Form 10-Q
November 09, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2006
Commission File Number: 001 31524
BROOKFIELD HOMES CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

Delaware	**37-1446709**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
8500 Executive Park Avenue **Suite 300** **Fairfax, Virginia**	**22031**
(Address of Principal Executive Offices)	(Zip Code)

(703) 270-1700
(Registrant s Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

As of October 31, 2006, the registrant had outstanding 26,554,506 shares of its common stock, $0.01 par value per share.

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BROOKFIELD HOMES CORPORATION

The Company s independent registered chartered accountants have substantially completed their review of the financial statements that accompany this Form 10-Q as required by Rule 10 01(d) of Regulation S X. However, due to an outstanding SEC comment on segment disclosure, they are unable to finalize their review until this comment is resolved. See Note 8(g) to the unaudited Consolidated Financial Statements.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

BROOKFIELD HOMES CORPORATION
CONSOLIDATED BALANCE SHEETS

(all dollar amounts are in thousands of U.S. dollars)

	Note	*(Unaudited)* September 30, 2006	December 31, 2005
Assets			
Housing and land inventory	2	$ 1,049,544	$ 912,617
Investments in housing and land joint ventures	3	103,044	53,260
Consolidated land inventory not owned	2	16,925	22,100
Receivables and other assets	8	36,177	94,081
Cash and cash equivalents		12,421	198,411
Deferred income taxes		44,894	49,417
		$ 1,263,005	$ 1,329,886
Liabilities and Equity			
Project specific and other financings	8	$ 665,718	$ 691,410
Accounts payable and other liabilities	4	217,615	320,787
Minority interest	2	61,778	53,040
Preferred stock - 10,000,000 shares authorized, no shares issued			
Common 65,000,000 shares authorized, 32,073,781 shares issued (December 31, 2005 32,073,781 shares issued)		321	321
Additional paid-in-capital		146,730	146,249
Treasury stock, at cost 5,519,275 shares (December 31, 2005 4,695,600 shares)		(248,606)	(217,182)
Retained earnings		419,449	335,261
		$ 1,263,005	$ 1,329,886

See accompanying notes to financial statements

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BROOKFIELD HOMES CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(all dollar amounts are in thousands of U.S. dollars, except per share amounts)

		(Unaudited)			
		Three Months Ended September 30,		**Nine Months Ended September 30,**	
	Note	**2006**	**2005**	**2006**	**2005**
Revenue					
Housing		$ 160,025	$ 253,059	$ 475,530	$ 633,566
Land and other revenues		16,159	14,650	76,014	38,728
		176,184	267,709	551,544	672,294
Direct Cost of Sales	2	(125,322)	(186,319)	(375,507)	(466,854)
		50,862	81,390	176,037	205,440
Equity in earnings from housing and land joint ventures	3	11,204	15,658	12,874	25,249
Selling, general and administrative expense		(13,592)	(28,907)	(34,664)	(69,894)
Minority interest		(3,737)	(6,888)	(9,141)	(15,877)
Net Income Before Taxes		44,737	61,253	145,106	144,918
Income tax expense		(17,134)	(23,431)	(55,575)	(55,797)
Net Income		$ 27,603	$ 37,822	$ 89,531	$ 89,121
Earnings Per Share					
Basic	5	$ 1.04	$ 1.22	$ 3.32	$ 2.88
Diluted	5	$ 1.03	$ 1.20	$ 3.27	$ 2.83
Weighted Average Common Shares Outstanding *(in thousands)*					
Basic	5	26,572	30,931	26,981	30,932
Diluted	5	26,898	31,481	27,368	31,518

See accompanying notes to financial statements

BROOKFIELD HOMES CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY
(all dollar amounts are in thousands of U.S. dollars)

	(Unaudited) Nine Months Ended September 30, 2006	2005
Common Stock	$ 321	$ 321
Additional Paid-in Capital		
Opening balance	146,249	142,016
Stock option exercises	481	4,233
Ending balance	146,730	146,249
Treasury Stock		
Opening balance	(217,182)	(22,091)
Share repurchases	(37,922)	(9,521)
Stock option exercises	6,498	3,756
Ending balance	(248,606)	(27,856)
Retained Earnings		
Opening balance	335,261	125,870
Net income	89,531	89,121
Dividends	(5,343)	(4,968)
Ending balance	419,449	210,023
Total stockholders equity	$ 317,894	$ 328,737

See accompanying notes to financial statements

BROOKFIELD HOMES CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(all dollar amounts are in thousands of U.S. dollars)

	(Unaudited)			
	Three Months Ended September 30,		**Nine Months Ended September 30,**	
	2006	**2005**	**2006**	**2005**
Cash Flows From Operating Activities				
Net income	$ 27,603	$ 37,822	$ 89,531	$ 89,121
Adjustments to reconcile net income to net cash used in operating activities:				
(Undistributed)/distributed income from housing and land joint ventures	(10,977)	1,796	(9,987)	2,034
Minority interest	3,737	6,888	9,141	15,877
Deferred income taxes	898	(703)	4,676	(1,664)
Other changes in operating assets and liabilities:				
Decrease/(increase) in receivables and other assets	5,130	(19,192)	57,904	23,720
Increase in housing and land inventory	(46,852)	(61,469)	(138,478)	(206,359)
(Decrease)/increase in accounts payable and other	1,339	39,519	(79,808)	49,583
Net cash (used in)/provided by operating activities	(19,122)	4,661	(67,021)	(27,688)
Cash Flows From Investing Activities				
Investments in housing and land joint ventures	(30,424)	(19,498)	(49,515)	(29,176)
Recovery from housing and land joint ventures	3,088	456	9,718	29,362
Net cash (used in)/provided by investing activities	(27,336)	(19,042)	(39,797)	186
Cash Flows From Financing Activities				
Net (repayments)/borrowings under revolving project specific and other financings	(15,486)	55,184	(25,692)	78,638
Distributions to minority interest	(510)	(1,200)	(14,627)	(20,982)
Contributions from minority interest	1,359	656	4,248	8,898
Repurchase of common shares	(1,251)	(3,971)	(37,922)	(9,521)
Exercise of stock options			164	244
Dividends paid in cash			(5,343)	(4,968)
Net cash (used in)/provided by financing activities	(15,888)	50,669	(79,172)	52,309
(Decrease)/increase in cash and cash equivalents	(62,346)	36,288	(185,990)	24,807
Cash and cash equivalents at beginning of period	74,767	175,250	198,411	186,731
Cash and cash equivalents at end of period	$ 12,421	$ 211,538	$ 12,421	$ 211,538

Supplemental Cash Flow Information

Interest paid	$ 15,531	$ 9,935	$ 40,628	$ 26,547
Income taxes paid	$ 13,375	$ 20,900	$ 52,185	$ 64,895
Non-cash increase/(decrease) in consolidated land inventory not owned	$ 531	$ (13,102)	$ (6,726)	$ (26,407)

See accompanying notes to financial statements

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BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

Note 1. Significant Accounting Policies

(a) Basis of Presentation

Brookfield Homes Corporation (the Company or Brookfield Homes) was incorporated on August 28, 2002 as a wholly-owned subsidiary of Brookfield Properties Corporation (Brookfield Properties) to acquire as of October 1, 2002 all of the California and Washington D.C. Area homebuilding and land development operations (the Land and Housing Operations) of Brookfield Properties pursuant to a reorganization of its business (the Spin-off). On January 6, 2003, Brookfield Properties completed the Spin-off by distributing all of the issued and outstanding common stock it owned in the Company to its common stockholders. Brookfield Homes began trading as a separate company on the New York Stock Exchange on January 7, 2003.

The consolidated financial statements include the accounts of Brookfield Homes and its subsidiaries and investments in joint ventures and variable interests in which the Company is the primary beneficiary.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. Since they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements, they should be read in conjunction with the Company s consolidated financial statements and footnotes thereto included in the Company s annual report on Form 10-K for the year ended December 31, 2005. In the opinion of management, all adjustments necessary for fair presentation of the accompanying consolidated financial statements have been made.

The Company historically has experienced, and expects to continue to experience, variability in quarterly results. The consolidated statements of income for the three months and nine months ended September 30, 2006 are not necessarily indicative of the results to be expected for the full year.

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

(b) Earnings Per Share

Earnings per share is computed in accordance with Statement of Financial Accounting Standards (SFAS) 128. Basic earnings per share is calculated by dividing net income by the weighted average number of common shares outstanding for the period. Diluted earnings per share is calculated by dividing net income by the weighted average number of common shares outstanding including all dilutive potentially issuable shares under various stock option plans.

(c) Recent Accounting Pronouncements

In September 2006, the Securities and Exchange Commission staff (the SEC staff) issued Staff Accounting Bulletin No. 108 (SAB 108) regarding the process of qualifying financial statement misstatements. SAB 108 expresses the SEC staff s view regarding the diversity in practice in qualifying financial statement misstatements and the potential under current practice for the build-up of improper amounts on the balance sheet. SAB 108 is effective for fiscal years ending after November 15, 2006 (the Company s fiscal year ending December 31, 2006). The Company does not believe that SAB 108 will have a material impact on its consolidated financial statements.

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS 157. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement is effective for fiscal years beginning after November 15, 2007 (the Company s fiscal year beginning January 1, 2008), and interim periods within those fiscal years. The Company is currently reviewing the impact of this Statement on its consolidated financial statements.

In July 2006, FASB issued FASB Interpretation 48 (FIN 48), Accounting for Uncertainty in Income Taxes , which clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with FASB 109, Accounting for Income Taxes . This Interpretation provides guidance on the financial statement recognition and

BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

measurement of a tax position taken or expected to be taken in a tax return. In addition, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently reviewing the effect of this Interpretation on its consolidated financial statements.

In December 2004, FASB issued SFAS 123(R), Share-Based Payment. SFAS 123(R) establishes accounting standards for transactions in which a company exchanges its equity instruments for goods or services. In particular, this Statement requires companies to record compensation expense for all share-based payments, such as employee stock options, at fair market value. This Statement became effective January 1, 2006 for the Company and did not have a material impact on its consolidated financial statements. See Note 6, Stock-Based Compensation, for further discussion on share-based payments.

(d) Variable Interest Entities

In December 2003, FASB issued revised Interpretation 46 (FIN 46R), Consolidation of Variable Interest Entities (VIEs), an Interpretation of Accounting Research Bulletin 51, Consolidated Financial Statements, which replaces the previous version of FASB Interpretation 46 issued in January 2003 (FIN 46). The decision whether to consolidate a VIE begins with establishing that a VIE exists. A VIE exists when either the total equity investment at risk is not sufficient to permit the entity to finance its activities by itself, or the equity investor lacks one of three characteristics associated with owning a controlling financial interest. Those characteristics are the direct or indirect ability to make decisions about the entity s activities through voting rights or similar rights, the obligation to absorb the expected losses of an entity, and the right to receive the expected residual returns. The entity with the majority of the expected losses or expected residual return is considered to be the primary beneficiary of the entity and is required to consolidate such entity. The Company has determined that it is the primary beneficiary of certain VIEs which are presented in these financial statements under Consolidated land inventory not owned with the interest of others included in Minority interest. See Notes 2 and 3 for further discussion on the consolidation of land option contracts and joint ventures.

(e) Segment Information

The Company designs, constructs and sells a wide range of homes designed to meet the specific needs of each of its markets. For internal reporting purposes, the Company is organized into geographical housing and land regions. Because each of the Company s geographical housing and land regions has similar economic characteristics, housing products and class of prospective buyers, the geographic housing and land regions have been aggregated into a single housing and land segment in accordance with SFAS 131, Disclosure About Segments of an Enterprise and Related Information .

(f) Reclassification

Certain prior period amounts in the consolidated financial statements have been reclassified to conform with the September 30, 2006 presentation. In particular, Treasury Stock, Common Stock and Additional Paid-in Capital, which were previously presented in aggregate, have been presented as separate items in the Consolidated Balance Sheet and Consolidated Statement of Stockholders Equity.

BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

Note 2. Housing and Land Inventory

Housing and land inventory includes homes completed, homes under construction, lots ready for construction, model homes and land under and held for development which will be used in the Company s homebuilding operations or sold as building lots to other homebuilders. The following summarizes the components of housing and land inventory:

	September 30, 2006	December 31, 2005
Housing inventory	$ 478,205	$ 441,912
Model homes	33,366	20,837
Land and land under development	537,973	449,868
	$ 1,049,544	$ 912,617

The Company capitalizes interest which is expensed as housing units and building lots are sold. For the three months ended September 30, 2006 and 2005 and for the nine months ended September 30, 2006 and 2005, interest incurred and capitalized by the Company was $15.5 million and $9.9 million, $40.6 million and $26.5 million, respectively. Capitalized interest expensed for the same periods was $4.5 million, $6.6 million, $10.8 million, and $15.5 million, respectively.

Capitalized costs are expensed as costs of sales on a specific identification basis or on a relative value basis in proportion to anticipated revenue. Included in direct cost of sales is $118.2 million and $343.5 million of costs related to housing revenue for the three and nine months ended September 30, 2006 (September 30, 2005 $179.7 million and $447.1 million) and $7.1 million and $32.0 million of costs related to land sales and other revenues (September 30, 2005 $6.6 million and $19.7 million).

In the ordinary course of business, the Company has entered into a number of option contracts to acquire lots in the future in accordance with specific terms and conditions of such agreements. Under these option agreements, the Company will fund deposits to secure the right to purchase land or lots at a future point in time. The Company has evaluated its option contracts and determined that for those entities considered to be VIEs, it is the primary beneficiary of options for 568 lots with an aggregate exercise price of $16.9 million (December 31, 2005 577 lots with an aggregate exercise price of $22.1 million), which are required to be consolidated. In these cases, the only asset recorded is the Company s exercise price for the option to purchase, with an increase in minority interest of $11.5 million (December 31, 2005 $18.3 million) for the assumed third party investment in the VIE. Where the land sellers are not required to provide the Company financial information related to the VIE, certain assumptions by the Company were required in its assessment as to whether or not it is the primary beneficiary.

Housing and land inventory includes non-refundable deposits and other costs totaling $96.1 million (December 31, 2005 $58.3 million) in connection with options that are not required to be consolidated under the provisions of FIN 46R. The total exercise price of these options is $715.2 million (December 31, 2005 $720.6 million) including the non-refundable deposits identified above. The number of lots for which the Company has obtained an option to purchase, excluding those already consolidated, and their respective dates of expiry and their exercise price are as follows:

Year of Expiry	Number of Lots	Total Exercise Price
2006	3,105	$ 116,298
2007	5,351	173,162

2008	543	99,189
Thereafter	7,258	326,594
	16,257	$ 715,243

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(Tabular amounts in thousands of U.S. dollars except per share amounts)

The Company holds agreements for a further 3,590 acres of land that may provide upon obtaining entitlements additional lots. However, based on the current stage of land entitlement, the Company has concluded at this time that the level of uncertainty in entitling these properties does not warrant including them in the above totals.

Note 3. Investments in Housing and Land Joint Ventures

The Company participates in a number of joint ventures in which it has less than a controlling interest. Summarized condensed financial information on a combined 100% basis of the joint ventures is as follows:

	September 30, 2006	December 31, 2005
Assets		
Housing and land inventory	$ 505,518	$ 357,833
Other assets	31,149	64,866
	$ 536,667	$ 422,699
Liabilities and Equity		
Project specific financings	$ 285,812	$ 289,851
Accounts payable and other liabilities	46,254	90,459
Investment and advances		
Brookfield Homes	103,044	53,260
Others	101,557	(10,871)
	$ 536,667	$ 422,699

	Three Months Ended September 30,		Nine Months Ended September 30,	
Revenue and Expenses	**2006**	**2005**	**2006**	**2005**
Revenue	$ 86,326	$ 160,816	$ 116,549	$ 232,912
Expenses	(46,973)	(104,523)	(73,496)	(155,370)
Net income	$ 39,353	$ 56,293	$ 43,053	$ 77,542
Company s share of net income	$ 11,204	$ 15,658	$ 12,874	$ 25,249

In reporting the Company s share of net income, all inter-company profits or losses from housing and land joint ventures are eliminated on lots purchased by the Company.

Joint ventures in which the Company has a non-controlling interest are accounted for using the equity method. In addition, the Company has performed an evaluation of its existing joint venture relationships by applying the provisions of FIN 46R. The Company has determined that for those entities for which this interpretation applies, none of these joint ventures were considered to be a VIE requiring consolidation pursuant to the requirements of FIN 46R.

The Company and/or its joint venture partners have provided varying levels of guarantees of debt in its joint ventures. At September 30, 2006, the Company had recourse guarantees of nil (December 31, 2005 $2.0 million) and limited maintenance guarantees of $84.7 million (December 31, 2005 $91.6 million) with respect to debt in its joint ventures.

As of September 30, 2006, the fair market value of the recourse guarantees was insignificant.

BROOKFIELD HOMES CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands of U.S. dollars except per share amounts)

Note 4. Accounts Payable and Other Liabilities

The components of accounts payable and other liabilities included in the Company s balance sheet are summarized as follows:

	September 30, 2006	December 31, 2005
Trade payables and cost to complete accruals	$ 49,514	$ 86,137
Warranty costs	18,899	17,743
Customer deposits	8,881	12,307
Stock-based compensation	23,806	44,935
Due to minority interest	22,776	39,478
Accrued and deferred compensation	25,359	47,974
Income tax liabilities	63,968	

(4) KPN Telecom B.V. is a subsidiary of Royal KPN N.V.

(5) An officer of the Company.

(6) A director of the Company.

(7) Includes an option to purchase 100,000 shares of common stock at an exercise price of $4.21 per share. 25,000 options vest on April 13, 2004, 25,000 options vest on April 13, 2005, 25,000 options vest on April 13, 2006, while 25,000 options vest on April 13, 2007.

(8) Effective March 22, 2005 the Board of Directors granted Mr. Attia and Mr. Kenig, 100,000 options at an exercise price of $3.40 per share under the 2004 Incentive Plan. Each options vests in four equal installments of 25,000 shares on September 22, 2005, September 22, 2006, September 22, 2007 and September 22, 2008.

The foregoing table is based upon 4,609,181 shares of common stock outstanding as of October 1, 2007.

SECTION 16(a) BENEFICIAL OWNERSHIP COMPLIANCE

Section 16(a) of the Securities Exchange Act of 1934 requires the Company s directors and executive officers, and persons who own more then 10 percent of the Company s Common Stock, to file with the SEC the initial reports of ownership and reports of changes in ownership of common stock. Officers, directors and greater than 10 percent stockholders are required by SEC regulation to furnish the Company with copies of all Section 16(a) forms they file.

Specific due dates for such reports have been established by the Commission and the Company is required to disclose in this Proxy Statement any failure to file reports by such dates during fiscal 2003. Based

solely on its review of the copies of such reports received by it, or written representations from certain reporting persons that no Forms 5 were required for such persons, the Company believes that during the fiscal year ended December 31, 2006, there was no failure to comply with Section 16(a) filing requirements applicable to its officers, directors and ten percent stockholders.

POLICY WITH RESPECT TO SECTION 162(m)

Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code), provides that, unless an appropriate exemption applies, a tax deduction for the Company for compensation of certain executive officers named in the Summary Compensation Table will not be allowed to the extent such compensation in any taxable year exceeds $1 million. As no executive officer of the Company received compensation during 2005 approaching $1 million, and the Company does not believe that any executive officer s compensation is likely to exceed $1 million in 2005, the Company has not developed an executive compensation policy with respect to qualifying compensation paid to its executive officers for deductibility under Section 162(m) of the Code.

EXECUTIVE COMPENSATION

The following table sets forth the cash compensation (including cash bonuses) paid or accrued and equity awards granted by us for years ended December 31, 2006 to the Company s CEO and our most highly compensated officers other than the CEO at December 31, 2006 whose total compensation exceeded $100,000.

SUMMARY COMPENSATION TABLE

Name & Principal Position	Year	Salary ($)	Bonus ($)	Stock Awards ($)	Option Awards ($)	Non-Equity Incentive Plan Compensation ($)	Change in Pension Value and Non-Qualified Deferred Compensation Earnings ($)	All Other Compensation ($)	Total ($)
Yossi Attia	2006	$149,396		$93,750 [(2)]					
Chief Executive Officer[(1)]	2005	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

(1) Mr. Attia was appointed as CEO of the Company on August 14, 2006.

(2) In accordance with Mr. Attia s employment agreements, Mr. Attia is entitled to receive 111,458 shares of common stock for the period from August 14, 2006 to August 13, 2007 representing a compensation of $250,000 to be paid in the form of Company shares of common stock. On May 31, 2007 the Company, ERC and Mr. Attia entered into a Memorandum of Understanding, pursuant to which, the August 14, 2006 amendment to Mr. Attia s employment agreement was terminated, and effective as of January 1, 2007, ERC s rights and obligations under Mr. Attia s employment agreement were transferred to the Company No shares have been issued to date.

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OUTSTANDING EQUITY AWARDS

Option Awards Stock Awards

Name

	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#)	Option Exercise Price ($)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested ($)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested ($)
Yossi Attia(1)	100,000 (2)			$ 3.40	03/12/2011	50,000(3)	$92,500(3)		

(1) Mr. Attia was appointed as Chief Executive Officer of the Company on August 14, 2006.

(2) On March 22, 2005, the Company granted 100,000 options to Yossi Attia. The stock options granted vest at the rate of 25,000 options on each September 22 of 2005, 2006, 2007 and 2008, respectively. The exercise price of the options ($3.40) is equal to the market price on the date the options were granted.

(3) In accordance with Mr. Attia s employment agreement, Mr. Attia is entitled to receive 111,458 shares of common stock for the first year. No shares have been issued. The 50,000 option represents the shares of common stock that have not vested to date. The value of such shares is based on the closing price for the Company s common stock of $1.85 as of December 29, 2006 (the last trading day of 2006).

Except as set forth above, no other named executive officer has received an equity award.

DIRECTOR COMPENSATION

The following table sets forth with respect to the named Director, compensation information inclusive of equity awards and payments made in the year end December 31, 2006.

Name	Fees Earned or Paid in Cash ($)	Stock Awards ($)	Option Awards ($)	Non-Equity Incentive Plan Compensation ($)	Change in Pension Value and Nonqualified Deferred Compensation Earnings	All Other Compensation ($)	Total ($)
Stewart Reich	$36,502						$36,502
Ilan Kenig	$29,002						$29,002
Robin Ann Gorelick	$59,500						$59,500
Gerald Schaffer	$25,002						$25,002

OPTIONS/SAR GRANTS IN LAST FISCAL YEAR

There were other grants of Stock Options/SAR made to the named Executive and President during the fiscal year ended December 31, 2006.

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AGGREGATED OPTION/SAR EXERCISES IN LAST FISCAL YEAR AND YEAR-END OPTION/SAR VALUES

Name	Shares acquired on exercise (#)	Value realized ($)	Number of securities underlying unexercised options/SARs at FY-end (#) Exercisable/Unexercisable	Value of the unexercised in the money options/SARs at FY-end ($)* Exercisable/Unexercisable
Yossi Attia, CEO, Director	None	None	100,000	$ 0.00

* Fair market value of underlying securities (calculated by subtracting the exercise price of the options from the closing price of the Company's common stock quoted on the NASDAQ as of December 29, 2006, which was $1.85 per share. None of Mr. Yossi's options are presently in the money.

EMPLOYMENT AND MANAGEMENT AGREEMENTS

Effective July 1, 2006, the Company entered into a five-year employment agreement with Yossi Attia as the President of ERC which commenced on July 1, 2006 and provides for annual compensation of $240,000 and an annual bonus of not less than $120,000 per year, as well as an annual car allowance for the same period. Mr. Attia will be entitled to a special bonus equal to 10% of the EBITDA of ERC, which such bonus is payable in shares of common stock of the Company; provided, however, the special bonus is only payable in the event that Mr. Attia remains continuously employed by ERC and Mr. Attia shall not have sold shares of common stock of the Company on or before the payment date of the special bonus unless such shares were received in connection with the exercise of an option that was scheduled to expire within one year of the date of exercise. In addition, on August 14, 2006, the Company amended the Agreement to provide that Mr. Attia shall serve as the CEO of the Company for a term of two years commencing August 14, 2006 and granting annual compensation of $250,000 to be paid in the form of Company shares of common stock. The number of shares to be received by Mr. Attia is calculated based on the average closing price 10 days prior to the commencement of each employment year. Mr. Attia will receive 111,458 of the Company shares of common stock for his first year service. No shares have been issue to Mr. Attia in 2006.

The employment agreements mentioned above further provide that, if employment is terminated other than for willful breach by the employee, for cause or in event of a change in control of the Company, then the employee has the right to terminate the agreement. In the event of any such termination, the employee will be entitled to receive the payment due on the balance of his employment agreement.

On May 31, 2007 the Company, ERC and Mr. Attia entered into a Memorandum of Understanding, pursuant to which, the August 14, 2006 amendment to Mr. Attia s employment agreement was terminated, and effective as of January 1, 2007, ERC s rights and obligations under Mr. Attia s employment agreement were transferred to the Company

The Company has no pension or profit sharing plan or other contingent forms of remuneration with any officer, Director, employee or consultant, although bonuses are paid to some individuals.

DIRECTOR COMPENSATION

Before June 11, 2006, Directors who are also officers of the Company were not separately compensated for their services as a Director. Directors who were not officers received cash compensation for their services: $2,000 at the time of agreeing to become a Director; $2,000 for each Board Meeting attended either in person or by telephone; and $1,000 for each Audit and Compensation Committee Meeting attended either in person or by telephone. Non-employee Directors were reimbursed for their expenses incurred in connection with attending meetings of the Board or any committee on which they served and were eligible to receive awards under the Company s 2004 Incentive Plan.

The Board has approved the modification of Directors' compensation on its special meeting held on June 11, 2006. Directors who are also officers of the Company are not separately compensated for their services as a Director. Directors who are not officers receive cash compensation for their services as follows: $40,000 per year and an additional $5,000 if they sit on a committee and an additional $5,000 if they sit as the head of such committee. Non-employee directors are reimbursed for their expenses incurred in connection with attending meetings of the Board or any committee on which they serve and are eligible to receive awards under our 2004 Incentive Plan.

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STOCK OPTION PLAN

2004 Incentive Plan

General

The 2004 Incentive Plan was adopted by the Board. The Board initially reserved 800,000 shares of common stock for issuance under the 2004 Incentive Plan. In 2005, the Plan was adjusted to increase the number of shares of common stock issuable under such plan from 800,000 shares to 1,200,000 shares. Under the Plan, options may be granted which are intended to qualify as Incentive Stock Options (ISOs) under Section 422 of the Internal Revenue Code of 1986 (the Code) or which are not (Non-ISOs) intended to qualify as Incentive Stock Options thereunder.

The 2004 Incentive Plan and the right of participants to make purchases thereunder are intended to qualify as an employee stock purchase plan under Section 423 of the Internal Revenue Code of 1986, as amended (the Code). The 2004 Incentive Plan is not a qualified deferred compensation plan under Section 401(a) of the Internal Revenue Code and is not subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

Purpose

The primary purpose of the 2004 Incentive Plan is to attract and retain the best available personnel for the Company in order to promote the success of the Company's business and to facilitate the ownership of the Company's stock by employees.

Administration

The 2004 Incentive Plan is administered by the Company's Board, as the Board may be composed from time to time. All questions of interpretation of the 2004 Incentive Plan are determined by the Board, and its decisions are final and binding upon all participants. Any determination by a majority of the members of the Board at any meeting, or by written consent in lieu of a meeting, shall be deemed to have been made by the whole Board.

Notwithstanding the foregoing, the Board may at any time, or from time to time, appoint a committee (the Committee) of at least two members of the Board, and delegate to the Committee the authority of the Board to administer the Plan. Upon such appointment and delegation, the Committee shall have all the powers, privileges and duties of the Board, and shall be substituted for the Board, in the administration of the Plan, subject to certain limitations.

Members of the Board who are eligible employees are permitted to participate in the 2004 Incentive Plan, provided that any such eligible member may not vote on any matter affecting the administration of the 2004 Incentive Plan or the grant of any option pursuant to it, or serve on a committee appointed to administer the 2004 Incentive Plan. In the event that any member of the Board is at any time not a disinterested person , as defined in Rule 16b-3(c)(3)(i) promulgated pursuant to the Securities Exchange Act of 1934, the Plan shall not be administered by the Board, and may only by administered by a Committee, all the members of which are disinterested persons, as so defined.

Eligibility

Under the 2004 Incentive Plan, options may be granted to key employees, officers, Directors or consultants of the Company, as provided in the 2004 Incentive Plan.

Terms of Options

The term of each option granted under the Plan shall be contained in a stock option agreement between the optionee and the Company and such terms shall be determined by the Board consistent with the provisions of the Plan, including the following:

(a) PURCHASE PRICE. The purchase price of the common shares subject to each ISO shall not be less than the fair market value (as set forth in the 2004 Incentive Plan), or in the case of the grant of an ISO to a principal stockholder, not less that 110% of fair market value of such common shares at the time such option

is granted. The purchase price of the common shares subject to each Non-ISO shall be determined at the time such option is granted, but in no case less than 85% of the fair market value of such common shares at the time such option is granted.

(b) VESTING. The dates on which each option (or portion thereof) shall be exercisable and the conditions precedent to such exercise, if any, shall be fixed by the Board, in its discretion, at the time such option is granted.

(c) EXPIRATION. The expiration of each option shall be fixed by the Board, in its discretion, at the time such option is granted; however, unless otherwise determined by the Board at the time such option is granted, an option shall be exercisable for ten (10) years after the date on which it was granted (the Grant Date). Each option shall be subject to earlier termination as expressly provided in the 2004 Incentive Plan or as determined by the Board, in its discretion, at the time such option is granted.

(d) TRANSFERABILITY. No option shall be transferable, except by will or the laws of descent and distribution, and any option may be exercised during the lifetime of the optionee only by him. No option granted under the Plan shall be subject to execution, attachment or other process.

(e) OPTION ADJUSTMENTS. The aggregate number and class of shares as to which options may be granted under the Plan, the number and class shares covered by each outstanding option and the exercise price per share thereof (but not the total price), and all such options, shall each be proportionately adjusted for any increase decrease in the number of issued common shares resulting from split-up spin-off or consolidation of shares or any like capital adjustment or the payment of any stock dividend.

Except as otherwise provided in the 2004 Incentive Plan, any option granted hereunder shall terminate in the event of a merger, consolidation, acquisition of property or stock, separation, reorganization or liquidation of the Company. However, the optionee shall have the right immediately prior to any such transaction to exercise his option in whole or in part notwithstanding any otherwise applicable vesting requirements.

(f) TERMINATION, MODIFICATION AND AMENDMENT. The 2004 Incentive Plan (but not options previously granted under the Plan) shall terminate ten (10) years from the earlier of the date of its adoption by the Board or the date on which the Plan is approved by the affirmative vote of the holders of a majority of the outstanding shares of capital stock of the Company entitled to vote thereon, and no option shall be granted after termination of the Plan. Subject to certain restrictions, the Plan may at any time be terminated and from time to time be modified or amended by the affirmative vote of the holders of a majority of the outstanding shares of the capital stock of the Company present, or represented, and entitled to vote at a meeting duly held in accordance with the applicable laws of the State of Delaware.

FEDERAL INCOME TAX ASPECTS OF THE 2004 INCENTIVE PLAN

THE FOLLOWING IS A BRIEF SUMMARY OF THE EFFECT OF FEDERAL INCOME TAXATION UPON THE PARTICIPANTS AND THE COMPANY WITH RESPECT TO THE PURCHASE OF SHARES UNDER THE 2004 INCENTIVE PLAN. THIS SUMMARY DOES NOT PURPORT TO BE COMPLETE AND DOES NOT ADDRESS THE FEDERAL INCOME TAX CONSEQUENCES TO TAXPAYERS WITH SPECIAL TAX STATUS. IN ADDITION, THIS SUMMARY DOES NOT DISCUSS THE PROVISIONS OF THE INCOME TAX LAWS OF ANY MUNICIPALITY, STATE OR FOREIGN COUNTRY IN WHICH THE PARTICIPANT MAY RESIDE, AND DOES NOT DISCUSS ESTATE, GIFT OR OTHER TAX CONSEQUENCES OTHER THAN INCOME TAX CONSEQUENCES. THE COMPANY ADVISES EACH PARTICIPANT TO CONSULT HIS OR HER OWN TAX ADVISOR REGARDING THE TAX CONSEQUENCES OF PARTICIPATION IN THE 2004 Incentive Plan AND FOR REFERENCE TO APPLICABLE PROVISIONS OF THE CODE.

The 2004 Incentive Plan and the right of participants to make purchases thereunder are intended to qualify under the provisions of Sections 421, 422 and 423 of the Code. Under these provisions, no income will be recognized by a participant prior to disposition of shares acquired under the 2004 Incentive Plan.

If the shares are sold or otherwise disposed of (including by way of gift) more than two years after the first day of the offering period during which shares were purchased (the Offering Date), a participant will recognize as ordinary income at the time of such disposition the lesser of (a) the excess of the fair market value of the shares at the time of such disposition over the purchase price of the shares or (b) 15% of the fair market value of the shares on the first day of the offering period. Any further gain or loss upon such disposition will be treated as long-term capital gain or loss. If the shares are sold for a sale price less than the purchase price, there is no ordinary income and the participant has a capital loss for the difference.

If the shares are sold or otherwise disposed of (including by way of gift) before the expiration of the two-year holding period described above, the excess of the fair market value of the shares on the purchase date over the purchase price will be treated as ordinary income to the participant. This excess will constitute ordinary income in the year of sale or other disposition even if no gain is realized on the sale or a gift of the shares is made. The balance of any gain or loss will be treated as capital gain or loss and will be treated as long-term capital gain or loss if the shares have been held more than one year.

In the case of a participant who is subject to Section 16(b) of the Exchange Act, the purchase date for purposes of calculating such participant's compensation income and beginning of the capital gain holding period may be deferred for up to six months under certain circumstances. Such individuals should consult with their personal tax advisors prior to buying or selling shares under the 2004 Incentive Plan.

The ordinary income reported under the rules described above, added to the actual purchase price of the shares, determines the tax basis of the shares for the purpose of determining capital gain or loss on a sale or exchange of the shares.

The Company is entitled to a deduction for amounts taxed as ordinary income to a participant only to the extent that ordinary income must be reported upon disposition of shares by the participant before the expiration of the two-year holding period described above.

Restrictions on Resale

Certain officers and directors of our company may be deemed to be affiliates of our company as that term is defined under the Securities Act. The Common Stock acquired under the 2004 Incentive Plan by an affiliate may be reoffered or resold only pursuant to an effective registration statement or pursuant to Rule 144 under the Securities Act or another exemption from the registration requirements of the Securities Act.

ANNUAL REPORT ON FORM 10-KSB

The Company will provide upon request and without charge to each stockholder receiving this Proxy Statement a copy of the Company's Annual Report on Form 10-KSB for the fiscal year ended December 31, 2006, including the financial statements and financial statement schedule information included therein, as filed with the SEC.

OTHER BUSINESS

The Board of Directors is not aware of any matter other than the matters described above to be presented for action at the Meeting. However, if any other proper items of business should come before the Meeting, it is the intention of the individuals named on your proxy card as the proxy holders to vote in accordance with their best judgment on such matters.

By Order of the Board of Directors

By: **/s/ Yossi Attia**

Yossi Attia, Director and President

November 8, 2007
Beverly Hills, California

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ANNEX 1

REPORT OF THE AUDIT COMMITTEE OF THE BOARD OF DIRECTORS

Membership and role of the Audit Committee

The Audit Committee of the board of directors reviews the internal accounting procedures of the company and consults with and reviews the services provided by our independent accountants. During 2006, the audit committee consisted of Messrs. Stewart Reich, Gerald Schaffer and Ilan Kenig.

As at December 31, 2006, a majority of the members of the Audit Committee (Messrs. Reich, Kenig and Schaffer) were independent for purposes of the National Association of Securities Dealers' listing standards. The Audit Committee operates under a written charter adopted by the Board of Directors which is included in the Company's Proxy Statement dated April 18, 2001.

The Audit Committee reviews the Company's financial reporting process on behalf of the Board of Directors. Management has the primary responsibility for the financial statements and the reporting process, including the system of internal controls. The independent auditors are responsible for performing an independent audit of the Company's consolidated financial statements in accordance with generally accepted accounting principles and to issue a report thereon. The Committee monitors these processes.

Review of the Company's audited financial statements for the fiscal year ended December 31, 2006

In this context, the Committee met and held discussions with management and the independent auditors. Management represented to the Committee that the Company's consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States, and the Committee reviewed and discussed the consolidated financial statements with management and the independent auditors. The Committee also discussed with the independent auditors the matters required to be discussed by Statement on Auditing Standards No. 61 (Codification of Statements on Auditing Standards, AU 380), as amended.

In addition, the Committee discussed with the independent auditors the auditors' independence from the Company and its management, and the independent auditors provided to the Committee the written disclosures and letter required by the Independence Standards Board Standard No. 1 (Independence Discussions With Audit Committees).

The Committee discussed with the Company's internal and independent auditors the overall scope and plans for their respective audits. The Committee met with the internal and independent auditors, with and without management present, to discuss the results of their examinations, the evaluation of the Company's internal controls, and the overall quality of the Company's financial reporting.

Based on the reviews and discussions referred to above, the Committee recommended to the Board of Directors, and the Board has approved, that the audited financial statements be included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2006, for filing with the Securities and Exchange Commission.

Audit Fees

The following table presents aggregate fees for professional audit services rendered by Deloitte Auditing and Consulting Kft. and Robison Hill & Co and affiliates for the audit of the Company s annual financial statements for the fiscal years ended December 31, 2006 and 2005, respectively, and fees billed for other services rendered.

	2006	2005
Audit Fees[1]	$ 160,000	$ 192,000
Audit-Related Fees[2]	$ 46,000	$ 127,000
Tax Fees[3]	$	$
All Other Fees[4]	$ 21,500	$ 67,200

(1) Audit Fees: The aggregate fees billed by our auditors for professional services rendered for the audit of the Company's annual financial statements for the years ended December 31, 2006 and 2005, and for the

reviews of the financial statements included in the Company's Quarterly Reports on Form 10-QSB during the fiscal years were $160,000 and $192,000, respectively.

(2) Audit Related Fees: In 2006 for replacement of auditors due to Deloitte resignation. In 2005, fees for the audit of the 2004 US GAAP financials statements of Navigator (for 8-K filing purposes) were $127,000. In 2006, no such fees were paid.

(3) Tax Fees: There were no tax services provided in fiscal year 2006 and 2005.

(4) All Other Fees: The aggregate fees billed by auditors for services rendered to the Company, other than the services covered in Audit Fees and Audit related fees and for the fiscal years ended December 31, 2006 and 2005 were $21,500 and $67,200. The 2006 and 2005 fees relate to the SB-2 registration statement costs.

(5) During April 2007, the Company was invoiced by the former auditors for $124,661 as a result of over run fees, which exceed the written agreement.

The Company s Audit Committee s policy is to pre-approve all audit and permissible non-audit services provided by the independent auditors. These services may include audit services, audit-related services, tax services and other services. All services rendered have been approved by the Audit Committee.

Upon resignation of former auditors, the Company was presented with overrun fees by its former auditors, as well as open balances aggregate to $175,281 for audit works NOT performed in the US. The Company investigates such charges, and demand breakdown of fees from its former auditors which was provided and open balances with Deloitte were brought current.

The Board of Directors has considered whether the provision of non-audit services is compatible with maintaining the principal accountant's independence.

Auditor Independence

The Audit Committee has considered whether, and has determined that, the provision of services described under All

Other Fees was compatible with maintaining the independence of Robison as the Company's principal accountants.

MEMBERS OF THE AUDIT COMMITTEE

Independent Members:

/s/ Stewart Reich
Stewart Reich

/s/ Ilan Kenig
Ilan Kenig

/s/ Gerald Schaffer
Gerald Schaffer

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ANNEX 2

REPORT OF THE COMPENSATION COMMITTEE OF THE BOARD OF DIRECTORS ON EXECUTIVE COMPENSATION

The Compensation Committee of the board of directors (i) reviews and recommends to the board the compensation and benefits of our executive officers; (ii) administers our stock option plans and employee stock purchase plan; and (iii) establishes and reviews general policies relating to compensation and employee benefits.

In 2006, the compensation committee consisted of Messrs. Reich, Schaffer and Kenig all of which are independent. No interlocking relationships exist between the board of directors or compensation committee and the board of directors or compensation committee of any other company. During the past fiscal year the Compensation Committee had two (2) meetings.

MEMBERS OF THE COMPENSATION COMMITTEE

Independent Members:

/s/ Stewart Reich
Stewart Reich

/s/ Ilan Kenig
Ilan Kenig

/s/ Gerald Schaffer
Gerald Schaffer

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PROXY

EMVELCO CORP.
ANNUAL MEETING OF STOCKHOLDERS TO BE HELD December 7, 2007
THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS

The undersigned, revoking all prior proxies, hereby appoints ROBIN ANN GORELICK (Company counsel) and YOSSI ATTIA (Company CEO) and each of them, with full power of substitution in each, as proxies for the undersigned, to represent the undersigned and to vote all the shares of Common Stock of the Company which the undersigned would be entitled to vote, as fully as the undersigned could vote and act if personally present, at the Annual Meeting of Stockholders (the Meeting) to be held on December 7, 2007, at 11:30 A.M., local time, at its corporate offices located at 468 North Camden Drive, Conference Room, 2nd Floor, Beverly Hills, California 90210, or at any adjournments or postponements thereof.

Should the undersigned be present and elect to vote at the Meeting or at any adjournments or postponements thereof, and after notification to the Secretary of the Company at the Meeting of the stockholder's decision to terminate this proxy, then the power of such attorneys or proxies shall be deemed terminated and of no further force and effect. This proxy may also be revoked by filing a written notice of revocation with the Secretary of the Company or by duly executing a proxy bearing a later date.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR ALL NOMINEES FOR DIRECTOR AND EACH OF THE LISTED PROPOSALS.

Proposal (1) The election as directors of all nominees listed below to serve until the 2007 Annual Meeting of Stockholders or until their successors have been duly elected and qualified (except as marked to the contrary).

Nominees:

01) Ilan Kenig	02) Stewart P. Reich	
03) Darren C. Dunckel	04) Yossi Attia	05) Gerald Schaffer
FOR ALL o	**WITHHOLD ALL** o	**FOR ALL EXCEPT** o

To withhold authority to vote, mark For All Except and write the nominee's number on the line below.

Proposal (2) Ratification of the appointment of ROBISON HILL & CO. as auditors of the Company for the fiscal year ending December 31, 2006.

FOR o	**AGAINST** o	**ABSTAIN** o

Proposal (3) Authorization of the Board of Directors for a period of one year to terminate the Company s status as a reporting company

FOR o	**AGAINST** o	**ABSTAIN** o

The shares represented by this proxy will be voted as directed by the stockholder, but if no instructions are specified, this proxy will be voted for the election of the Board nominees and for proposals (1), (2) and (3). If any other business is presented at the Meeting, this proxy will be voted by those named in this proxy in their best judgment. At the present time, the Board of Directors knows of no other business to be presented at the Meeting.

The undersigned acknowledges receipt from the Company, prior to the execution of this proxy, of the Notice of Annual Meeting and accompanying Proxy Statement relating to the Meeting and an Annual Report to Stockholders for fiscal year ended December 31, 2006.

NOTE: PLEASE MARK, DATE AND SIGN AS YOUR NAME(S) APPEAR(S) HEREON AND RETURN IN THE ENCLOSED ENVELOPE. IF ACTING AS AN EXECUTORS, ADMINISTRATORS, TRUSTEES, GUARDIANS, ETC., YOU SHOULD SO INDICATE WHEN SIGNING. IF THE SIGNER IS CORPORATION, PLEASE SIGN THE FULL CORPORATE NAME, BY DULY AUTHORIZED OFFICER. IF SHARES ARE HELD JOINTLY, EACH SHAREHOLDER SHOULD SIGN.

Signature (Please sign within the box) [________] DATE: _______, 2007	Signature (Joint owners) [_________]	DATE: _______, 2007

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