

STORAGE COMPUTER CORP

Form PRE 14A

April 29, 2004

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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

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 (S) 240.14a-11(c) or (S) 240.14a-12

STORAGE COMPUTER CORPORATION

(Name of Registrant as Specified In Its Charter)

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

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(3) Filing Party:

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STORAGE COMPUTER CORPORATION

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

TO BE HELD ON JULY 15, 2004

To our Stockholders:

The 2004 annual meeting of the stockholders of Storage Computer Corporation will be held at the offices of the Company at 11 Riverside Drive, Nashua, New Hampshire 03062 (Route 3, Exit 5) on Thursday July 15, 2004, beginning at 10:00 a.m. local time. At the meeting, the holders of common stock of the Company will act on the following matters:

1. Election of five directors to hold office until the next annual meeting of stockholders and until their respective successors are duly elected and qualified;
2. Amendment to the 1999 Stock Incentive Plan;
3. Amendment of the Company's Certificate of Incorporation to increase the authorized number of shares of Common Stock of the Company from 50,000,000 shares to 100,000,000 shares;
4. Ratification of the appointment of Sullivan Bille PC as the Company's independent auditors for 2004; and
5. Any other matters that properly come before the meeting.

All holders of record of Storage common stock (AMEX:SOS) at the close of business on April 28, 2004 are entitled to receive notice of and to vote at the annual meeting of stockholders and any postponements or adjournments of the meeting.

By order of the Board of Directors,

MICHAEL J. O DONNELL

Secretary

April 29, 2004

Nashua, New Hampshire

YOUR VOTE IS IMPORTANT

Whether or not you expect to attend the annual meeting, please complete, date, sign and promptly return the accompanying proxy in the enclosed postage-paid envelope so that your shares may be represented at the meeting.

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STORAGE COMPUTER CORPORATION

11 Riverside Street

Nashua, New Hampshire 03062

PROXY STATEMENT

This proxy statement is being furnished in connection with the solicitation by the Board of Directors of the Company of proxies for the annual meeting of stockholders of Storage Computer Corporation to be held on Thursday July 15, 2004 at 10:00 AM EST at the offices of the Company, 11 Riverside Drive, Nashua, New Hampshire, and at any postponements or adjournments thereof.

The Company is mailing this proxy statement, the accompanying proxy card and the Company's 2003 Annual Report on or about June 28, 2004 to the holders of record of the Company's outstanding shares of common stock on April 28, 2004. The Board of Directors of the Company is soliciting the accompanying proxy for use at the annual meeting. The Company will bear the cost of solicitation of proxies. Directors, officers and employees may assist in the solicitation of proxies, in person or otherwise, without additional compensation.

ABOUT THE MEETING

What is the purpose of the annual meeting?

At our annual meeting, stockholders will act upon the matters outlined in the Notice of Annual Meeting of Stockholders on the cover page of this proxy statement. In addition, management will report on the performance of the Company during fiscal 2003 and respond to questions from stockholders.

Who is entitled to vote at the meeting?

Only stockholders of record at the close of business on April 28, 2004, the record date for the meeting, are entitled to receive notice of and to vote at the annual meeting. If you were a shareholder of record on that date, you will be entitled to vote all of the shares that you held on that date at the meeting, or any postponements or adjournments of the meeting. Each share of common stock is entitled to one vote on all matters presented at the annual meeting.

Who can attend the meeting?

All stockholders as of the record date, or their duly appointed proxies, may attend the meeting, and each may be accompanied by one guest. Seating, however, is limited. Admission to the meeting will be on a first-come, first-served basis. Registration will begin at 8:30 a.m. If you attend, please note that you may be asked to present valid picture identification, such as a driver's license or passport. Cameras, recording devices and other electronic devices will not be permitted at the meeting. Please also note that if you hold your shares in street name (that is, through a broker or other nominee), you will need to bring a copy of a brokerage statement reflecting your stock ownership as of the record date and check in at the registration desk at the meeting.

What constitutes a quorum?

The presence at the meeting, in person or by proxy, of the holders of a majority of the aggregate voting power of the Company's common stock outstanding on the record date will constitute a quorum, permitting business to be conducted at the meeting. As of the record date, 38,910,125 shares of the Company's common stock, representing the same number of votes, were outstanding. Thus, the presence of the holders of common stock representing at least 19,455,064 votes will be required to establish a quorum. Proxies received but marked as abstentions and broker non-votes will be included in the calculation of the number of votes considered to be present at the meeting.

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How do I vote?

If you complete and properly sign the accompanying proxy card and return it to the Company, it will be voted as you direct in the proxy card. If you are a registered stockholder and attend the meeting, you may either vote or deliver your completed proxy card in person at the meeting. Street name stockholders who wish to vote at the meeting will need to obtain a proxy form from the institution that holds their shares.

Can I change my vote after I return my proxy card?

Yes. Even after you have submitted your proxy, you may change your vote at any time before the proxy is exercised by filing with the Secretary of the Company either a notice of revocation or a duly executed proxy bearing a later date. In addition, the powers of the proxy holders will be suspended if you attend the meeting in person and so request, although attendance at the meeting will not by itself revoke a previously granted proxy.

What are the Board's recommendations?

Unless you give other instructions on your proxy card, the persons named as proxy holders on the proxy card will vote in accordance with the recommendations of the Board of Directors. The Board's recommendations are set forth together with the description of each proposal to be voted upon in this proxy statement. In summary, the Board recommends you vote: **For** election of the nominated slate of directors (see page 6); **For** Amendment to the 1999 Stock Incentive Plan (see page 17); **For** Amendment of the Company's Certificate of Incorporation to increase the authorized number of shares of Common Stock of the Company from 50,000,000 shares to 100,000,000 shares (see page 18); and **For** ratification of the appointment of Sullivan Bille, P C as the Company's independent auditors for fiscal year 2004 (see page 18).

With respect to any other matter that properly comes before the meeting, the proxy holders will vote as recommended by the Board of Directors or, if no recommendation is given, in their own discretion.

What vote is required to approve each proposal?

Election of Directors. The affirmative vote of a plurality of the votes cast at the meeting is required for the election of directors. A properly executed proxy marked **WITHHOLD AUTHORITY** with respect to the election of one or more directors will not be voted with respect to the director or directors indicated, although it will be counted for purposes of determining whether there is a quorum. If no instructions are indicated on your proxy card, the shares represented by your proxy will be voted **FOR** the election of the nominees for director listed in this proxy statement.

Amendment to the 1999 Stock Incentive Plan. The affirmative vote of a plurality of the votes cast at the meeting is required for approval the amendment to the 1999 Stock Incentive Plan.+

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Increase of Authorized Shares of Common Stock. To increase by 50,000,000 the number of authorized shares of the Company's Common Stock requires the affirmative vote of a majority of all outstanding shares of Common Stock entitled to vote.

Other Items. For each other proposal, the affirmative vote of the holders of a majority of the shares represented in person or by proxy at the meeting and entitled to vote on the item will be required for approval. A properly executed proxy marked "ABSTAIN" with respect to any such matter will not be voted, although it will be counted for purposes of determining whether there is a quorum. Accordingly, an abstention will have the effect of a negative vote.

If you hold your shares in "street name" through a broker or other nominee, your broker or nominee may not be permitted to exercise voting discretion with respect to some of the matters to be acted upon. Thus, if you do not give your broker or nominee specific instructions, your shares may not be voted on those matters and will not be counted in determining the number of shares necessary for approval. Shares represented by such "broker non-votes" will, however, be counted in determining whether there is a quorum.

Table of Contents**STOCK OWNERSHIP****Who beneficially owns more than five percent of the Company's stock?**

The following table lists certain information regarding the beneficial ownership of the Company's common stock, par value \$0.001 per share as of April 28, 2004, by those persons known to the Company to be beneficial owners of more than five percent of the outstanding shares of common stock.

<u>Name and Address of Beneficial Owner</u>	<u>Shares of Common Stock Beneficially Owned</u>	
	<u>Number of Shares</u>	<u>Percent</u>
Theodore J. Goodlander c/o Storage Computer Corporation 11 Riverside Street Nashua, New Hampshire 03062	12,763,906(1)	32.00%
Jeanne McCready, Trustee c/o Storage Computer Corporation 11 Riverside Street Nashua, New Hampshire 03062	2,728,380(2)	7.01%

- (1) Includes 8,724,240 shares of common stock beneficially owned by Mr. Goodlander and 1,268,201 shares of common stock beneficially owned by Kristiania Corp., a corporation controlled by Mr. Goodlander, acquired upon conversion of all of the remaining outstanding shares of the Company's Series A and Series C convertible preferred stock into shares of common stock in January 2003. Excludes 2,678,336 shares gifted by Mr. Goodlander in 2003. Also includes 787,856 shares of common stock issuable upon the exercise of a warrant held by Mr. Goodlander to purchase 787,856 shares of common stock at \$21.03 per share and shares issuable pursuant to the exercise of a warrant held by Kristiania Corp. to purchase 186,989 shares of common stock at \$10.58 per share. Does not include 2,728,380 shares of common stock held by the Goodlander children's trusts established for the exclusive benefit of Mr. Goodlander's children, and as to which Mr. Goodlander exercises no voting or dispositive control and disclaims beneficial ownership.
- (2) Jeanne McCready is the Trustee of three separate trusts established for each of the following of Mr. Goodlander's minor children: Christine Marian Goodlander, Margaret Vivian Goodlander and John Samuel Goodlander.

Table of Contents**How much stock do the Company's directors and executive officers own?**

The following table sets forth certain information regarding the beneficial ownership of the Company's common stock by its directors and executive officers and the directors and executive officers as a group. Except as otherwise indicated, all information is as of April 28, 2004.

Directors and Officers	Shares of Common Stock Beneficially Owned	
	Number of Shares	Percent
Theodore J. Goodlander President, Chief Executive Officer and Chairman of the Board of Directors	12,763,906(1)	32.00%
Steven Chen Director	17,200(2)	*
Edward A. Gardner Director	207,200(3)	*
Peter N. Hood Chief Financial Officer	69,314(4)	*
Roger E. Gauld, Director (Chairman Audit Committee)	38,000(5)	*
Thomas A. Wooters Director	19,028(6)	*
All directors and executive officers as a group (7 persons)	13,179,648(7)	32.78%

* less than 1%.

- (1) Includes 8,724,240 shares of common stock beneficially owned by Mr. Goodlander and 1,268,201 shares of common stock beneficially owned by Kristiania Corp., a corporation controlled by Mr. Goodlander, acquired upon conversion of all of the remaining outstanding shares of the Company's Series A and Series C convertible preferred stock into shares of common stock in January 2003. Excludes 2,678,336 shares gifted by Mr. Goodlander in 2003. Also includes 787,856 shares of common stock issuable upon the exercise of a warrant held by Mr. Goodlander to purchase 787,856 shares of common stock at \$21.03 per share and shares issuable pursuant to the exercise of a warrant held by Kristiania Corp. to purchase 186,989 shares of common stock at \$10.58 per share. Does not include 2,728,380 shares of common stock held by the Goodlander children's trusts established for the exclusive benefit of Mr. Goodlander's children, and as to which Mr. Goodlander exercises no voting or dispositive control and disclaims beneficial ownership.
- (2) Includes 17,200 shares of common stock issuable upon the exercise of options granted pursuant the Company's 1994 Amended and Restated Stock Incentive Plan that are exercisable or will become exercisable within sixty days.
- (3) Includes 200,000 shares of common stock issuable upon the exercise of options pursuant to the Company's 1994 and 1999 Amended and Restated Stock Incentive Plan that are exercisable or will become exercisable within 60 days. Excludes options to purchase 65,000 shares of common stock gifted by Mr. Gardner.
- (4) Mr. Hood resigned as Chief Financial Officer of the Company on February 2, 2004.
- (5) Includes 30,000 shares of common stock issuable upon the exercise of options pursuant to the Company's 1994 and 1999 Amended and Restated Stock Incentive Plans that are exercisable or will become exercisable within sixty days.
- (6) Includes 15,000 shares of common stock issuable upon the exercise of options pursuant to the Company's 1999 Stock Incentive Plan that are exercisable or will become exercisable within sixty days.
- (7) See footnotes (1) through (6) above.

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Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires directors, executive officers and persons who own more than 10% of the outstanding common stock of the Company to file with the Securities and Exchange Commission and the American Stock Exchange reports of ownership and changes in ownership of voting securities of the Company and to furnish copies of such reports to the Company. Based solely on review of the copies of such reports furnished to the Company or written representations from certain persons that no reports were required for those persons, the Company believes that all Section 16(a) filing requirements were satisfied.

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PROPOSAL NO. 1 ELECTION OF DIRECTORS

The Board of Directors of the Company has nominated the following persons for election as directors, each to serve until the next annual meeting of stockholders and until his or her successor has been duly elected and qualified or until such director's earlier resignation, death or removal: Steve S. Chen, Edward A. Gardner, Roger E. Gauld, Theodore J. Goodlander, and Thomas A. Wooters. The proxies solicited by the Board of Directors will be voted in favor of the five nominees named below, unless you mark "WITHHOLD AUTHORITY" on the proxy card. All of the nominees are currently members of the Board. There are no family relationships between any directors or executive officers of the Company. The Board knows of no reason why any of the nominees will be unavailable or unable to serve as a director, but in such event, proxies solicited hereby will be voted for the election of another person or persons to be designated by the Board of Directors.

THE BOARD RECOMMENDS A VOTE *FOR* THE ELECTION OF EACH OF THE NOMINEES LISTED BELOW.

The directors standing for election are:

THEODORE J. GOODLANDER

Director since August 1991

Mr. Goodlander, 60, founded the Company and has been Chairman of the Board of Directors and Chief Executive Officer since the Company's inception. Mr. Goodlander served as the Company's President from its inception until May 8, 2000 and, in August 2002 he reassumed the office of President. Mr. Goodlander served as President of Cab-Tek, Inc., a computer accessories manufacturing company, from 1981 to 1991. From 1978 to 1981, he was a private investor, and from 1968 to 1978 Mr. Goodlander held various management positions at Wang Laboratories, Inc., including Vice President International and Far East Marketing Manager. Mr. Goodlander attended Syracuse University and is a graduate of the Program for Management Development at Harvard Business School.

STEVEN CHEN

Director since May 1996

Mr. Chen, 58, has been the Chairman and Chief Executive Officer of Tonbu, Inc. since 1999. During 1996 and 1997, Mr. Chen was the Executive Vice President and Chief Technology Officer of Sequent Computer Systems, Inc. Prior to 1996, Mr. Chen was the founder and Senior Vice President of Chen Systems, Inc., a high performance computer server manufacturer, which was acquired by Sequent Computer Systems, Inc. in 1996. Prior to that, Mr. Chen founded Supercomputing Systems, Inc., with partial funding from IBM. He had previously been Senior Vice President of Cray Research, with responsibility for development of the Cray XMP and YMP Supercomputers.

EDWARD A. GARDNER

Director since May 2000

Mr. Gardner, 57, served as the Company's President from May 8, 2000 until his resignation in August 2002. Mr. Gardner also served as President of Winnepesaukee Flagship Corp. for the past five years, a company in the tourism industry. Mr. Gardner has held several other senior positions, including president, of a national industrial gas and welding supply company. Previously, he served as controller for Fidelity Management and Research Company and was a certified public accountant while at the accounting firm of Deloitte and Touche (formerly Haskins and Sells).

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ROGER E. GAULD

Director since May 2000

Mr. Gauld, 57, has been a director and Chief Financial Officer of Hampshire Holdings, Inc. since 1995. Mr. Gauld was previously co-founder and Chief Financial Officer of several manufacturing and distribution firms. From 1993 to 1995, he was Chief Financial Officer of Phoenix Custom Molders, Inc. Earlier, he was founder and President of The Phoenix Consulting Group, Inc., which specialized in financial planning and controls, risk management, data processing, mergers and acquisitions. In addition, he is a certified public accountant, served as an audit manager with Ernst & Young (formerly Arthur Young) and was an officer in the U.S. Army for four years.

THOMAS A. WOOTERS

Director since July 2001

Mr. Wooters, 63. Since December 2003 Mr. Wooters has been Executive Vice President and General Counsel of LoJack Corporation, a NASDAQ listed company. LoJack is a world-leader in stolen vehicle recovery technology. From June 1999 to December 2003 he practiced law with the firm of Sullivan & Worcester LLP in Boston, MA. Prior to that, he was with the firm of Peabody & Arnold LLP in Boston, MA for more than five years. He has practiced law for more than 35 years, representing public and private companies and investors in such companies in a range of businesses including software, computer subsystems, biotechnology, communications, and leading edge metallurgy.

Who are the other executive officers of the Company?

Peter N. Hood, 63. Mr. Hood resigned as Chief Financial Officer of the Company on February 2, 2004.

Michael J. O'Donnell, 61, joined the Company as Chief Financial Officer on March 5, 2004. From January 2001 to April 2003 Mr. O'Donnell was Chief Financial Officer for Artisoft, Inc. a NASDAQ listed company. Artisoft develops and markets computer software telephony products and services. For the previous two years he was Chief financial Officer with Lilly Transportation Company, a provider of leasing and logistic services. From 1976 to 2000 he was Chief Financial Officer of Silver Platter International a content software and retrieval company focusing on medical industry verticals Mr. O'Donnell has held several other senior financial positions in manufacturing and industrial companies and started his career in public accounting with Peat Marwick Mitchell & Co in Boston Mass.

How are the directors compensated?

Prior to the second quarter of 2003, members of the Board of Directors did not receive any cash compensation for their service on the Board of Directors. In May 2003 in recognition of the increasing demands on the members of the Board of Directors, the Board of Directors approved the payment of director's fees of \$2,000 per quarter beginning in the second quarter of 2003 and an additional \$2,000 per quarter to Mr. Gauld, Chairman of the Audit Committee, and to Mr. Gardner for his continuing efforts in the oversight of the Company's enforcement of its intellectual property rights. Directors are also entitled to reimbursement of expenses related to attending Board of Directors meetings. Directors who are employees of the Company are not paid any additional compensation for serving as directors. In August 2003 the Board voted to suspend cash

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payments to Directors in order to conserve operating cash. In addition, each of the Directors receive stock option grants.

In August 2001, the Company's Board of Directors approved the issuance of advances secured by demand notes receivable with interest at prime plus 1% to executive officers and directors of the Company in the aggregate amount of \$500,000 for the purpose of purchasing the common stock of the Company in the public market. Demand notes receivable and accrued interest totaling \$133,247 were outstanding at December 31, 2002.

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During 2003 \$130,150 of demand notes receivable from three directors were forgiven in recognition of previous service on the Board of Directors.

Are there certain relationships and related transactions among the Company and its Executive Officers or the Board of Directors?

Kristiania Corp. The Company currently leases from Kristiania Corp. (an affiliated entity owned by Mr. Goodlander and Mr. Goodlander's children), as a tenant under a non-cancelable, five year, triple-net lease that was entered into as of December 1, 2000, a 35,000 square foot facility that is occupied by its research and development and office operations in Nashua, New Hampshire. The lease provides for monthly rental payments of \$25,000 commencing in January 2001, which lease payments are increased annually based upon changes in the consumer price index. The Company paid annual rentals of \$311,904, \$304,655 and \$300,000 in 2003, 2002, and 2001, respectively.

Related Party Debt. Since the inception of the Company, Mr. Goodlander has made cash loans to the Company. The aggregate amount owing to Mr. Goodlander at the end of fiscal years 2003, 2002 and 2001 was \$487,899 in 2003 and 2002 and, \$810,000 in 2001. The debt is unsecured, and \$387,899 bears interest at prime plus 1% and \$100,000 bears interest at 6% and is convertible into common stock of the Company at \$4.00 per share.

In August 2003 Mr. Goodlander, through an affiliate (Kristiania Corp.) of the Company controlled by him, began advancing funds to supplement the Company's cash flow for operating expenses and occupancy costs until operating cash flows improve and permanent additional financing can be arranged. Originally such advances were unsecured, due upon demand and accrue interest at the affiliate's cost of funds. Subsequently, the Board of Directors, with Mr. Goodlander abstaining, approved the Company formalizing the agreement with the affiliate in the form of a \$500,000 line of credit, of which \$358,285 was outstanding at December 31, 2003, secured by all the assets of the Company with interest at the affiliate's cost of funds which is currently 21% and a one year term renewal by mutual agreement of the parties.

John Thonet resigned his position as a director of the Company on April 30, 2003. At the time of his resignation, the Company owed Mr. Thonet a balance of \$177,101 plus accrued and unpaid interest on a note payable representing the balance of sums advanced by him to CyberStorage Systems that was acquired by the Company in 2000, and Mr. Thonet was due \$156,333 in accrued and unpaid salary by CyberStorage Systems. The Company also had a demand note receivable due from Mr. Thonet of \$44,729 plus accrued interest. On April 30, 2003, the Company and Mr. Thonet agreed to offset the note receivable and accrued interest against the note payable and accrued interest and Mr. Thonet agreed to accept a cash payment of \$40,000 in exchange for cancellation by him of the balance of the note payable. In addition, Mr. Thonet gave up any and all claims to accrued and unpaid salary and any other amounts due to him as of that date in exchange for the extension of period for exercise of his vested stock options to purchase 62,500 shares of common stock until May 1, 2004.

Stock Purchase Loans. In August 2001, the Company's Board of Directors approved the issuance of advances secured by demand notes receivable with interest at prime plus 1% to Messrs. Gauld, Gardner, Thonet and Hood, for the purpose of purchasing the Company's common stock in the public market with no single director or executive officer having more than \$50,000 outstanding. Mr. Thonet's note was settled as described in the immediately preceding paragraph. In May 2003, Messrs. Gauld and Gardner's notes were forgiven as described above under the caption How are the directors compensated. Mr. Hood's note was repaid in May 2003.

How often did the Board of Directors meet during fiscal year 2003?

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The Board met four times during 2003. Each director attended at least an aggregate of 75% of the meetings of the Board of Directors and Committees on which he served. In addition the Board took action by written consent five times.

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What committees has the Board of Directors established?

The Board of Directors has standing Audit and Compensation Committees.

Audit Committee. The Audit Committee of the Board of Directors oversees the accounting and financial reporting processes of the Company and reviews the results and scope of the audit and other services provided by the Company's independent auditors. The Audit Committee met four during 2003. The current members of the Audit Committee are Roger E. Gauld (chairman of the Audit Committee), Steven Chen and Thomas A. Wooters.

Compensation Committee. The Compensation Committee makes recommendations concerning salaries and incentive compensation for employees of, and consultants to, the Company and administers the Company's stock option plans and deferred compensation plan. The Compensation Committee met once during 2003. The current members of the Compensation Committee are Edward A. Gardner and Thomas A. Wooters (Chairman of the Compensation Committee).

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Report of the Audit Committee

The following report of the Audit Committee 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 of 1934, except to the extent the Company specifically incorporates this Report by reference.

The Audit Committee of the Board of Directors consists of three directors, each of whom is independent as defined by Section 121(A) of the American Stock Exchange's listing standards. The Audit Committee operates under a written charter that was approved by the full Board on June 9, 2000, and amended by the full Board on August 7, 2000 and May 15, 2003. The Audit Committee charter, as currently in effect, is attached to this proxy statement as Exhibit A. As set forth in more detail in the charter, the Audit Committee's primary responsibilities fall into three broad categories:

First, the Committee oversees that management has maintained the reliability and integrity of the accounting policies and financial reporting disclosure practices of the corporation;

Second, the Committee oversees that management has established and maintained processes to assure that an adequate system of internal control is functioning with the Corporation.; and

Third, the Committee oversees that management has established and maintained processes to assure compliance by the Corporation with all applicable laws, regulations and corporate policy.

The Committee has implemented procedures to ensure that during the course of each fiscal year it devotes the attention that it deems necessary or appropriate to each of the matters assigned to it under the Committee's charter. To carry out its responsibilities, the Committee met four times during fiscal 2003.

On March 19, 2004 after discussions between our management and BDO Seidman L.L.P. (BDO) it was mutually agreed that BDO would no longer serve as our independent auditor. The decision was approved by the Audit Committee of our Board of Directors.

BDO's reports on the financial statements for our most recent two fiscal years ended December 2001 and 2002 did not contain an adverse opinion or disclaimer of opinion, nor were they qualified or modified as to uncertainty, audit scope or accounting principles. During our two most recent fiscal years ended December 31, 2001 and 2002, and through March 26, 2004, there were no disagreements with BDO on any matter of accounting principles or practices, financial statement disclosure or auditing scope and procedure, which disagreement, if not resolved to the satisfaction of BDO, would have caused BDO to make reference to the subject matter of the disagreement(s) in connection with its report. None of the reportable events as defined in paragraph (A) through (D) of Item 304(a)(1)(v) of regulation S-K occurred during our two most recent fiscal years ended December 31, 2001 and December 31, 2002, and through March 26, 2004.

We have provided BDO with a copy of the above disclosure as it appeared in our Form 8K filing. A copy of BDO's letter dated March 25, 2004 stating its agreement with the above is filed in our Form 8K filing as exhibit 16.1.

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We have engaged Sullivan Bille PC (Sullivan Bille) as our new independent auditor, effective March 19, 2004. The decision to engage Sullivan Bille was recommended by the Audit Committee of our Board of Directors and was approved by our Board of Directors.

During our two most recent fiscal years ended December 31, 2001 and December 31, 2002, and the subsequent interim period commencing December 31, 2002 we did not consult with Sullivan Bille regarding any matters or events set forth in Item 304 (a)(2)(i) and (ii) of regulation S-K.

In overseeing the preparation of the Company s financial statements, members of the Committee met with both management and the Company s outside auditors to review and discuss all financial statements prior to their

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issuance and to discuss significant accounting and disclosure issues. Management advised the Committee that all financial statements were prepared in accordance with generally accepted accounting principles, and the Committee discussed the statements with both management and the outside auditors. The Committee's review included discussion with the outside auditors of matters required to be discussed pursuant to Statement on Auditing Standards No. 61 (Communication With Audit Committees).

With respect to the Company's outside auditors, the Committee, among other things, discussed with Sullivan Bille PC matters relating to the auditors independence, and has received the written disclosures and letter from Sullivan Bille PC as required by the Independence Standards Board Standard No. 1 (Independence Discussions with Audit Committees).

On the basis of these reviews and discussions, the 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 fiscal year ended December 31, 2003, for filing with the Securities and Exchange Commission. In addition, the Committee recommended to the Board of Directors the appointment of Sullivan and Bille, PC as the Company's independent auditors for fiscal year 2004.

Members of the Audit Committee

Roger E. Gauld, CPA, Chairman of the Audit Committee (Independent)

Steven Chen (Independent)

Thomas A. Wooters, Esq. (Independent)

Table of Contents**EXECUTIVE COMPENSATION****Summary Compensation Table**

The following table sets forth certain information with respect to the compensation paid or accrued by the Company for services rendered to the Company by its Chief Executive Officer and Chief Financial Officer (the only other executive officer in fiscal year 2002 whose total salary and bonus exceeded \$100,000) for the fiscal years 2001, 2002 and 2003:

Name and Principal Position	Fiscal Year	Annual Compensation		Long Term Compensation	
		Salary	Bonus	Awards Securities Underlying Stock Options	All Other Compensation
	(1)	\$	\$	(#)	\$(2)
Theodore J. Goodlander, Chief Executive Officer and President (President as of August 28, 2002)	2003	\$ 131,250			
	2002	\$ 131,260			
	2001	\$ 200,000			
Peter N. Hood, Chief Financial Officer (as of May 8, 2000) Mr. Hood Resigned on February 2, 2004.	2003	\$ 97,626			
	2002	\$ 130,000(3)	\$ 8,270(3)		
	2001	\$ 130,000			

- (1) The Company's fiscal year ends on the last day of December.
- (2) In accordance with the rules of the Securities and Exchange Commission, other compensation in the form of prerequisites and other personal benefits has been omitted because such prerequisites and other personal benefits constituted less than the lesser of \$50,000 or ten percent of the total annual salary and bonus reported for the executive officer during the fiscal year ended December 31, 2003.
- (3) The bonus amount in 2002 was in connection with Mr. Hood's participation in the Company's 2002 Short-Term Deferred Compensation Plan under which salary of \$29,792 and bonus of \$8,270 were accrued and deferred at December 31, 2002. In 2003 Mr. Hood was paid the amounts accrued at December 31, 2002 plus an additional \$3,668.00 for 2003. The deferred compensation is reflected in salaries for the applicable years. The Short-Term Deferred Compensation Plan is no longer in effect.

Aggregated Option Exercises In Last Fiscal Year And Fiscal Year-End Option Values

Name	Number Of Securities		Value Of Unexercised In-The-Money Options At Year-End(2)	
	Underlying Unexercised Options At Year-End(1)			
	Exercisable	Unexercisable	Exercisable	Unexercisable
Theodore J. Goodlander	0	0	0	0
Peter N. Hood(3)	75,000	25,000	0	0

- (1) No options were exercised during the year ended December 31, 2003 by the Named Executive Officers.

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- (2) Based on the difference between closing price of the underlying shares of common stock on December 31, 2003 as reported by the American Stock Exchange (\$0.36) and various option exercise prices.
- (3) Mr. Hood was granted 30,000 options to purchase shares of the Company's common stock in May 2000, exercisable at \$6.625 per share and was granted 70,000 options to purchase shares of the Company's common stock in December 2000, exercisable at \$4.00 per share. Mr. Hood's options were repriced to \$1.37 per share in July 2002. Mr. Hood's options were cancelled upon his resignation on February 2, 2004.

Table of Contents**10-Year Option / SAR Repricings**

<u>Name</u>	<u>Date</u>	<u>Number of Securities Underlying Options/SARs Repriced or Amended(#)</u>	<u>Market price of Stock at Time of Repricing or Amendment(\$)</u>	<u>Exercise Price at Time of Repricing or Amendment(\$)</u>	<u>New Exercise Price(\$)</u>	<u>Length of Original Option Term Remaining at Date of Repricing or Amendment (Months)</u>
Peter N. Hood,	July 19, 2002	30,000	\$ 1.37	\$ 6.625	\$ 1.37	94
Chief Financial Officer,	July 19, 2002	70,000	\$ 1.37	\$ 4.00	\$ 1.37	101

Equity Compensation Plan Information

<u>Plan Category</u>	<u>Number of securities to be issued upon exercise of outstanding options, warrants and rights(1)</u>	<u>Weighted-average exercise price of outstanding options, warrants and rights(1)</u>	<u>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column(a)(1))</u>
Equity compensation plans approved by security holders:			
1994 Amended and Restated Stock Incentive Plan(2)	286,407	\$ 1.21	240,660
1999 Stock Incentive Plan	1,516,700	\$ 1.36	432,587

(1) Information is as of the most recently completed fiscal year ended December 31, 2003.

(2) The 1994 Amended and Restated Stock Incentive Plan is intended to promote the long-term