COMPUTERIZED THERMAL IMAGING INC
Form 10KSB
October 31, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-KSB

(Mark One)

|X| ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE FISCAL YEAR ENDED JUNE 30, 2005

|_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER 1-16253

COMPUTERIZED THERMAL IMAGING, INC.
(Exact name of registrant as specified in its charter)

NEVADA (State or other jurisdiction of incorporation or organization)	87-0458721 (I.R.S. Employer Identification No.)
1719 West 2800 South, Ogden, UT (Address of principal executive offices)	84401 (Zip Code)

Registrant's telephone number including area code: (801) 776-4700

Securities registered under Section 12(b) of the Act:
None
Securities registered under Section 12(g) of the Act:
Common Stock
(Title of class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the 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 |X| No |_|

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. |_|

Revenues of the registrant for its most recent fiscal year were $235,972.

The aggregate market value of Common Stock held by non-affiliates of the registrant at October 1, 2005 was approximately $14 million. Shares of Common Stock held by each officer and director and by each person who owns 5% or more of the outstanding Common Stock have been excluded from this computation in that such persons may be deemed to be affiliates.

As of October 12, 2005, there were 114,561,698 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE
None

COMPUTERIZED THERMAL IMAGING, INC.

FORM 10-KSB

ANNUAL REPORT

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PART I

THIS DOCUMENT, INCLUDING, BUT NOT LIMITED TO, CERTAIN STATEMENTS CONTAINED IN ITEM 1, "DESCRIPTION OF BUSINESS" AND ITEM 6, "MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS," CONTAINS FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF THE SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), AND SECURITIES EXCHANGE ACT OF 1934, AS AMENDED. FORWARD-LOOKING STATEMENTS INVOLVE KNOWN AND UNKNOWN RISKS, UNCERTAINTIES AND OTHER FACTORS WHICH MAY CAUSE OUR ACTUAL RESULTS, PERFORMANCE OR ACHIEVEMENTS TO BE MATERIALLY DIFFERENT FROM ANY FUTURE RESULTS, PERFORMANCE OR ACHIEVEMENTS EXPRESSED OR IMPLIED. WHEN USED IN THIS DOCUMENT THE WORDS "EXPECTS," "ANTICIPATES," "INTENDS," "PLANS," "MAY," "BELIEVES," "SEEKS," "ESTIMATES" AND SIMILAR EXPRESSIONS GENERALLY IDENTIFY FORWARD-LOOKING STATEMENTS. ALL FORWARD-LOOKING STATEMENTS INCLUDED IN THIS DOCUMENT ARE BASED ON INFORMATION AVAILABLE TO US ON THE DATE HEREOF, AND WE ASSUME NO OBLIGATION TO UPDATE ANY FORWARD-LOOKING STATEMENT, EXCEPT AS OTHERWISE REQUIRED UNDER APPLICABLE LAWS AND REGULATIONS.

THIS DOCUMENT SHOULD BE READ IN CONJUNCTION WITH OUR AUDITED FINANCIAL STATEMENTS INCLUDED IN PART II BELOW AND "RISK FACTORS" NOTED BELOW.

ITEM 1. BUSINESS

INTRODUCTION

Computerized Thermal Imaging, Inc. ("WE," "US," "CTI," or the "COMPANY") designs, manufactures and markets thermal imaging and infrared devices and services used for clinical diagnosis, pain management and non-destructive testing of industrial products and materials. We have historically developed, manufactured and marketed the following principal products:

- BREAST IMAGING: We are seeking pre-market approval from the U.S. Food and Drug Administration (the "FDA") of our breast imaging system, called the BCS 2100(TM), which, if approved and marketed, we believe will assist radiologists in their efforts to distinguish between benign and malignant breast masses. On January 23, 2003, the FDA declined to grant pre-market approval for the BCS 2100 and recommended additional data analysis, clinical trials and other steps that we might take to obtain FDA approval. As explained in greater detail in "Government Regulation--Pre-market Approval of the BCS 2100" beginning on page [15] below, we do not currently have the resources necessary to conduct the additional clinical studies requested by the FDA, but we are seeking to persuade the FDA to grant pre-market approval based on our existing data. Unless and until we receive final or conditional

approval of the BCS 2100, we cannot sell, market or distribute the BCS 2100 in the United States, and lack of FDA approval significantly hinders marketing of this product in international markets. In April 2004, we received a Medical Device License from Health Canada to market the BCS 2100 in Canada. In late August 2004, we shipped a BCS 2100 to Ville Marie in Montreal, Canada for a short term evaluation. The BCS did not fit into Ville Marie's procedures and protocol. The BCS has been returned to the our plant. We are also pursuing other potential customers in Canada.

- PAIN MANAGEMENT--PHOTONIC STIMULATOR: Our Photonic Stimulator emits infrared light that penetrates the skin in an effort to promote increased blood flow and circulation in order to provide temporary relief of minor aches and pains where heat is indicated.

- PAIN MANAGEMENT--THERMAL IMAGE PROCESSORS: Our Thermal Image Processor (or "TIP,") uses the same infrared camera as the BCS 2100 to measure body heat naturally radiated by the patient as he/she stands (or sits) before the camera. The heat-measuring capabilities of the TIP are generally used to develop a physiological profile of a patient to assist in the diagnosis and treatment of a wide range of physiological and circulatory abnormalities, principally soft-tissue related injuries and pain. The TIP may also have application as a pre-screening device to identify persons with increased skin temperature at international ports of entry and other public facilities.

- TURBINE BLADE INSPECTION SYSTEM: Our Turbine Blade Inspection System (the "TBIS") is a quality assurance tool which, using techniques similar to our BCS 2100, meets industrial requirements for non-destructive testing and examination of turbine blades used in aircraft and power generation, and other industrial components, composite materials and metals.

We manufacture our products internally at our Ogden, Utah facility. Our Ogden facilities are certified to ISO 9000 quality standards. Our common stock is quoted on the Over-the-Counter Bulletin Board or "OTCBB" under the symbol "CIOB." As of October 1, 2005, we had approximately 114 million shares of common stock outstanding held by approximately 1,562 shareholders of record. In addition to the outstanding shares of our common stock, there are outstanding exercisable warrants and options to acquire approximately 4.5 million shares of our common stock at exercise prices ranging from $0.10 to $2.27. Of the approximately 119 million fully-diluted shares of our common stock outstanding, 14 million shares are beneficially owned by insiders and affiliates. Other than our wholly-owned subsidiary, Bales Scientific, Inc., we have no interest in any other entity.

We are a development stage company and, to date, we have funded our business activities with funds raised through the private placement of common stock, debt and warrants, the exercise of warrants and options and limited revenues from product sales and licenses. We currently face substantial financial challenges. For each of the past four years, our auditors have issued their report with a going concern qualification, reflecting their assessment that we do not possess the resources necessary to continue as a going concern through the end of the applicable fiscal year. We have substantially reduced our operations, and will not be able to continue our limited operations without a substantial capital infusion. Therefore we are seeking cash from either a

private placement of equity or debt.

INDUSTRY OVERVIEW & TRENDS

The American Cancer Society estimated in 2003 that 211,300 new cases of invasive breast cancer would be diagnosed among women and an estimated 39,800 women in the United States would die from the disease during 2003. Except for skin cancer, breast cancer is the most commonly diagnosed cancer among American women, accounting for nearly one of every three new cancers diagnosed, and is the second leading cause of cancer death (after lung cancer). According to information compiled by Atairgin, a biotechnology company dedicated to improving the quality of care in women's health, each year more than 20 million women in the United States have a mammogram to screen for breast cancer. Approximately two million of those mammograms require additional follow-up due to a suspicious finding, and approximately 1.3 million abnormal mammograms require a breast biopsy to characterize the suspicious tissue as benign or malignant. The statistics compiled by Atairgin also indicate that approximately 20% of the suspicious tissues that are subjected to biopsies will turn out to be cancerous. In other words, more than 80% of these breast biopsies performed during 2002 were expected to yield benign results.

According to Atairgin's statistics, of the 1.3 million breast biopsies performed in the United States each year, approximately 800,000 are open surgical procedures where the patient is anesthetized or heavily sedated and a surgeon extracts the mass through an incision. The remaining approximately 500,000 biopsies are less invasive "core" biopsies, where a needle is guided to the region of interest and a sample is obtained without having to perform open surgery. We believe the trend is toward less invasive biopsy methods in an effort to reduce scaring, cost and emotional trauma.

If we receive pre-market approval from the FDA for our BCS 2100, we believe that, under prescribed circumstances, radiologists and surgeons will be able to use the physiological profile of the suspicious tissue produced by our BCS 2100 to determine whether breast masses are benign, without performing a biopsy. The target users of the BCS 2100 are the more than 10,000 certified mammography centers in the United States and more than 10,000 mammography centers throughout the rest of the world.

The primary target markets for our pain management products consist of over 50,000 chiropractors, pain management practitioners, occupational therapists, physical therapists and major sports teams in the United States looking for ways to diagnose and treat injuries and pain conditions effectively and quickly. Various reports estimate the number of Americans suffering from chronic pain at between 50 million and 80 million, and estimate that an additional 25 million Americans suffer acute injury-related pain, costing the United States economy between $50 billion and $100 billion annually in missed work days, emergency room visits, medications and other costs.

The primary target market for our industrial products is manufacturers of complex castings, particularly in the aerospace and power generation markets.

OUR PRODUCTS AND SERVICES

We have developed six significant proprietary technologies, four of which relate to the BCS 2100: 1) a climate-controlled examination unit to provide patient comfort and facilitate reproducible tests for the BCS 2100; 2) an imaging protocol designed to produce consistent results for the BCS 2100; 3)

a statistical model that detects physiological irregularities for the BCS 2100; 4) infrared imaging and analysis hardware, including our proprietary heat-sensing camera, which is used in the BCS 2100 as well as our pain management and industrial systems (collectively, we refer to items 2-4 as our "Thermal Imaging Process"); 5) a system to treat pain and other symptoms of diseases that restrict blood flow, which is used in the Photonic Stimulator; and 6) the TBIS.

Medical Products - BCS 2100

Our BCS 2100 provides a non-invasive, painless method to collect information that could supplement the information provided by mammograms for the evaluation of suspicious breast lesions. To receive a breast scan on the BCS 2100, a patient would lie face down on our device and expose one breast at a time to the flow of cold air. The breast is then observed by our infrared imager as it cools. Because malignant tissue is more vascular and less likely to constrict upon contact with cool air than benign tissue, malignancies are measurably warmer than benign tissue. The BCS 2100 captures 103 dynamic images of each breast and analyzes over 8.3 million temperature values per breast to measure minute changes in physiological and metabolic activity. From these measurements, the BCS 2100 is able to compute a mathematical probability and indicate the likelihood that a suspicious breast lesion is benign or malignant. We believe that this data, when combined with diagnostic information from mammograms, will provide radiologists with additional information that can be useful in determining more precisely when a surgical biopsy is needed.

Mammography and related imaging methods capture a snapshot of anatomical structure at a moment in time, but do not provide information about the behavior of the structures exposed. While mammography may detect the presence of an abnormality in the breast, a biopsy is required to determine whether the abnormality is benign or malignant. We believe our technology produces images that expose the physiology and function of breast tissue. If we receive FDA approval for the BCS 2100, we believe this physiological information can provide health professionals with a tool for more accurately discriminating between those cases that require invasive biopsy and those that do not; furthermore, we believe our BCS 2100 will be able to provide physiological data that can lead to fewer biopsies, 80% of which have benign findings.

We believe the BCS 2100 provides a tool that could detect cancer in almost all types of abnormal breast lesions: masses, micro-calcifications and architectural distortions. In our clinical trials, where BCS 2100 findings were confirmed by biopsy, we detected malignancy 96.4% of the time when cancer was present, and we believe we can improve this overall sensitivity with additional clinical research studies and statistical software development.

Our best sensitivity is with lesions classified as masses. According to our clinical trials, where BCS 2100 results were confirmed by biopsies, our BCS 2100 detected cancer in lesions described as masses 99.3% of the time when cancer was present. This means the BCS 2100 has a false negative rate of less than 1%. Our pre-market approval application addresses efficacy for all breast lesions, but later amendments and panel presentations focused on lesions described as "masses," which represent about half of all anomalies noted on mammograms referred for biopsy, and where the BCS 2100 had the best clinical sensitivity. If utilized as a decision tool, excluding all other factors, procedures and tests, we believe the BCS 2100 would have resulted in the deferral or avoidance of 19.2% of biopsies in women who had masses detected on

their mammograms. The efficacy data presented shows a false positive rate (cases where results from the BCS 2100 indicated the possible presence of cancer when none existed) approximately 80% of the time when cancer was not present. We believe that ongoing clinical research and future developments in the software algorithms (statistical models), as part of the product maturation process and under FDA-approved procedures, will enable the BCS 2100 to safely achieve significantly lower false positive rates, thereby leading to higher biopsy avoidance rates.

We view biopsy as the direct competition for the BCS 2100. According to the American College of Radiology, the average breast biopsy costs between $1,000 and $3,000 per patient. We believe that a breast scan on the BCS 2100 would cost a fraction of the cost of a biopsy and avoid the pain, risk of infection and other complications arising from an invasive surgical procedure.

We have not received FDA pre-market approval for the BCS 2100 and, accordingly, are not presently permitted to market, sell or distribute the BCS 2100 in the United States. Medical device marketing and distribution efforts rely upon building relationships with other manufacturers (strategic alliances), equipment dealers, physicians and clinical investigators. Local distributors tend to have the essential relationships with hospitals that are difficult to duplicate with a captive sales force. In the hope of possibly obtaining FDA approval, we have initiated relationships with distributors who have established relationships in the radiology and medical imaging communities. Such persons have not, however, initiated efforts to market or sell the BCS 2100. We presently anticipate that unless and until we obtain FDA pre-market approval of the BCS2100, our marketing activities in the United States will be limited to our attendance at industry trade shows and professional conferences where we can present product information in an educational format to radiologists. The lack of FDA approval, and our resulting inability to market, sell or distribute the BCS 2100, among other factors, have limited our ability to generate revenues at a level that would sustain our business operations. Due to our financial difficulties, we have substantially curtained our operations, including substantially all of our manufacturing, research and development, sales and marketing and regulatory compliance activities..

Medical Products - Pain Management

We market two pain management devices used for diagnostic imaging and therapeutic treatment, the TIP and the Photonic Stimulator.

The TIP falls into a class of devices that the FDA permits to be marketed within the limitations of the following identification:

> A telethermographic system for adjunctive diagnostic screening for detection of breast cancer or other uses in an electrically powered device with a detector that is intended to measure, without touching the patient's skin, the self-emanating infrared radiation that reveals the temperature variations of the surface of the body. This generic type of device may include signal analysis and display equipment, patient and equipment supports, component parts, and accessories.

The TIP uses the same infrared camera as the BCS 2100 to measure body heat naturally radiated by the patient as he/she stands (or sits) before the camera. The heat-measuring capabilities of the TIP are generally used by our customers to develop a physiological profile of a patient to assist in the

diagnosis and treatment of a wide range of physiological and circulatory abnormalities, principally soft-tissue related injuries and pain. We have not conducted clinical studies confirming the effectiveness of the TIP for any specific uses.

The TIP system competes indirectly with x-ray, computed tomography, ultrasound and magnetic resonance imaging ("MRI"). Medical practitioners typically view imaging technologies as elements of a toolkit, each uniquely suited for the diagnosis of a specific problem or problems. The TIP also competes against infrared cameras available in the aftermarket and marketed by several direct competitors.

The outbreak of Sudden Acute Respiratory Syndrome ("SARS") in recent years provided a new opportunity for employing the TIP as a pre-screening device at international ports of entry and other public facilities; e.g., train stations and airports. The TIP is not designed or calibrated to screen for SARS; however, the TIP is designed to provide an accurate reading of surface skin temperature. One of the outward symptoms of SARS (along with the common cold, flu and numerous other ailments) is elevated skin temperatures. The TIP can be used to identify persons with increased skin temperature, who would then be identified for further, more accurate and invasive testing procedures that could determine if the person is infected with SARS.

We have not marketed or sold any TIPs in the United States to entities that have expressed their intent to use the TIP as a pre-screening device for SARS. Because we have not sought or received pre-marketing approval of the TIP as a SARS screening device, we are not permitted to make claims that the TIP is effective as a SARS screening device. We may, however, make claims that the TIP is effective in reading surface skin temperatures. As described above, certain government authorities may find the ability of the TIP to detect elevated skin temperature useful in identifying symptoms that are consistent with (but not definitively indicative of) SARS or other diseases.

We have sold TIPs for pre-screening use into the People's Republic of China, and we are participating in a Canadian program to evaluate the use of infrared imaging for airport passenger screening. While these activities appear positive, we are uncertain whether SARS screening procedures using the TIP, or a competing thermal imaging device, will be adopted on a widespread basis. If adopted, we are uncertain that the TIP would be selected over alternative devices, which may be more suitable for such purpose.

The current suggested retail price for the TIP is $55,000. Our average selling price for new equipment during fiscal 2004 was $31,250 and during fiscal 2003 was $43,800. Our average selling price for reconditioned TIP is $28,000. Although we believe our TIP system competes favorably with aftermarket and other direct offerings in terms of capability and price, we expect TIP system prices to decline over time as a result of increased competition. This past fiscal year we did not sell any new or used TIP systems, much due to the reduced sales force and our financial status.

A complementary infrared light therapy device, our Photonic Stimulator, is a hand-held device that emits infrared energy which penetrates the skin to stimulate blood flow and promote circulation. The Photonic Stimulator falls into a class of devices that the FDA permits to be marketed within the limitations of the following identification:

An infrared lamp is a device intended for medical purposes that emits energy at infrared frequencies (approximately 700 nanometers to 50,000 nanometers) to provide topical heating.

In addition to its general classification, an approval statement of specifications attached to the authorization received from the FDA states: "The

Photonic Stimulator emits infrared light that penetrates the skin to promote increased blood flow and circulation, thereby providing safe, temporary relief of minor aches and pains where heat is indicated."

We believe the infrared light-focusing capabilities of the Photonic Stimulator are generally used by our customers to treat general aches and pains. Published reports written by practitioners who use the Photonic Stimulator indicate that infrared light therapy is also used in an attempt to promote circulation and speed healing. We have not conducted clinical studies confirming the effectiveness of the Photonic Stimulator for any specific uses.

The Photonic Stimulator competes with therapeutic ultrasound, electrical stimulation and newly-approved laser light therapy devices. The current suggested retail price of our Photonic Stimulator is $4,995. Our average selling price during 2005 was $3,593, during 2004 the average was $2,600, and during 2003 it was $2,130. We expect Photonic Stimulator resale prices to remain at current levels for the foreseeable future as we continue our efforts to expand unit volume and compete with other light therapy devices as light therapy becomes more accepted.

In order for us to expand our pain management segment, there must be increased market adoption of both the TIP and the Photonic Stimulator based on customer referrals, testimonials, and published third-party research in order to build credibility of products and earn expanded indications for use of the devices from the FDA. The adoption of new products may be adversely affected by general economic conditions, changes in insurance coverage offered by private insurers in response to the general economy and new competitive offerings. We cannot guarantee that customers will accept our products, or that we will be able to profitably manufacture and sell these products.

Until recently, pain management product marketing has relied upon trade advertising, word-of-mouth recommendations, public relations and media outreach, trade show attendance, direct and channel sales, and educational seminars, where products are demonstrated to groups of potential customers. Due to the company's financial condition this past year, we have relied on word-of-mouth recommendations and our website for marketing. We have held user group meetings and worked with our current customer base to place articles and provide testimonials about how our pain management devices have impacted their practices and improved the condition of their patients.

In an effort to develop credibility in the marketplace, and to obtain additional market exposure, we have developed relationships with pain management dealers in California, Texas, Florida, New England and Asia who have established relationships and reputations in these markets.

Industrial - Non-Destructive Testing Products

Bales Scientific, Inc. ("Bales Scientific"), our wholly-owned subsidiary, provided industrial test services and has, for many years, designed and sold industrial test systems to customers who desire to perform their own testing. Our industrial non-destructive testing product focus has been the analysis of turbine blade defects. Turbine blades are very complex cast parts used in aircraft, power generation, pumps and compressors. Using techniques similar to those employed by our BCS 2100 and the infrared camera used in the BCS 2100 and TIP products, our TBIS creates thermal stress by rapidly heating a component, collecting a series of images as the component returns to ambient

temperature, and then analyzing these images to determine the presence or absence of characteristics determined to correlate with certain manufacturing and usage-induced defects. The analysis identifies defects, abnormalities and flaws in the test material. This system can identify blockages in cooling holes as small as the diameter of a human hair. We believe that this technology is uniquely capable of testing turbine blades automatically, quickly, inexpensively and without destroying or compromising the blade part. During the third quarter of fiscal 2003, to reduce cash outlays, we relocated this activity to our Ogden, Utah facility and closed the operations formerly conducted by Bales Scientific in Walnut Creek, California.

The turbine blades tested using our TBIS include aircraft turbines employed in military aircraft, and electrical power turbines. TBIS sales have long lead times and require significant integration into the customer's production systems. TBIS sales have been infrequent, are dependent upon the health of the aerospace industry and general economic conditions, and there may be relatively few customers for this device.

TBIS base systems are generally priced in a range between $350,000 and $450,000 and compete with industrial x-ray, ultrasound and other technological approaches. The TBIS provides a safe, effective and hygienic approach to locating product defects, and requires no disposable supplies; i.e., x-ray film. We also market smaller, less expensive systems utilizing our TIP and an alternative thermal stimulus device with a suggested retail price of approximately $130,000. We market these products directly to engine and power system manufacturers and other industrial customers. These products typically have long sales cycles, and demand is directly impacted by general economic conditions.

PATENTS

As of June 30, 2005, we had the following patents or patent applications pending before the United States Patent and Trademark Office:

- Patent No. 5,999,842, dated December 7, 1999, acquired by assignment from TRW on a Functional Thermal Imaging Apparatus (our BCS 2100 Patient Positioning Table). Patent No. 6,157,854, dated December 5, 2000, covering techniques designed to reduce or eliminate pain by the application of infrared therapy while monitoring the process as it is being conducted. The techniques involve
- the use of our Photonic Stimulator to apply infrared energy to a patient while using the TIP to monitor the patient's response to the therapy. Patent No. 6,366,802, dated April 2, 2002, covering techniques designed to reduce or eliminate pain by the application of infrared therapy while monitoring the process as it is being conducted. The techniques involve
- the use of our Photonic Stimulator to apply infrared energy to a patient while using the TIP to monitor the patient's response to the therapy.
- Patent No. 6,570,175, dated May 27, 2003, covering an infrared imaging arrangement for the turbine component inspection system covering the overall fixture and infrared imager arrangement
- Patent No. 6,711,506, dated March 23, 2004, covering software providing operator assistance during the use of an automated infrared inspection system of turbine components.
- Patent No. 6,750,454, dated June 15, 2004, covering software performing automated analysis of the thermal response of a turbine

component to application of thermal stimuli by an infrared inspection system.

- Patent No. 6,757,412, dated June 29, 2004, covering an algorithm used to analyze imaging data collected through our BCS 2100

- Patent application (Serial No. 60/378,764, dated May 7, 2002) for the cold stimulus turbine component inspection system

Subject to the availability of capital, we hope to pursue the registration of additional copyrights, patents and trademarks in the United States; however, we presently lack the resources to pursue any additional intellectual property protection. We believe that our patents and patent applications are valid and enforceable and provide some competitive protection for our products; however, any of our patents or other intellectual property rights may be challenged, invalidated or circumvented, or the rights granted thereunder may not provide any competitive advantage. We could also incur substantial costs in asserting our intellectual property or proprietary rights against others, including any such rights obtained from third parties, and/or defending any infringement suits brought against us. We do not currently possess the resources necessary to assert or defend our intellectual property rights. Although we generally enter into confidentiality and invention assignment agreements with our employees and consultants, there can be no assurance that we have done so with all relevant employees and consultants, that such agreements will be honored or that we will be able to effectively protect our rights to unpatented trade secrets and know-how. Moreover, there can be no assurance that others will not independently develop substantially equivalent proprietary information and techniques or otherwise gain access to our trade secrets and know-how. We may be required to obtain licenses to certain intellectual property or other proprietary rights from third parties. Such licenses or proprietary rights may not be made available under acceptable terms, if at all. If we do not obtain required licenses or proprietary rights, we could encounter delays in product development or find that the development or sale of products requiring such licenses is foreclosed.

SOURCE OF SUPPLY

Manufacture and assembly of our pain management and thermal imaging devices require standard electronic components, formed or machined metal and plastic parts, wiring harnesses, printed circuit boards and metal cases which are available from any number of suppliers with relatively short lead times. We have historically purchased certain proprietary optical components and cooling equipment from a single source, and have typically experienced; 12 to 16-week lead times. Historically, we have experienced no supply disruptions with vendors. While there are alternative sources for these products, the loss of an established vendor supplier would require that we invest time developing and certifying a new vendor. Until the new vendor is located and certified, we could experience a disruption in ability to supply TIP systems, which are a component of the BCS 2100 and our industrial products. Furthermore, due to our lack of financial resources, we have suspended our manufacturing and product sourcing activities. As a result, our vendor relationships are presently uncertain.

BUSINESS STRATEGY AND PRODUCT DEVELOPMENT

We believe our products and technologies provide a unique collection of cost-effective diagnostic, pain management and product testing solutions for medical and industrial customers. Our target customers are hospital radiology departments, cancer research facilities and imaging centers, chiropractors and

physical therapists, and manufacturers of products with complex cast components or processes.

Critical to our business strategy is to obtain the required approval from the FDA with respect to our BCS 2100 and our pain management products. As described in greater detail below under "Government Regulation," we have obtained Section 510(k) approval for our Photonic Stimulator and TIP. Section 510(k) approval permits us to market and sell such products for the uses described in the approval letter and the applicable section of the Code of Federal Regulations. As described in greater detail below, we have applied for, but have not received, pre-market approval with respect to our BCS 2100. We believe that securing pre-market approval for the BCS 2100 is essential to our efforts to develop and market the BCS 2100 because, without such approval, we will not be able to market the BCS 2100 as a breast cancer screening device in the United States, obtain insurance payment codes or develop physician acceptance of our system.

Our marketing efforts rely upon building relationships with manufacturers, local medical equipment dealers, physicians and clinical investigators. We established a medical advisory board to assist us in preparing for the FDA panel meeting and to help us devise programs and projects to facilitate acceptance in the market place. We have also attended trade shows and conferences and make direct sales calls to industrial customers and sponsor clinics, where we introduce and demonstrate our breast imaging, pain management and non-destructive testing products. We believe marketing our medical products directly and through a dealer channel, augmented with trade shows, conference presentations, direct mail and inside sales, provides a cost-effective approach to diagnostic imaging and pain management practitioners. As of August 31, 2004 our medical advisory board was dormant, we had discontinued trade show participation and had limited our marketing activities to user group meetings with current and potential customers and direct selling; however, if we are successful in securing additional capital, we plan to continue investing resources in these programs.

As with all medical devices, it is important that our BCS 2100 customers receive adequate reimbursements from third-party payers: insurance companies, Medicare and Medicaid reimbursement agencies. We applied for a reimbursement code from the American Medical Association during December 2001 for our BCS 2100. Our application will not be acted upon unless and until we receive FDA pre-market approval for the BCS 2100.

Our pain management products qualify for insurance reimbursement in most states at rates that vary on a state-by-state basis. Generally insurance providers offer coverage if the state's workers compensation scheme recommends coverage. Currently only New York, Montana and Minnesota do not recommend coverage for treatments that include infrared imaging or infrared therapy. Average reimbursement for an infrared imaging procedure with our TIP camera, in states offering reimbursement, is $198, with a high of $375 and a low of $96. Average reimbursement for an infrared treatment with the Photonic Stimulator is $12, with a high of $38 and a low of $4 per treatment.

In order to conserve cash as we seek FDA approval for the BCS 2100, we have scaled back operations and staffing levels by, among other things, reducing our research and development group from 16 full-time employees in the fall of 2002 to none in October 2005 and reducing our manufacturing group from 20 full-time employees in the fall of 2002 to one full-time employee in October 2005. In addition, we were in the process of developing temperature screening

software for the TIP to include a fever detection algorithm, color-map settings for fever threshold, reporting, and networking, but suspended development of the software in June 2003 due to lack of resources.

COMPETITION

MEDICAL IMAGING. The principal methods used to visualize internal human anatomy are x-ray, computed tomography, ultrasound and MRI. We believe many physicians view these technologies as elements of a toolkit, each uniquely suited to the diagnosis of a specific problem or problems.

Our BCS 2100 provides physiological information that supplements the anatomical information obtained from mammography and does not compete directly with x-ray, computed tomography, ultrasound or MRI. Our system is painless, requires no radioactive materials and involves no invasive technology.

Our pain management products compete with ultra-sound, electrical stimulation, newly approved laser light therapy devices and infrared cameras purchased from competitors or in the aftermarket for infrared cameras.

Our industrial applications compete with industrial x-ray, and high pressure water and air techniques; which require skilled labor, are time consuming and may utilize dangerous radiation that requires special facilities. Our TBIS provides additional defect analysis more quickly by using less skilled labor and no special environment, and may replace high pressure water and air or x-ray for certain applications.

The companies that supply diagnostic and industrial imaging equipment range from large manufacturers to smaller specialized companies. Large diversified manufacturers, for which imaging systems define only a portion of their total business, include General Electric, Siemens, Toshiba, Hitachi and Philips.

NEW TECHNOLOGIES. Digital x-ray captures images electronically and may provide several important benefits relative to existing technologies: 1) reduced radiation dosage; 2) faster access to images, which is critical for emergency room use; 3) the ability to distribute and access an image through a computer, enabling remote consultation; and 4) reductions in labor and radiographic film costs. Our BCS 2100 does not compete with digital x-ray equipment. In fact, as mammography technology improves, we believe more women will be referred for biopsies. We believe this will create a greater demand for technologies, like our BCS 2100, that may be able to determine whether a patient's mass is benign without the use of an invasive surgical procedure.

Positron Emission Tomography ("PET"), a nuclear medicine-based diagnostic imaging technique for measuring the metabolic activity of human cells, may benefit patients suffering from certain types of cancer or certain conditions affecting the brain and heart. Many insurance carriers approve PET, but the technology is expensive and difficult to administer.

Optical imaging of the breast is based on laser transillumination. This technology is under investigation as a possible approach for medical imaging, and at least one potential competitor is attempting to secure FDA approval for its version of this technology. Laser transillumination has been investigated for over 20 years and recent implementations of this technology used computed tomography to improve the results. We believe our BCS 2100 competes favorably

with this technology.

PROCEDURES. We view biopsies, either needle aspiration or open surgery, as direct competition for the BCS 2100. We believe that the BCS 2100, if approved by the FDA with the indications for use we have requested, will be adjunctive to mammography, and that every patient with an abnormal mammogram indicating a mass, who might be referred to biopsy under current protocols, will be a potential candidate for a BCS 2100 procedure. We believe that, through the product maturation process involving additional product development, we will be able to obtain expanded indications for use and effectively screen all patients referred for biopsy. To successfully market our product, which can occur in the United States only if we receive FDA approval, we will have to educate physicians about the BCS 2100 so that they will be able to recommend a BCS 2100 procedure to their patients, persuade hospitals and imaging centers to purchase the equipment and convince insurance carriers to provide reimbursement for the BCS 2100 procedure.

OUR SALES AND MARKETING STRATEGY

OVERVIEW. If we are able to generate sufficient capital to resume our operations, of which there can be no assurance, we plan to market our products with a multi-channel strategy incorporating independent distributors, direct marketing, telemarketing, the internet and corporate marketing. We plan to address the industrial market with a direct sales force augmented by distributors and dealer representatives as appropriate.

DISTRIBUTORS. Prior to substantially reducing the scope of our operations, we retained the services of distributors to market our products. If we are able to resume our operations, we currently intend to see to re-establish distributor relationships for the purpose of marketing our products. Our distributors have historically focused their efforts on a specific channel in a specific region; e.g. chiropractors and physical therapists in Northern California. We believe that distributors provide intimate local market knowledge and contacts critical to accessing hospital imaging facilities, radiologists, chiropractors and physical therapists, and local service capability. Our agreements with these distributors allow the distributor to purchase products at a discount from list price, usually 15%, and provide extended terms for an initial order of demonstration equipment, which we do not recognize as a sale until the distributor actually pays for the equipment. We retain the right to develop and service national accounts in the distributor's territory, but provide a period of limited exclusivity with regard to the distributor's own customers, which can be extended only if the distributor meets certain sales goals. In our experience, which is somewhat limited, no distributor has met these goals. We have also generally required the distributor to participate with us in certain marketing programs, such as user group meetings.

TELEMARKETING / TELESALES. We believe telemarketing/telesales provides important direct marketing, lead follow-up and customer service capability, particularly in the pain management segment. Telemarketing creates revenue through direct sales and generates leads for distributors. However, due to limited resources, our use of telemarketing and telesales has been very limited.

INTERNET. We use the internet to provide information to current and potential customers. Our web address is www.cti-net.com.

USER GROUPS AND SEMINARS. We believe meeting with our customers and potential customers at informal user conferences and training sessions provides valuable market intelligence, product use information, and assists us in selling our products. We have conducted user group meetings at various sites across the United States and by conference call. Due to our limited financial resources, we are not currently conducting any user groups or seminars.

TRADE SHOWS AND ASSOCIATIONS. From time to time, we have attended medical and industrial trade shows and presented papers at professional conferences. We believe attendance at trade shows and conferences allows us to build product awareness, demonstrate our products, educate customers and generate leads for future sales. Due to our limited financial resources, we are not currently participating in trade shows or association events.

CORPORATE MARKETING. To the extent our financial resources permit, we intend to develop product and corporate collateral materials, advertise in select trade journals, demonstrate our products and present papers, and research results at conferences and trade shows. We believe these activities have the potential to build product and corporate awareness and support our sales efforts in selected vertical markets.

SERVICE PROVIDERS AND CONTRACTOR RELATIONSHIPS

CONTRACTOR RELATIONSHIPS. Our business model relies upon contractors and suppliers to reduce our development risk and to provide necessary clinical resources. During the course of preparing our FDA pre-market approval application and conducting regular clinical studies, we engaged the services of certain contractors, including Battelle Memorial Institute, which assisted us in the preparation of regulatory submissions and provided technical consulting services, on a time and materials basis, in connection with algorithm development and statistical consultation for interaction with the FDA. We have terminated our relationship with Battelle because of a shortage of working capital. If we were to require such consulting services in the future in connection with a supplement to our pre-market approval application or otherwise, replacing Battelle would be costly and difficult (because any competing entity would be unfamiliar with our data). We hope Battelle would continue to work with us if needed in the future (if we are able to generate sufficient capital to retain Battelle), but we have no contractual commitments to that effect.

We have also used the services of Quintiles, Inc., an independent consulting firm authorized by the FDA, to verify clinical examination results, to provide clinical trial monitoring and FDA preparation support. We have terminated our relationship with Quintiles because we no longer need their services. If we were to require such consulting services in the future in connection with a supplement to our pre-market approval application or otherwise, we believe Quintiles would continue to work with us (if we are able to generate sufficient capita to retain Quintiles), but we have no contractual commitments to that effect. If we were unable to engage Quintiles again, we believe we could find alternative providers of similar services at similar rates.

CLINICAL TRIALS. Previously, we contracted with six hospitals to conduct the clinical trials reflected in our application for FDA pre-market approval of the BCS 2100. The six hospitals are:

- USC/Norris Comprehensive Cancer Center, Los Angeles;
- Los Angeles County Hospital, Los Angeles;
- Mt. Sinai Hospital, Miami;
- St. Agnes Hospital, Baltimore;
- Lahey Clinic, Boston; and
- Providence Hospital, Washington, D.C.

We do not have any ongoing contractual relationships with any of these

institutions, and no clinical trials are ongoing. We continue to have periodic contacts with officials at the USC/Norris Comprehensive Cancer Center and the Lahey Clinic, and believe that such persons would be available for consulting and other services if requested, but we have no written commitments to such effect.

CLINICAL STUDIES. Clinical studies are clinical research conducted for purposes of developing expanded indications for use, testing product enhancements, identifying potential product issues and obtaining product trials by practitioners and patients. Clinical trials are experiments where patient results are withheld from us pursuant to experimental controls designed to ensure scientific accuracy and are conducted in connection with obtaining FDA pre-market approval.

If we obtain pre-market approval from the FDA for our BCS 2100, of which we can provide no assurance, and if we are able to generate sufficient capital to continue our operations, we plan to expand our clinical studies utilizing the BCS 2100 with institutions and practitioners to obtain user feedback, test product enhancements and secure technical papers, and for training and educational marketing purposes. During 2002, we entered into a research relationship with McKay-Dee Hospital in Ogden, Utah for a study of up to 70 patients referred for biopsy of a single mass after undergoing conventional diagnostic procedures. We conducted this study to acquire information about the effectiveness of the BCS 2100 for women age 60 and over presenting with a lesion described as a mass. We ended this study during the third quarter of fiscal 2003, without conclusion, when it became apparent that the institution did not treat sufficient patients to complete the study in a timely fashion. A separate study at McKay-Dee Hospital involved 125 women to obtain baseline information regarding the characteristic thermal profile associated with normal breast tissue in women 21 and older. We concluded this study during March 2002 and are holding the data for further analysis if we receive FDA pre-market approval. We also initiated a study at Massachusetts General Hospital, Harvard Medical School's largest teaching hospital, for a clinical study involving up to 250 patients referred for biopsy of a single mass after undergoing conventional diagnostic procedures. This study was intended to acquire information to study the effectiveness of the BCS 2100 in women age 60 and under who present with a lesion described as a mass. This study is on hold, pending the FDA's final decision regarding our application for pre-market approval of the BCS 2100. These studies could provide us with an opportunity to evaluate the form and function of the BCS 2100 and develop product enhancements for next generation products. We are not currently conducting clinical studies or trials for our TIP or Photonic Stimulator.

In addition, we have utilized the services of Regulatory Insight, Inc., an independent clinical research organization, to conduct a study with our Photonic Stimulator to evaluate its effect on neck and shoulder pain after a limited course of treatment. Under our agreement with Regulatory Insight, they agreed to develop a protocol for the study, submit the protocol to the FDA for review, and conduct a study in accordance with the protocol in exchange for our payment of a fee, reimbursement of expenses and provision of training and materials. Regulatory Insight has completed their analysis of data collected, and the study is completed. We cannot guarantee customer acceptance, published results, expanded indications for use or the effectiveness of any product enhancement or protocol tested in connection with these efforts. We believe, however, these efforts are important and intend to continue this activity if we obtain sufficient capital to continue our operations.

GOVERNMENT REGULATION

OVERVIEW. Our BCS 2100, Photonic Stimulator and TIP qualify as medical devices under U.S. federal law because they are intended for use in the diagnosis, cure, mitigation, treatment or prevention of disease but do not interact chemically with the body. Medical devices are divided into three classes under FDA regulations. Low risk devices that are substantially similar to approved products already on the market are classified as Class I or Class II devices and may be marketed if approved by the FDA following submission of a fairly simple Section 510(k) filing. Sophisticated instruments that entail significant risk, or utilize unique or new technology, are classified as Class III devices and, as further described below, may not be marketed absent a comprehensive FDA review and pre-market authorization.

All Class I, II and III devices are subject to certain requirements after the marketing of the product is approved by the FDA, including rules requiring the following:

- that the manufacturer register with the FDA and list its devices with the FDA;
- that the manufacturer label the devices for their approved use and otherwise in accordance with governing rules;
- that the manufacturer maintain manufacturing processes in accordance with the FDA's regulations and prescribed procedures regarding manufacturing processes, including a quality assurance system, document control and manufacturing and design control requirements promulgated by the FDA;
- that the manufacturer report adverse events with respect to such devices and maintain a corrective and preventative action program; and
- that the manufacturer comply with certain export and import limitations.

In the event a manufacturer (including CTI) is found to be out-of-compliance with any of these regulations, the FDA may require the manufacturer to cease production and marketing until corrective measures have been implemented. The FDA also could require a product recall and could enforce civil and criminal penalties against the manufacturer, its officers and others.

Certain rules promulgated by the FDA, which relate to Class III products, do not generally relate to Class I or II products. Such rules include those mandating the following:

- that an investigational device exemption be obtained in connection with clinical studies,
- that the manufacturer adhere to specified clinical and investigational practices and procedures (called Good Clinical Practices) in connection with its studies,
- that the manufacturer obtain specified approvals from an institutional review board at each study site,
- that the manufacturer monitor, and permit the monitoring of, clinical sites and data to assure adherence to protocol,
- that the manufacturer report any adverse patient reactions that might occur in connection with its studies, and
- the manufacturer submit, as requested, to an FDA audit of clinical trials in connection with approving pre-market approval. During September 2002, the FDA conducted such an audit of our clinical trials at our Ogden, Utah, facility and concluded that our clinical trials

were conducted in compliance with FDA regulations.

Most significantly, the FDA rules related to Class III medical devices prohibit making claims of efficacy in connection with the marketing and sale of the device unless and until pre-market approval has been obtained following a determination by the FDA that the pre-marketing application contains sufficient valid scientific evidence to assure that the device is safe and effective for its intended use.

THE TIP AND PHOTONIC STIMULATOR. Our pain management products, the TIP and Photonic Stimulator, are classified for FDA purposes as Class II devices. The Photonic Stimulator received Section 510(k) approval under a generic category as "an infrared lamp .... intended for medical purposes that emits energy at infrared frequencies to provide topical heating" on April 15, 1998. Our TIP received Section 510(k) approval on April 26, 1990 under a generic category as a "telethermographic system for adjunctive diagnostic screening for detection of breast cancer or other uses in an electrically powered device with a detector that is intended to measure, without touching the patient's skin, the self-emanating infrared radiation that reveals the temperature variations of the surface of the body." As required by governing rules, each of the TIP and the Photonic Stimulator is listed with the FDA and labeled, manufactured and designed according to governing rules. We have not experienced any adverse events with respect to the Photonic Stimulator or the TIP, have not had to recall either such product and have not had any penalty or legal remedies exercised against us by the FDA with respect to such products. In connection with our export of the Photonic Stimulator and TIP to foreign countries, we have obtained (in accordance with import regulations of the destination countries) certification of United States clearance and complied with specific labeling and quality management requirements. As explained above, because the TIP and Photonic Stimulator are not Class III devices, rules related to investigational device exemptions, clinical investigator monitoring, institutional review board approval and pre-market approval do not apply to such devices.

THE BCS 2100. The BCS 2100 is classified for FDA purposes as a Class III medical device. As a result, we obtained an investigational device exemption in connection with the commencement of clinical studies on the BCS 2100. In addition, our clinical studies with respect to the BCS 2100 were subject to monitoring and conducted in accordance with Good Clinical Practices. Our clinical studies were reviewed and monitored by institutional review boards at USC/Norris Comprehensive Cancer Center in Los Angeles, Mt. Sinai Hospital in Miami, St. Agnes Hospital in Baltimore, Lahey Clinic in Boston and Providence Hospital in Washington, D.C. As described in greater detail below, we have requested from the FDA pre-market approval for our BCS 2100 but have not obtained it. Until we obtain pre-market approval for the BCS2100, we are not permitted to market or sell the device in the United States or list it with the FDA. Because pre-market approval has not been obtained, FDA rules related to listing, labeling, and manufacturing (other than design controls) do not yet apply. In addition, because we are not yet marketing the BCS 2100, we have not had any adverse events, recalls or penalties from the FDA with respect thereto. We have sold a single BCS 2100 to a purchaser in the Peoples Republic of China, and we obtained the requisite export permit with respect to such single sale.

PRE-MARKET APPROVAL OF THE BCS 2100. As noted above, we are not permitted to market the BCS 2100 or make claims of efficacy with respect thereto unless and until our application for pre-market approval is approved by the FDA. An application for pre-market approval typically contains significant clinical testing, manufacturing and other data, all of which are scrutinized by the FDA

to demonstrate the product's safety, reliability and effectiveness, and that proposed indications and conditions for use are appropriate. Only companies that are registered with the FDA can submit a 510(k) or pre-market approval application. As a registered company, we obtained the clearance necessary to conduct clinical tests and submit the request for pre-market approval of the BCS 2100 by the FDA.

For the past five years, we have pursued pre-market approval for our BCS 2100 as an adjunct diagnostic tool to mammography in patients with suspicious breast lesions that include mass being considered for biopsy. We believe pre-market approval is essential because pre-market approval 1) permits us to reference medical efficacy claims in our marketing; 2) leads to improved physician acceptance of our system; and 3) is a key step in the process of obtaining insurance reimbursement codes.

We submitted our application for pre-market approval in five modules.

Module 1 provided:

- An introduction of the use of infrared imaging, its safety and effectiveness;
- Summary of indications for use of infrared imaging as an adjunct to mammography and clinical examination in the detection of breast cancer;
- Summary of incidence, diagnosis and prognosis of breast cancer;
- Description of current modalities for detecting breast cancer;
- Description of our BCS 2100, including major components and the population for which our device has clinical utility;
- Description of our clinical trial and the population of the trial; and
- Statement of marketing of our device for its intended use.

Module 2 provided:

- A detailed description of our BCS 2100 and its component parts;
- Detailed discussion of the clinical evaluation system required to analyze and interpret the clinical data obtained through the clinical trial; and
- Documentation of all software used in our BCS 2100, including software used in the development of our system and the acquisition of data in our clinical trial.

Module 3 provided:

- Manufacturing information concerning our BCS 2100, including a detailed discussion of the facilities, personnel, equipment and controls used to manufacture our system;
- Information concerning the distribution and installation of our system; and
- A description of the procedures and record keeping associated with the manufacture, testing and installation of our device.

Module 4 reiterated certain information and provided additional information regarding:

- The safety of our BCS 2100, including all non-clinical testing of the structural and functional components of our device; and
- The safety of materials used in manufacturing our system.

Finally, Module 5 was an evaluation of our clinical trials, including the accumulation and analysis of all the clinical trials, efficacy data and an update to our indicated use as follows: "The CTI BCS 2100 is a dynamic, computerized infrared-based image acquisition device intended for use as an

adjunct to mammography in patients with suspicious breast lesions that include masses being considered for biopsy. The CTI BCS 2100 provides additional information to guide a breast biopsy recommendation."

On December 10, 2002, the FDA's Radiological Devices Panel, which is composed of independent experts, was convened by the FDA and held a public hearing to evaluate our application in order to make a recommendation to the FDA whether to approve or disapprove the BCS 2100 for its intended uses. The panel, by a vote of 4-3, recommended that the FDA not approve the BCS 2100. On January 23, 2003, the FDA concurred with that recommendation. In a letter dated January 23, 2003, the FDA identified the following reasons for its denial of the application:

- The proposed indications for use ("IFU") were revised (i.e., restricted to women with masses visible on mammography) on the basis of a retrospective analysis of the results of CTI's clinical study in the original approval dated June 15, 2001, which the FDA believed had the effect of limiting further use of the approval result for the purpose of supporting the proposed new IFU.

- The FDA concluded that the added clinical data from 69 of 275 subjects in the "post-approval" (the "PPMA") results were insufficient by themselves (i.e. too few subjects) to constitute an adequate study. The FDA concluded that combining the PPMA data with the original approval data, employing the Bonferroni correction, would be statistically inappropriate in the absence of multiple formal hypotheses.

- The FDA determined that the basis for enrollment was not consistent with the final proposed IFU. That is, the FDA believes enrollment was not limited to mammographically visible masses.

- The FDA concluded that the number of exclusions of enrolled subjects was excessive - over 50%.

In the same letter, the FDA explained that, in order to place our application for approval in approvable form, we should do the following:

- Perform a new, focused pre-market clinical study, which clearly defines the target population for the device, and strictly adhere to this definition for the enrollment of subjects.

- Before beginning the new study, revise the IFU (in particular, the target population) based on exhaustive data mining of the approval/PPMA database.

- Perform a reproducibility study that takes into account the variations that may be encountered in clinical practice. This should include such things as patient positioning, room temperature, different technologists, different radiologists (ROI selection variances), menstrual cycle, etc.

- Provide a validated quality assurance procedure that the user can perform on a daily basis to ensure that the device is performing properly. Include instructions for corrective action if it is not.

In light of our shortage of capital, we do not currently have the

resources necessary to conduct the additional clinical study requested by the FDA. We disagree with the FDA's conclusions, including the FDA's interpretation of data forming the basis for such conclusions In an attempt to secure approval without conducting the request clinical study and other tasks, we have corresponded and met face to face with the FDA's ombudsman, Deputy Commissioner, Chief Counsel and other staff on various occasions in an attempt to persuade them that the conclusions of the FDA's Radiological Devices Panel and the decision of the FDA were incorrect. We have also described our situation to government officials outside of the FDA, including the staffs of various congressmen, and asked such persons to encourage the FDA to reconsider its decision.

On March 19, 2004, we received from the FDA's Center for Devices and Radiological Health a memorandum addressing the potential bases for pre-market approval of the BCS 2100. The FDA's memorandum did not grant us pre-market approval of the BCS 2100; however, it did identify two additional approaches for obtaining pre-market approval, and indicated that, although a new clinical study would be required under either alternative approach, the number of subjects required to complete either study would be considerably less than the number of subjects that would be required to complete our pending studies.

Our management has reviewed the FDA's March 19, 2004 memorandum in an effort to determine the most efficient path to obtaining pre-market approval of the BCS 2100. We have also reviewed the FDA's alternative approaches to assess the anticipated impact of the two approaches on our ability to develop market and sell the BCS 2100, as well as the use of the BCS 2100 by our customers. We are pursuing the methods we believe to be fiscally responsible given our difficult financial situation to obtain FDA approval. Unless and until we receive approval or conditional approval), we cannot sell, market or distribute the BCS 2100 for commercial use in the United States. The BCS 2100 has been licensed for sale for commercial use in Canada and is in the approval process in China through our contracted affiliate, NanDa.

On June 30, 2004 we filed a "Citizen Petition" with the FDA contending that consideration of our application for pre-market approval was severely and improperly prejudiced because of pervasive bias against CTI by the Food and Drug Administration staff reviewers who improperly undermined the Advisory Panel's review of our application and ultimately caused the FDA to reject that application. We seek internal documents within the FDA to help us understand what prejudiced the FDA staff.

CURRENT EMPLOYEES

As of October 1, 2005, we have two full-time employees: one accounting and administrative and one manufacturing and service. Though generally categorized as mentioned, the reduced number of employees requires each employee to "cross task" in each area of operation. Consultants are used in each area when needed. None of our employees are represented by a union and we consider our employee relations to be good.

RISK FACTORS

INVESTMENT IN SHARES OF OUR COMMON STOCK IS SUBJECT TO A NUMBER OF RISK FACTORS THAT, IF REALIZED OR COME TO FRUITION, MAY ADVERSELY AFFECT OUR PROFITABILITY AND THE VALUE OF THESE SHARES WHILE HELD BY OUR SHAREHOLDERS.

OUR AUDITORS HAVE QUESTIONED OUR ABILITY TO CONTINUE OUR OPERATIONS.

For the past four years our auditors issued their audit report with a going concern qualification. This means that based on our expected cash flow from operations and our existing current assets, our auditors did not believe that we would be able to continue our operations in their current form through

the end of the applicable fiscal year. At present, we are not generating

sufficient operating revenues to offset our operating expenses. We have experienced a loss from operations in every fiscal year since our inception. As a result of these losses, we had working capital deficits throughout our 2005 fiscal year. Working capital is a measure of the amount of liquid assets an enterprise has available to build its business. Our working capital deficit is an indication that we currently lack the liquid funds required to operate our business. We can provide no assurance that we will ever generate sufficient revenues to restore our working capital or to continue our operations.

WE DO NOT CURRENTLY HAVE SUFFICIENT CAPITAL TO MEET OUR OBLIGATIONS.

As of June 30, 2005, we had $52 thousand in cash and a working capital deficit of $2.2 million. Accordingly, we did not have sufficient capital to conduct our operations or pay our debts when due. The only way we will be able to continue our business operations will be if we are able to obtain outside financing to fund our business operations and satisfy our liabilities. We hope to use a combination of equity and debt securities and instruments in order to secure additional funding; however, we do not presently have any funding or financing commitments from prospective investors or lenders, and can provide no assurance that we will be able to secure additional funding from any source or, if available, upon acceptable terms and conditions. We have actively sought to obtain funding from external sources and, except for limited circumstances we have not been successful in obtaining capital necessary to continue operations throughout the next fiscal year. We may not be able to obtain the amount of additional capital we need or may be forced to pay an extremely high price for capital. Factors which may affect the availability and price of capital include the following: o market conditions affecting the availability and cost of capital generally;

- o our financial results, particularly the absence of significant revenue;
- o our success, or lack thereof, in obtaining FDA pre-market approval of BCS 2100;
- o the amount of our capital needs;
- o the market's perception of biotechnology stocks;
- o the market's perception of our ability to generate revenues through the sale of our products and services; and
- o the price, volatility and trading volume of our common stock.

WE HAVE SUBSTANTIALLY CURTAILED OUR OPERATIONS AND MAY NEVER RESUME EXPANDED OPERATIONS

Due to our extremely limited financial resources, we have suspended substantially all of our operations. We are not currently able to pay for the employees, supplies and other resources that would be necessary for us to restore our business operations to their prior level. We currently employ only two employees, who are responsible for general and administrative matters, but have limited experience in manufacturing, marketing or distributing products like ours. As a result of our significantly reduced level of operations, our revenues have declined dramatically and we can provide no assurance that we will ever generate revenues sufficient to restore our operations to their former level. We currently lack the financial resources to expand our operations, and have no current basis to believe we will be able to attract additional capital in an amount to resume our prior level of operations.

If our losses continue and we are unable to obtain additional

third-party financing or proceeds from the sale of certain of our assets, we will likely be unable to continue our business operations, may be forced to liquidate our assets and may elect to seek protection under federal bankruptcy laws, which could adversely affect us and our shareholders.

OUR FAILURE TO OBTAIN FDA APPROVAL OF OUR BCS 2100 HAS SIGNIFICANTLY LIMITED OUR BUSINESS OPERATIONS AND COULD RESULT IN THE COMPLETE TERMINATION OF OUR OPERATIONS.

On January 23, 2003, the FDA concurred with the recommendation of its Radiological Devices Advisory Panel to decline approval of our BCS 2100. The FDA's decision, if not modified, precludes us from marketing the BCS 2100 in the United States. Since the FDA's decision, we have advocated a reversal or modification of the decision through multiple channels, but have been unsuccessful in our efforts. We may formally appeal the FDA's non-approval decision; however, an appeal would be expensive and time-consuming, and we do not presently have the financial resources to sustain our operations or pursue an appeal. We do not know whether our negotiations or any appeal we might file will be successful. There is no assurance that we will receive FDA approval. Our efforts to obtain FDA pre-market approval of the BCS 2100 have substantially depleted our financial and other resources, which have led to significant reductions in our operations and threaten our ability to fund our operations. Failure to secure FDA approval would materially reduce or eliminate the market for our BCS 2100 and could result in the complete termination of our operations.

ONGOING INVESTIGATIONS BY THE SEC AND U.S. ATTORNEY ARE CAUSING US TO INCUR SIGNIFICANT LEGAL EXPENSES, WHICH HAVE NEGATIVELY AFFECTED OUR WORKING CAPITAL, OPERATIONS AND BUSINESS PROSPECTS.

Both the Securities and Exchange Commission (the "SEC") and the U.S. Attorney's Office for the Southern District of New York are conducting investigations involving possible violations of proscriptions on insider trading by our Chairman and Chief Executive Officer. Although we believe CTI is not currently a target of the investigations, we have incurred substantial legal expenses in responding to requests for information and documents from the SEC and the U.S. Attorney, preparing for and attending depositions by our officers, conducting investigations of our own affairs, and advancing legal fees on behalf of officers who are or may be entitled to indemnification in connection with these investigations. As of June 30, 2005, we had incurred expenses of approximately $825 thousand associated with these investigations. The expenses we have incurred to date have substantially and adversely affected our limited working capital and have negatively impacted our operations and limited our efforts to raise badly needed capital. The investigations (although slowed in fiscal year 2005) are ongoing; and we anticipate that the expenses we will incur in the future will continue to adversely affect our working capital, distract management from day-to-day operations and limit our capital-raising activities, any of which may result in us having to materially reduce or terminate our operations.

WE HAVE LIMITED REVENUES FROM OPERATIONS AND MAY NEVER HAVE SUBSTANTIAL REVENUE FROM OPERATIONS.

With limited exceptions, our products have not been used in commercial applications and there is no assurance that the market will accept our products in sufficient volume to assure profitability. From inception on June 10, 1987 to June 30, 2005, we recorded accumulated operating losses as of June 30, 2005 of $97.6 million. We recorded revenues of approximately $236 thousand and $357

thousand for the fiscal years ended June 30, 2005 and 2004, respectively. We can provide no assurance that we will ever generate sufficient revenues to exceed our operating expenses. If our expenses continue to exceed our revenues, our business will fail.

FAILURE TO OBTAIN INSURANCE REIMBURSEMENT CODES FOR OUR BCS 2100 MAY MAKE THE BCS 2100 UNMARKETABLE, THEREBY ADVERSELY AFFECTING SHAREHOLDER VALUE.

Most healthcare providers, insurance companies and other third-party payers will not use or pay for the use of a medical device or a procedure unless it is has an accompanying insurance reimbursement code. In December 2001, we applied to the American Medical Association for an Emerging Technology Code, which is the first step in obtaining Medicare, Medicaid and private insurance reimbursement for procedures performed using our BCS 2100. Our application will not be acted upon unless and until we receive FDA approval for the BCS 2100. There can be no assurance that we will receive these codes, that Medicare, Medicaid or private insurers will provide reimbursement under these codes, or that our customers will find the reimbursements sufficient to warrant the use of our BCS 2100. If our customers cannot obtain adequate insurance reimbursement for their services, the market for our BCS 2100 would be reduced and this would have a material adverse effect on us and our shareholders.

WE EXPECT TO CONTINUE TO INCUR LOSSES, DEFICITS, AND DEFICIENCIES IN LIQUIDITY THAT WILL IMPAIR OUR OPERATIONS.

We must develop clinical applications, obtain regulatory approvals, market our BCS 2100, develop further applications and markets for our other products and raise operating capital in order to become profitable. There is no assurance that we will be able to accomplish these objectives. We have incurred substantial losses in the past and expect to continue to incur losses, deficits and deficiencies in liquidity due to the significant costs associated with the continuing development and commercialization of our products. From June 10, 1987 until June 30, 2005, we incurred accumulated losses of approximately $97.6 million. We recorded accumulated losses of $702 thousand and $2.5 million for the fiscal years ended June 30, 2005 and 2004, respectively. Such losses and deficiencies have had, and will likely continue to have, a material adverse impact on our operations and financial condition. Our losses have limited our operations, including our efforts to obtain critical regulatory approvals, and our product development efforts. If we continue to incur losses, our operations will be impaired and we may be unable to remain in business.

WE HAVE LIMITED MANAGEMENT AND OTHER KEY PERSONNEL, WHICH LIMITS OUR ABILITY TO EFFECTIVELY ADDRESS THE DEMANDS OF OUR BUSINESS.

During the 2005 fiscal year, key management personnel were lost due to necessary workforce reductions and resignations. During 2005 we were forced to reduce our total workforce from 6 full and part-time employees to 2 full time employees. We have not engaged a new President, nor have we replaced any of the other key personnel who resigned or were subject to our reductions in workforce. As a result of these departures, the demands on our management team and key personnel are extreme; frequently, they lack the time and resources to effectively address the demands of our business. At present we lack the financial resources to expand our management team, and do not anticipate that we will be able to attract or engage additional management or qualified key personnel in the immediate future.

WE MAY SELL ASSETS OR REDUCE ACTIVITIES TO FUND OPERATIONS, WHICH COULD

ADVERSELY AFFECT SHAREHOLDER VALUE.

If we are unable to secure adequate capital through the sales of securities, or as part of a funding arrangement, we may continue to seek raising capital by selling all or part of our intellectual property and know-how, enter into license agreements for all or part of our intellectual property rights (which might include manufacturing licenses) to third parties for certain territories or business segments, terminate operations in any of our business segments to reduce expenditures, or reduce our operations in any or all of our business segments to preserve our business until funding is available. There can be no guarantee that we will be successful in these efforts. If we are not successful, we may have to severely reduce or terminate all or some of our operations, either of which could severely reduce or completely eliminate any shareholder value.

WE HAVE TERMINATED INSURANCE POLICIES, LEAVING THE COMPANY, COMPANY OFFICERS AND DIRECTORS VULNERABLE.

Due to our lack of resources, we have terminated most of our insurance policies including directors and officers insurance, clinical trials insurance, and employee life insurance. We continue to carry minimal employee health and workers compensation coverage. The reduction in insurance policies leaves the Company, as well as our officers and directors vulnerable to claims against CTI and our directors and officers. The lack of directors and officers insurance will limit the company's ability to attract quality executives for future growth unless adequate funds are obtained to re-instate directors and officers insurance.

THE RECENT VOLATILITY IN THE MARKET PRICE OF OUR COMMON STOCK COULD CONTINUE TO ADVERSELY AFFECT SHAREHOLDER VALUE.

The market price of our common stock may continue to experience wide fluctuations, as it has in the past, which could be unrelated to our financial and operating results. Such volatility could result in a material loss in the value of an investment in our shares. Our stock price has varied between $4.97 to $.06 in the past 5 years.

	High	Low
2001	$ 4.97	$ 1.44
2002	$ 4.05	$ 0.56
2003	$ 1.29	$ 0.09
2004	$ 0.68	$ 0.06
2005	$ 0.22	$ 0.06

The price at which our common stock trades has been and will likely continue to be highly volatile and fluctuate substantially due to factors such as the following:

- General market conditions;
- Changes in or failure to meet investors' expectations;
- Speculation regarding the likelihood of success, or lack thereof, of our FDA application relating to the BCS 2100;
- Concerns related to our solvency, liquidity or cash balances;
- Actual or anticipated fluctuations in our operating results;
- Ability to meet announced or anticipated profitability goals;
- Developments with respect to intellectual property rights; and
- Announcements of technological innovations or the introduction of new

products or services by us or our competitors;

THE LISTING OF OUR COMMON STOCK ON THE AMERICAN STOCK EXCHANGE WAS TERMINATED, WHICH CREATES SUBSTANTIAL UNCERTAINTY ABOUT THE ADEQUACY AND EFFICIENCY OF THE MARKET FOR OUR COMMON STOCK.

On March 29, 2004, our common stock ceased to be traded on the American Stock Exchange ("AMEX"), due to our failure to comply with the requirements for continued listing on AMEX. Within a few months following the delistment, our common stock was quoted on the Over-the-Counter Bulletin Board Market ("OTCBB"), with the changed symbol of COIB.

The termination of our AMEX listing has created substantial uncertainty about the adequacy and efficiency of the market for our common stock. An inadequate or inefficient trading market for our common stock will likely compound the market volatility risks described in the preceding paragraphs.

WE COULD ISSUE PREFERRED STOCK AND THIS COULD HARM YOUR INTERESTS.

We have authorized 3 million shares of preferred stock, par value $5.00 per share, none of which are currently outstanding. The preferred stock, if issued, could have preferential voting, dividend and liquidation rights, which could adversely affect the rights of our shareholders. Our authority to issue preferred stock without shareholder approval could discourage potential takeover attempts and could delay or prevent a change in control through merger, tender offer, proxy contest or otherwise by making such attempts more difficult and costly. The inability of a third party to enter into such a transaction may reduce the value of our shares. In connection with our efforts to raise capital, we could sell preferred stock to an investor. While we cannot quantify the impact at this time from any such issuance, this stock could offer conversion, dividend or other rights that could significantly dilute current shareholders of our common stock.

WE RELY ON THIRD PARTIES IN THE DEVELOPMENT AND MANUFACTURE OF KEY COMPONENTS FOR OUR PRODUCTS. IF OUR PRODUCTS FAIL TO PERFORM, FDA APPROVALS, PRODUCT DEVELOPMENT, AND/OR PRODUCTION COULD BE SUBSTANTIALLY DELAYED.

We depend upon third parties to assist us with clinical studies, product development and to supply product components. Our products are highly specialized and have component parts developed and manufactured according to unique specifications. Although there may be more than one developer or manufacturer for these components, failure to develop or manufacture in a timely manner could result in a loss of business and further result in substantial delays in FDA approvals and/or commercialization of our products. Such delays could adversely affect our operations and shareholder value.

IF WE ARE UNSUCCESSFUL IN PREVENTING OTHERS FROM USING OUR INTELLECTUAL PROPERTY, WE COULD LOSE A COMPETITIVE ADVANTAGE.

Our business activities depend, in part, on our ability to use and prevent others from using our patents, trademarks and other intellectual property. We currently hold seven patents and have submitted two patent applications. There can be no assurance that the steps we have taken to protect our property will protect our rights. Defense of our intellectual property rights could be expensive and time-consuming, and parties that misappropriate our intellectual property could have significantly more financial resources than us, making it financially impossible to protect our rights.

ITEM 2. PROPERTIES

We lease facilities under two operating leases requiring fixed monthly payments, adjusted periodically over their term as follows: OGDEN, UTAH LEASE AGREEMENTS. We lease approximately 7,660 square feet of manufacturing space in Ogden, Utah, on a month-to-month basis. Monthly payments under the lease are $5,783. We also rent a storage space on a monthly basis for $80 per month. All of our operations are consolidated in the Ogden facility. We believe that our existing offices and other physical facilities are adequate for our present needs.

ITEM 3. LEGAL PROCEEDINGS

SEC AND DEPARTMENT OF JUSTICE INVESTIGATIONS

Both the Securities and Exchange Commission (the "SEC") and the U.S. Attorney's Office for the Southern District of New York are conducting investigations involving possible violations of proscriptions on insider trading by our Chairman and Chief Executive Officer. Although CTI is not currently a target of the investigations, we are incurring substantial legal expenses in responding to requests for information and documents from the SEC and the U.S. Attorney, preparing for and attending depositions by our officers, conducting investigations of our own affairs, and advancing legal fees on behalf of officers who are or may be entitled to indemnification in connection with these investigations. As of June 30, 2005, we had incurred expenses of approximately $825 thousand associated with these investigations. The expenses we have incurred to date have substantially and adversely affected our limited working capital and have negatively impacted our operations and limited our efforts to raise badly needed capital. The investigations (although slowed in fiscal year 2005) are ongoing; and we anticipate that the expenses we will incur in the future will continue to adversely affect our working capital, distract management from day-to-day operations and limit our capital-raising activities, any of which may result in us having to materially reduce or terminate our operations.

In December 2002, we were requested to provide certain documents to the SEC and the U.S. Attorney for the Southern District of New York in connection with their investigation of possible violations by our Chairman of the Board and Chief Executive Officer of the insider trading prohibitions found in the federal securities laws. During the year ended June 30, 2003 we incurred approximately $658 thousand in legal costs in complying with these requests. During the fiscal year ended June 30, 2004, we incurred approximately $168 thousand in additional legal costs associated with these investigations. For fiscal year ending June 30, 2005, legal costs held steady with little or no changes. We also may be required to indemnify our officers and directors for fees incurred for these investigations. For the year ended June 30, 2004, such indemnification obligations totaled approximately $48 thousand, and during the year ended June 30, 2005 indemnification obligations were reduced to approximately $34 thousand.

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

No matters were submitted to a vote of the security holders during the fiscal year ended June 30, 2005.

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

On March 29, 2004, our common stock ceased to be traded on the American Stock Exchange ("AMEX"), due to our failure to comply with the requirements for continued listing on AMEX. Within a few months following the delisting of our common stock on AMEX, the Over-the-Counter Bulletin Board ("OTCBB") began quotation of transactions in our common stock with the changed symbol of COIB.

Year Ended June 30, 2004	Low Bid	High Bid
First Quarter	$ 0.31	$ 0.76
Second Quarter	$ 0.19	$ 0.39
Third Quarter	$ 0.17	$ 0.58
Fourth Quarter	$ 0.06	$ 0.27
Year Ended June 30, 2005		
First Quarter	$ 0.09	$ 0.17
Second Quarter	$ 0.10	$ 0.15
Third Quarter	$ 0.11	$ 0.22
Fourth Quarter	$ 0.08	$ 0.13

PRICE RANGE OF OUR COMMON STOCK

The following table summarizes the quarterly low and high bid prices per share for our common stock on AMEX and the OTCBB, as applicable, during the periods indicated. The bid prices reflect inter-dealer prices, without retail markup, markdown, or commission and may not represent actual transactions.

On June 30, 2005, the closing bid for our common stock as reported on the OTCBB was $0.11per share. On June 30, 2005, we had approximately 14 million shares of our common stock held by beneficial shareholders and approximately 114 million shares of our common stock outstanding.

Year Ended June 30, 2004	Low Bid	High Bid
First Quarter	$ 0.31	$ 0.76
Second Quarter	$ 0.19	$ 0.39
Third Quarter	$ 0.17	$ 0.58
Fourth Quarter	$ 0.06	$ 0.27
Year Ended June 30, 2005		
First Quarter	$ 0.09	$ 0.19
Second Quarter	$ 0.10	$ 0.15
Third Quarter	$ 0.11	$ 0.22
Fourth Quarter	$ 0.08	$ 0.13

We have not paid dividends with respect to our common stock, and do not presently possess the resources to pay dividends in the future.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

FORWARD-LOOKING STATEMENTS CONCERNING OUR BUSINESS

The following discussion should be read in conjunction with the Consolidated Financial Statements, the notes thereto and the other information included in this Report. Certain statements in this "Management's Discussion and Analysis or Plan of Operation" are forward-looking statements. When used in this document, the words "expects," "anticipates," "intends," "plans," "may," "believes," "seeks," "estimates," and similar expressions generally identify forward-looking statements. The forward-looking statements contained herein are based on current expectations and entail various risks and uncertainties that could cause actual results to differ materially from those expressed in such forward-looking statements. For a more detailed discussion of these and other business risks, see "Risk Factors."

OVERVIEW

Our mission is to improve the quality of life by raising the performance standards of infrared thermal imaging technology for both the medical device and industrial markets. We design, manufacture and market thermal imaging devices and services used for clinical diagnosis, pain management and industrial non-destructive testing. We provide inspection services and design and build non-destructive test systems for industrial customers.

Our current products are the BCS 2100, Photonic Stimulator, TIP and TBIS. We have historically marketed our products with an internal sales force and through independent distributors. At present, however, due to our troubled financial condition, we are not actively marketing our products. To date, our revenues have been generated principally from the sale of our Photonic Stimulator, TIP, TBIS and services provided in connection with our TBIS.

Given our inability to market our principal product unless we secure FDA pre-market approval, our need to raise capital to fund our operations, our history of losses (over $97 million since inception), and the risk of pending or future litigation, our independent auditor's opinion dated October 2005 contains a "going concern qualification," meaning that our independent auditors have indicated that there is substantial doubt as to our ability to continue as a going concern. Our efforts to raise additional funds during the 2005 fiscal year have been largely unsuccessful. Since the FDA's rejection of our application for pre-market approval of the BCS 2100 in December 2002, we have raised $500 thousand in advances under an equity line of credit with Beach Boulevard, $1.32 million through a private issuance of restricted stock, $660 thousand from the NanDa License Agreement and $320 thousand from short-term notes. We have pursued additional financing transactions, but, as of the date of this report, we have been unsuccessful in our efforts to raise additional capital. Regardless of the FDA's ultimate decision regarding our application for pre-market approval of the BCS2100, we will require additional capital to execute our operating plan, which may include more clinical trials, research and development, marketing outside the United States and marketing and manufacturing expenses.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements requires us to estimate the effect of various matters that are inherently uncertain as of the date of the financial statements. Each of these required estimates varies in regard to the

level of judgment involved and its potential impact on our reported financial results. Estimates are deemed critical when a different estimate could have reasonably been used or where changes in the estimate are reasonably likely to occur from period to period, and would materially impact our financial condition, changes in financial condition or results of operations. Our significant accounting policies are discussed in Note 1 of the Notes to our consolidated financial statements set forth in Item 7 below; critical estimates inherent in these accounting policies are discussed in the following paragraphs. Our management has discussed the development and selection of these critical accounting policies with the Audit Committee of our Board of Directors.

REVENUE RECOGNITION--We believe revenue recognition is a significant business process that requires management to make estimates and assumptions. We recognize revenue from product sales after shipment when persuasive evidence of an agreement exists, delivery of the product has occurred, no significant obligations remain, the price or fee is fixed or determinable, and collectibility is probable. If these conditions are not met, revenue is deferred until such obligations and conditions are fulfilled.

Our standard domestic terms for our medical products to end-user customers require prepayment and our standard international terms for our medical products is cash. On occasion, we offer extended payment terms beyond our normal business practices, usually in connection with providing an initial order of demonstration equipment to a new domestic distributor. We consider fees on these extended terms agreements to not be fixed and collectibility to be less than probable. Accordingly, we defer the revenue until receipt of payment. We sell separate extended warranty contracts for our TIP and Photonic Stimulator and recognize revenue from those arrangements ratably over the contract life. We do not offer rights or return privileges in sales agreements.

Industrial sales are made pursuant to individually negotiated commercial contracts which specify payment terms that have ranged from 60 to 90 days from shipment or service completion. With industrial products, even if delivery and payment have occurred, we may retain a significant ongoing obligation under a sales arrangement for the delivery of components or customized software and customer testing, and we defer recognizing revenue until all the multiple elements of the sale are completed.

INVENTORY VALUATION--We value inventory at lower of cost or market. Inventory values are determined using standard purchase quantities and prices agreed with our vendors. If purchase costs decrease, any difference is recorded to cost of revenues and the carrying value of inventory is reduced. We have not experienced significant material cost increases for any production part though we do expect price increases due to the increased costs of petroleum products.

INVENTORY RESERVES--We reserve for excess and obsolete inventory by comparing inventory on hand to estimated consumption during the next 12 months. Consumption is estimated by annualizing trailing three or six-month trailing sales volumes, adjusting those volumes for known activities and trends, and comparing forecast consumption to quantity on hand. Any difference between inventories on hand greater and estimated consumption is recorded to cost of revenues and an excess and obsolete reserve which is included as an element of net inventory reported on our balance sheet. Amounts charged into the inventory reserves are not reversed to income until the reserved inventory is sold or otherwise disposed.

IMPAIRMENT OF LONG-LIVED ASSETS--We follow the provisions of the Financial Accounting Standards Board ("FASB") SFAS No. 121, ACCOUNTING FOR THE

IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF, which requires that if the sum of the future undiscounted cash flows expected to result from the assets is less than the carrying value of the assets, then the asset is not recoverable and the company must recognize an impairment. The amount of impairment to be recognized is the excess of the carrying value of the assets over the fair value of those assets and is recorded as a component of impairment loss on our consolidated statement of operations. In estimating impairments, management makes assumptions about future cash flows, the likelihood of those cash flows occurring and fair values of the related assets based on estimates that may differ from actual results.

STOCK-BASED COMPENSATION--We measure compensation expense for our employee stock-based compensation plans using the intrinsic value method prescribed by Accounting Principles Board ("APB") Opinion 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES and FASB Interpretation No. 44, ACCOUNTING FOR CERTAIN TRANSACTIONS INVOLVING STOCK COMPENSATION--AN INTERPRETATION OF ACCOUNTING PRINCIPLES BOARD (APB) OPINION NO. 25 ("FIN 44").

Pursuant to the prescribed guidelines, we have recorded adjustments associated with the exercise price of employee stock options, extension of the exercise period of employee stock options, issuing stock options at a strike price lower than the then prevailing price for our common stock and issuing stock to directors or stock to an employee.

During 2001, we modified the exercise price of certain stock options granted to certain of our executives and managers in connection with concluding severance agreements or to align the interests of executives, managers and shareholders. As a result, these options became subject to variable accounting. Variable accounting requires us to adjust compensation expense for the increases or decreases in the intrinsic value of the modified awards in subsequent periods until the award is exercised, is forfeited, or expires unexercised.

We follow SFAS 123, ACCOUNTING FOR STOCK-BASED COMPENSATION, for non-employee stock options and warrants granted. Values have been estimated at the date of grant and beginning of the period respectively, using a Black-Scholes security-pricing model. In determining values under the Black-Scholes pricing model, we make estimates and assumptions regarding our volatility, risk-free lending rate and the expected life of the security, which materially impact the security's value.

Our Board of Directors authorize all stock option and warrant grants, and approve any changes to option
or warrant terms.

RESULTS OF OPERATION

FISCAL YEARS ENDED JUNE 30, 2005 AND 2004

REVENUES

Total revenues for the fiscal year ended June 30, 2005 were $236 thousand, compared to $357 thousand for the fiscal year ended June 30, 2004, a decrease of $121 thousand or 34%. We attribute the decrease in revenues to reductions in sales personnel and other staff, as well as other consequences of our limited financial and operational resources. We recognize revenue from product sales to end customers upon shipment of products when persuasive evidence of an agreement exists, delivery of the product has occurred, no significant Company obligations remain, the fee is fixed or determinable, and collectibility is probable. If these conditions are not met, revenue is deferred until such obligations and conditions are fulfilled. If we retain an ongoing obligation under a sales arrangement, revenue is deferred until all our obligations are fulfilled

Our medical segment revenues were $136 thousand and $269 thousand for the fiscal years ended June 30, 2005 and 2004, respectively. The decrease of $133 thousand, or 49% resulted primarily from decreased shipments of TIP units and Photonic Stimulators.

The remaining $100 thousand and $88 thousand of revenues reported in 2005 and 2004, respectively, were attributable to our industrial segment. The $71 thousand in industrial revenues that we recognized during fiscal 2005 was primarily repair work on existing customer cameras.

As of June 30, 2005, we did not have a backlog of industrial orders for our TBIS and industrial products, nor did we have a backlog as of June 30, 2004. We generally have no backlog for pain management products, which are shipped promptly upon receipt of an order. Reported backlog represents the actual value of purchase orders issued to us for delivery of goods in the future. As of June 30, 2005, we had not recognized revenue for the sale of a TBIS to Pratt & Whitney because, even though the TBIS was delivered during the quarter ended March 31, 2003, we have not yet satisfied our post-delivery obligations related to customer acceptance testing, installation and training, and customization of software for the needs of Pratt & Whitney. We have not included the TBIS sold to Pratt & Whitney in backlog because an invoice with respect to such TBIS had been sent and was payable as of June 30, 2003. Pratt & Whitney has requested the Company remove the TBIS. We have reclassified the deferred revenue as a liability until this issue is resolved. Revenue will be recognized as a gain on sale of fixed assets when all of our sales commitments and obligations have been fulfilled.

EXPENSES

GROSS MARGINS AND COST OF REVENUES. Total gross margins for the fiscal year ended June 30, 2005 were $70 thousand, compared to $191 thousand for the fiscal year ended June 30, 2004, a decrease of approximately 64%. This decrease is principally attributable to the 34% decrease in revenues. However, gross margins decreased as a percentage of sales from 54% to 30%. This decrease in gross margin as a percentage of sales was due primarily to the increase of physical discrepancies (adjustment of inventory to physical count)). Total cost of goods sold for fiscal 2005 was $166 thousand, compared to $165 thousand in fiscal 2004, a .4% increase in dollar value.

We have not tracked segment information beyond certain revenue levels due primarily to the similarity of inventoried products used in each segment. The absence of segmented information is also due to the fact that industrial revenues for fiscal 2005 were principally repair-oriented.

Gross margins and cost of revenues as a percentage of sales for the fiscal years ended June 30, 2005 and 2004 were:

	Total Sales 2005	Percentage of Sales	Total Sales 2004	Percentage of Sales	Increase (Decrease)	Percentag of Chang
Net Revenue	235,972	100%	356,710	100%	(120,738)	-3
Cost of Goods Sold	165,100	70%	165,741	46%	(641)	

Gross Margin	70,872	30%	190,969	54%	(120,097)	-6

	2005	2004
Leasehold Improvements	--	--
Office Furniture & Fixtures	8,421	38,421
Machinery & Equipment	409,618	557,281

OPERATING, GENERAL AND ADMINISTRATIVE. Operating, general and administrative expenses for the year ended June 30, 2005 were $523 thousand, compared $1.235 million for the year ended June 30, 2004. Operating, general and administrative expenses decreased by $712 thousand, or 58%, from fiscal 2004 to fiscal 2005. If we obtain FDA pre-market approval or funding to facilitate the steps suggested by the FDA, neither of which appears imminent at this point in time, or, if customers in Canada or China begin to purchase our BCS 2100, then our expense level would increase in connection with hiring people to manufacture and market our BCS 2100.

Operating, general and administrative expenses decreased from fiscal 2004 to fiscal 2005 primarily due to: 1) $427 thousand decrease in legal and other professional services expenses; 2) $135 thousand decrease in insurance expense; 3) a $102 thousand decrease in wages and related expenses: and 4) a $44 thousand decrease in travel expenses.

We may also be required to indemnify our officers and directors in connection for fees incurred in connection with these investigations. The decrease in wages was due primarily to a material decrease in the number of employees, as well as salary reductions. The decrease in expense spending in conjunction with reduction of employees decreased travel expenses. .

LITIGATION SETTLEMENTS. Litigation settlements were $110 thousand for the year ended June 30, 2004 and $0 for the year ended June 30, 2005, a decrease of $110 thousand. Two separate legal issues, which were settled in the year ending June 30, 2004, were expensed in the same year.

RESEARCH AND DEVELOPMENT. Research and development expenses for the year ended June 30, 2005 were $182 thousand compared to $997 thousand for fiscal 2004 a decrease of $815 thousand, or 82% from fiscal 2004 to fiscal 2005. The decrease in research and development expense was primarily a result of: 1) a $551 thousand decrease in wages; 2) a $147 thousand decrease in insurance expense; and 3) a $69 thousand reduction in legal fees.

The decrease of research and development expenses during the year ended June 30, 2005 primarily relates to our efforts to decrease costs and reduce our negative cash flow. We no longer employ medical and industrial research and development personnel and have eliminated all capital projects. Research and development spending is highly dependant upon our ability to secure FDA approval, attract investors and generate revenue from sales. The FDA has asked for more clinical trials to be preformed which may require us to increase efforts in research and development. After reviewing the circumstances associated with our application for pre-market approval, we have filed with the FDA a "Citizen's Petition" alleging that our application was severely and improperly prejudiced because of bias against CTI by FDA staff reviewers who improperly undermined the Advisory Panel's review of our application and

ultimately caused the FDA to reject that application. Our Citizen's Petition requests that the FDA Commissioner review and reconsider our application for pre-market approval of the BCS 2100.

If our Citizen's Petition is unsuccessful, we may be required to conduct more clinical trials. We do not presently have the financial resources or personnel on staff to complete additional clinical trials. If additional trials are required, we will need to obtain additional capital in the form of debt or equity. Given our current financial condition, we do not believe we will be able to raise debt capital. We have previously evaluated, and will continue to evaluate, opportunities to raise equity capital through private offerings of our capital stock; however, we can not provide any assurance that we will be able to raise equity capital if necessary to fund additional clinical trials.

For the fiscal year ended June 30, 2005 and all prior periods, we expensed all costs associated with process and systems development, including software code development, computer hardware and software purchases, and expenses related to the development of our BCS 2100.

MARKETING. Marketing expenses for the year ended June 30, 2005 were $24 thousand, compared to $242 thousand for the year ended June 30, 2004. Marketing expenses decreased by $218 thousand, or 90% from fiscal 2004 to fiscal 2005.

Marketing expense decreases were primarily a result of: 1) a $147 thousand decrease in wages and related expenses resulting from a material reduction in the number of sales and marketing employees; 2) a $34 thousand reduction in insurance expenses: and 3) a $16 thousand decrease in marketing, travel and tradeshow expenses, reflecting our reduced marketing efforts.

Marketing expenses decreased due to our decision to significantly reduce our marketing activities, including tradeshows and travel expenses, and sales and marketing personnel. As a result of these significant reductions in workforce and curtailed marketing efforts since June 30, 2004 sales have dropped significantly.

DEPRECIATION AND AMORTIZATION. Depreciation and amortization expenses for the fiscal year ended June 30, 2005 were $17 thousand, compared to $142 thousand for the year ended June 30, 2004 a decrease of $125 thousand, or 88%.

IMPAIRMENT LOSSES. Impairment losses consisted of asset impairments of approximately $711 thousand for the fiscal year ended June 30, 2003. There was no impairment of assets in fiscal 2004. We evaluate our property, plant and equipment for impairment whenever indicators of impairment exist. For fiscal year 2005 we recorded an impairment of equipment for $14 thousand.

Accounting standards require that if the sum of the future cash flows expected to result from the assets, undiscounted and without interest charges, is less than a company's reported value of the assets, then the asset is not recoverable and the company must recognize an impairment. The amount of impairment to be recognized is the excess of the reported value of the assets over the fair value of those assets and is recorded as an impairment expense on the company's statement of operations. In estimating impairments, our management makes assumptions about future cash flows and fair value that are inherently uncertain, can significantly affect the results, and may differ from actual future results.

OPERATING INCOME/LOSS

We recorded an operating loss of $709 thousand for the fiscal year ended June 30, 2005, compared to an operating loss of $2.5 million for the fiscal year ended June 30, 2004 an improvement of $1.79 million or 72%.

We did not maintain medical and industrial segment information beyond the gross margin level due to the dramatic changes in the scope of our operations. Segment allocations were previously calculated on a budgetary allocation. As we dramatically reduced our expenses during fiscal 2005 and significantly changed the structure of our operations, segment allocations became misleading and therefore, we have abandoned such allocations.

NET INTEREST INCOME/EXPENSE

Interest income for the fiscal year ended June 30, 2005 was less than $1 thousand, compared to $5 thousand for the year ended June 30, 2004. The $4 thousand, or 97%, decrease was primarily a result of decreased investments available for sale and lower interest rates. Interest income declined as we used investments available for sale to fund operations.

Interest expense for the fiscal year ended June 30, 2005 was $20 thousand, compared to $10 thousand for the year ended June 30, 2004. Interest expense for fiscal year 2005 was comprised of interest accrued but not paid for three loans 1) $14,178 attributable to a $100 thousand debt to Thermal Imaging Inc assumed at the time of settlement of the departure of our former president; 2) $12,526 attributable to a $200 thousand loan received June 14, 2004; and 3) $1,364 attributable to a $20 thousand loan received May 11, 2004. The remaining interest expense for fiscal 2005 was due to finance charges from vendors for late payments.

OTHER INCOME/EXPENSE

Other income/expense for the fiscal year ended June 30, 2005 was $0, compared to $69 thousand for the year ended June 30, 2004.

NET LOSS

We incurred a loss of $709 thousand, or $(.006) per share, for the fiscal year ended June 30, 2005, compared to a loss of $2.47 million, or $(.02) per share, for the fiscal year ended June 30, 2004.

UNAUDITED QUARTERLY RESULTS OF OPERATIONS

The following table summarizes our results of operations for each of the four quarters in the fiscal years ended June 30, 2005 and 2004. This information was derived from unaudited interim consolidated financial statements that, in the opinion of our management, have been prepared on a basis consistent with the audited consolidated financial statements contained elsewhere in this Report and includes all adjustments necessary for fair statement of such information when read in conjunction with the audited consolidated financial statements and notes thereto. Period-to-period comparisons of our historical operating results are not necessarily indicative of future performance.

	Quarter ended (unaudited) (in thousands)

	6/30/05	3/31/05	12/30/04	9/30/04	6/30/04
Revenues	$ 28	$ 76	$ 56	$ 76	$ 93
Cost of goods sold	(119)	(23)	(9)	(13)	(90)
Gross margin	(92)	53	47	63	3
Operating general & administrative	283	23	95	116	58
Litigation Settlement	-		-	-	-
Research & development	71	17	36	58	69
Marketing	0	(2)	8	17	(54)
Depreciation & amortization	(2)	11	3	5	10
Impairment Loss	14	-	-	-	
Total costs and expenses	366	49	141	196	83
Interest income/(expense)	(6)	(5)	(5)	(5)	64
Misc. Income	-		-	-	
Total other income	(6)	(5)	(5)	(5)	64
Net loss	$(464)	$(1)	$(99)	$(138)	$ (16)

Period-to-period comparisons of our historical operating results are not necessarily indicative o

Revenue fluctuates quarter-to-quarter primarily due to large industrial sales and contracts.

In the quarter ended June 30, 2005 cost of goods sold increase due to inventory adjustments related to impairment evaluations and physical count.

Operating expenses steadily declined as we attempt to conserve cash. In the quarter ended June 30, 2005 expenses increased due to impairment losses.

Gross margin decreased for June 30, 2005 due to the physical adjustment to cost of goods sold when reconciling the physical count of inventory.

SOURCES OF LIQUIDITY

Given our inability to market our principal product unless we secure FDA pre-market approval, our need to raise capital to fund our operations, our history of losses ($97 million since inception), and the risk of pending or future litigation, our independent auditor's opinion dated September 2005 contains a "going concern qualification," meaning that our independent auditors have indicated that there is substantial doubt as to our ability to continue as a going concern. Our efforts to raise additional funds during the 2005 fiscal year have been largely unsuccessful. Since the FDA's rejection of our application for pre-market approval of the BCS 2100 in December 2002, we have raised $500 thousand in advances under an equity line of credit with Beach Boulevard, $1.32 million through a private issuance of restricted stock, $660 thousand from the NanDa License Agreement and $330 thousand from short-term notes. We have pursued additional financing transactions, but, as of the date of this Report, we have been unsuccessful in our efforts to raise additional capital. Regardless of the FDA's ultimate decision regarding our application for pre-market approval of the BCS2100, we will require additional capital to execute our operating plan, which may include more clinical trials, research and development, marketing outside the United States and marketing and manufacturing expenses.

Our cash requirements include general corporate expenses including salaries and benefits, lease payments for office space, technology acquisition, software license and maintenance contract payments, legal and accounting fees, clinical trial and technical support, FDA consulting, marketing, and expenses associated with the private placement of our equity securities. Capital resources needed to meet our past and planned expenditures have been financed and are likely to continue to be primarily from the sale of equity securities.

Our operations used $217 thousand of cash during the fiscal year ended June 30, 2005, compared to $1.8 million in the fiscal year ended June 30, 2004. The reduction of cash usage was due primarily to a significant decrease in our operating costs.

Investing activities provided no cash in fiscal year 2005. During the fiscal year ended June 30, 2005, we received a short term note to assist in continuing operations of $100 thousand in June of 2005. The term and details are yet to be determined. We are, however, accruing on our financial statements the obligation to repay the loans, together with interest at an imputed interest rate for accounting purposes.

As of June 30, 2005, we believed that we had sufficient liquidity to sustain current operations for three to four months. We have received $300 thousand of debt proceeds since June 30, 2005 and we continue to engage in discussions with other prospective sources of equity capital. To restore operations to former levels, we must secure additional funding. As of June 30, 2005, our current monthly cash outlay rate was approximately $30 thousand; our cash monthly outlay at our former full operation rate was approximately $1.1 million. We cannot continue to reduce our monthly cash outlay and be able to service our current customers. As of June 30, 2005, we hold four notes totaling $420 thousand. No payment schedule has been determined for repayment.

As of June 30, 2005 we had no contractual obligations, other than payment plans for existing vendors whose invoices are reflected on our balance sheet as accounts payable.

CAPITAL REQUIREMENTS/PLAN OF OPERATION

Our capital requirements may vary from our estimates and depend upon numerous factors including 1) time and costs involved in obtaining regulatory approvals for the BCS 2100, 2) results of pre-clinical and clinical testing, 3) costs of technology, 4) progress in our research and development programs, 5) costs of filing, defending and enforcing any patent claims and other intellectual property rights, 6) the economic impact of developments in competing technology and our markets, 7) competing technological and market developments, 8) the terms of any new collaborative, licensing and other arrangements that we may establish, 9) litigation costs, and 10) market acceptance of our products and the cost of obtaining acceptance.

Our current operating level consists of significantly reduced staffing, minimal services, halted production and consolidated facilities. Since December 2002, we have significantly cut back on our expenses to maintain solvency and continue efforts to obtain FDA pre-market approval of the BCS 2100. Since June 30, 2002, we have reduced our monthly cash outlays from $1.1 million to approximately $30 thousand by: a) reducing staff from 72 to 2 employees and eliminating certain benefit programs; b) eliminating regional trade shows and related marketing expenses; c) consolidating our Bales Scientific facility into our Ogden, Utah facility; d) eliminating research and development activities; and e) decreasing manufacturing and production expenditures.

Under our bylaws and contractual agreements, we are required to indemnify our current and former officers and directors who are a party to certain litigation proceedings by providing legal defense through our attorneys (or reimbursing them for their own attorneys) and covering all damages they may suffer if the plaintiffs are successful. For the year ended June 30, 2005, such indemnification obligations totaled approximately $33 thousand.

Given our inability to market our principal product unless we secure FDA pre-market approval, our need to raise capital to fund our operations, our history of losses ($97.6 million since inception), and the risk of pending or future litigation, our independent auditor's opinion dated September 2005 contains a "going concern qualification," meaning that our independent auditors have indicated that there is substantial doubt as to our ability to continue as a going concern. Our efforts to raise additional funds during the 2005 fiscal year have been largely unsuccessful. Since the FDA's rejection of our application for pre-market approval of the BCS 2100 in December 2002, we have raised $500 thousand in advances under an equity line of credit with Beach Boulevard, $1,.320 million through a private issuance of restricted stock, $660 thousand from the NanDa License Agreement and $320 thousand from short-term notes. We have pursued additional financing transactions, but, as of the date of this report, we have been unsuccessful in our efforts to raise additional capital. Regardless of the FDA's ultimate decision regarding our application for pre-market approval of the BCS2100, we will require additional capital to execute our operating plan, which may include more clinical trials, research and development, marketing outside the United States and marketing and manufacturing expenses.

There can be no guarantee that will be successful in obtaining FDA pre-marketing approval or that we will be able to raise additional capital required to continue our operations. We are pursing opportunities internationally including Canada. Our discussions with potential investors are in an early stage and we cannot guarantee that we will be able to successfully conclude any transaction.

RECENT ACCOUNTING PRONOUNCEMENTS

During the year ended June 30, 2005 there were no new accounting pronouncements that had a material effect on our operations or financial conditions.

ITEM 7. FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders of
Computerized Thermal Imaging, Inc. and Subsidiaries
Ogden, Utah

We have audited the accompanying consolidated balance sheets of Computerized Thermal Imaging, Inc. and subsidiaries as of June 30, 2005, and the related consolidated statements of operations and other comprehensive income (loss), stockholders' equity (deficit) and cash flows for the years ended June 30, 2005 and 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Computerized Thermal Imaging, Inc. and Subsidiaries as of June 30 and the consolidated results of their operations and their cash flows for the years ended June 30, and 2005 in conformity with United States Generally Accepted Accounting Principles.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has suffered recurring losses and has a working capital deficit at June 30, 2005 of $1.944 million. Together these factors raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

HJ & Associates, LLC
Salt Lake City, Utah

October 12, 2005

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COMPUTERIZED THERMAL IMAGING, INC.
CONSOLIDATED BALANCE SHEETS

ASSETS	JUNE 30, 2005	JUNE 30, 2004
CURRENT ASSETS:		
Cash and cash equivalents	$ 51,688	$ 168,9
Accounts Receivable - trade, less allowance for doubtful accounts of $0 on June 30, 2005	40	53,3
Accounts Receivable- other (net)	--	1,3
Inventories	87,276	260,3
Prepaids expenses	33,809	91,4
Total current assets	172,813	575,4
NET PROPERTY PLANT & EQUIPMENT (Net)	7,525	169,3
INTANGIBLE ASSETS:		
Intellectual property rights, less accumulated amortization of $20,107 and $17,437 respectfully	12,740	15,4
TOTAL ASSETS	$ 193,078	$ 760,2
LIABILITIES & STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts Payable	$ 558,045	$ 512,5
Accrued Liabilities	555,262	172,0
Short-term Note Payable with interest	333,891	220,6
Deferred Revenue	669,991	1,083,1
Total Current Liabilities	2,117,189	1,988,3
LONG-TERM NOTE PAYABLE	114,181	109,1
TOTAL LIABILITIES	2,231,370	2,097,5
STOCKHOLDERS' EQUITY		
Convertible preferred stock, no par value, 3,000,000 shares authorized; none issued	--	
Common stock, $.001 par value, 200,000,000 shares authorized, 114,561,698 and 114,561,698 issued and outstanding on June 30, 2005 and June 30, 2004, respectively	114,562	114,5
Additional paid-in capital	95,462,474	95,454,2
Deficit accumulated	(97,615,328)	(96,906,1
TOTAL STOCKHOLDERS' EQUITY	(2,038,292)	(1,337,2
TOTAL LIABILITIES & STOCKHOLDERS' EQUITY	$ 193,078	$ 760,2

The accompanying notes are an integral part of these consolidated financial statement

COMPUTERIZED THERMAL IMAGING, INC.
CONSOLIDATED STATEMENT OF OPERATIONS
THE TWELVE MONTH PERIOD ENDED JUNE 30, 2005 AND 2004

Revenue	YEARS ENDED JUNE 30, 2005	2004
PS	$ 82,652	$ 124,499
TIP	94,570	26,859
Turbine	48,173	13,748
Warranty Revenue	--	19,929
Other Services	6,475	87,520
Discounts & Other	(4,995)	(2,875)
Freight	9,097	4,364
Net Revenue	235,972	356,710
COST OF SALES		
Materials	28,762	149,175
Variance	--	611
Physical Discrepancies	129,439	--
Freight	6,899	306
Total Cost of Sales	165,100	165,741
GROSS MARGIN	70,872	190,969
OPERATING EXPENSES		
General & Administration	523,079	1,235,482
Sales & Marketing	23,855	242,373
Research & Development	181,878	996,567
Depreciation	14,442	139,346
Amortization	2,670	2,656
Total Depreciation & Amortization	17,112	142,002
Litigation settlement	--	110,000
Impairments	13,990	--
Total Operating Expenses	759,914	2,726,424
OPERATING INCOME (LOSS)	(689,042)	(2,535,455)
OTHER INCOME / EXPENSE		
Interest Income	118	4,512
Interest Expense	(20,320)	(10,478)
Other	51	69,074
Total Other Income / Expense	(20,151)	63,108

Profit / (Loss) Before Taxes	(709,193)	(2,472,347)
Tax Expense	--	--
State	--	--
NET LOSS	(709,193)	(2,472,347)
WEIGHTED AVERAGE SHARES OUTSTANDING	114,566,981	114,566,981
BASIC AND DILUTED LOSS PER COMMON SHARE	$ (0.01)	$ (0.02)

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL PAID-IN CAPITAL
Balance at June 30, 2003	109,329,098	$ 109,329	$ 94,041,104
Converion of remaining premium pntly 7.7.04	196,451	196	88,206
Kuwait Restriced Stock Sale 7.10.04	3,344,482	3,344	996,656
Garvey Schubert Issue for debt 1.22.04	25,000	25	9,975
Xue Zheng Charlie DAI (CMS) 1.30.04	1,000,000	1,000	219,000
Nabeel Al Mulla Stock Sale 5.14.2004	666,667	667	99,333
Net loss			
Balance at June 30, 2004	114,561,698	114,562	95,454,274
In trin sic Value of Options			8,200
Net Loss			
Balance at June 30, 2005	114,561,698	$ 114,562	$ 95,462,474

The accompanying notes are an integral part of these consolidated financ

COMPUTERIZED THERMAL IMAGING, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	YEAR ENDED	YEAR ENDED

	30-JUN 2005	30-JUN 2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (709,193)	(2,472,34
Depreciation and amortization	17,113	142,00
Common stock, warrants, and options issued as compensation for services	8,200	-
Impairment loss and loss on disposition of assets	13,990	4,01
Common stock issued to pay debenture	--	(68,87
Bad debt expense	--	1,06
Changes in operating assets and liabilities:		
Accounts receivable - trade	53,289	366,00
Accounts receivable - other	1,391	(1,39
Inventories	173,055	45,53
Prepaid expenses	57,665	218,77
Accounts payable	45,503	(122,53
Accrued liabilities	144,930	(224,12
Deferred revenues	(23,208)	296,45
Net cash used in operating activities	(217,266)	(1,815,43
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net cash provided by (used in) investing activities	--	-
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock and warrants, net of offering costs	--	1,310,00
Proceeds from loan	100,000	
Proceeds from related party borrowing	--	220,00
Net cash provided by financing activities	100,000	1,530,00
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(117,265)	(285,43
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	168,955	454,38
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 51,690	$ 168,95
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid for:		
Interest	--	89
SUPPLEMENTAL SCHEDULE OF NON-CASH FINANCING AND INVESTING ACTIVITIES		
Common stock issued to reduce debenture, interest and penalty	--	157,27

The accompanying notes are an integral part of these consolidated financial state

COMPUTERIZED THERMAL IMAGING, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

1. SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION--Computerized Thermal Imaging, Inc. (the "Company" or "CTI"), a Nevada corporation, develops and markets thermal imaging systems for applications in healthcare and industrial markets. The Company's system is based upon computer interpretation of thermal photography using proprietary software developed by the Company. The Company also applies elements of its core thermal imaging technology to industrial non-destructive testing applications.

Since inception, the Company has devoted substantially all of its efforts to: 1) the development and improvement of systems for commercial application of thermal imaging technology in the medical industry; 2) the development of markets for its technology; and 3) the search for sources of capital to fund its efforts. On April 18, 2000, the Company acquired 100% of the outstanding common stock of Bales Scientific, Inc. ("Bales"), a company that designs, manufactures, and sells high-resolution, dynamic, digital infrared-imaging workstations and related products for both medical and industrial applications.

BASIS OF PRESENTATION--The Company's consolidated financial statements have been presented on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company has been primarily involved in research and development activities. This has resulted in significant operating losses and an accumulated deficit at June 30, 2005, of $97,615,328. As explained in the paragraphs below, the Company has numerous conditions that may adversely affect its ability to continue as a going concern. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary if the Company is unable to continue as a going concern.

The following conditions may adversely affect the Company's ability to continue as a going concern:

The Company has not received regulatory approval for the BCS 2100. On December 10, 2002, the Radiological Devices Advisory Panel (the "Panel") of the U.S. Food and Drug Administration (the "FDA") voted four to three against recommending the BCS 2100 for FDA pre-marketing approval. On January 24, 2003, the FDA advised the Company that it concurred with the Panel's recommendation to not approve the Company's pre-market approval application. Regulatory approval is contingent upon, among other things, successful negotiation with the FDA to reverse its decision or conduct additional data analysis, clinical trials and other steps followed by an FDA audit of the Company's manufacturing and clinical trial practices. The Company has filed a "Citizen's Petition" with the FDA to request internal FDA documents help the Company to understand why FDA procedures were not followed and the panel rejected the Company's request. There is no assurance that the Company will receive the documents from the FDA or receive pre-marketing approval for the BCS 2100.

If the BCS 2100 receives FDA pre-marketing approval, the Company's cash flow and profitability will be dependant upon, among other things, successful marketing and acceptance of the system by the medical community, obtaining reimbursements from private and public insurance providers for procedures performed with the BCS 2100, and those customers will find these reimbursements sufficient to

warrant its use. There is no assurance that the Company will be able to successfully market the system or secure reimbursements, nor can the Company assure that customers will believe reimbursements offered are sufficient.

The current operating plan for fiscal 2006 does not encompass: 1) additional costs required to bring the BCS 2100 to market if FDA approval is obtained; or 2) start new clinical trials as described in the FDA non-approval letter, which

describes additional steps the Company can take to obtain approval including more clinical trials and further research. In order to fund operations, the Company will be required to raise additional capital through debt or equity financing. Uncertainties regarding FDA approval for the BCS 2100 and shareholder litigation may make fundraising more difficult, if not impossible.

Management of the Company has taken certain actions in response to these risk factors. Management believes that regulatory approval is contingent upon, among other things, successful negotiations and resolution to FDA concerns and a device panel review and an audit of the Company's manufacturing and clinical trial practices. The Company cannot guarantee whether or when the FDA may approve the BCS 2100, and proposes to retain third-party consultants to assist with preparation for the Radiological Devices Panel meeting, manufacturing practices and clinical trial audits. The FDA could affirm its prior decision, approve the Company's application or approve the Company's application with conditions. Unless and until the Company receives approval or conditional approval, which could include having to conduct further clinical trials, clinical studies or analysis of clinical trial data, the Company proposes to conduct clinical studies of and analysis of existing clinical trial data to develop product improvements, obtain patient and clinician feedback and collect clinical data for product training purposes. The Company cannot sell, market or distribute the BCS 2100 in the United States for commercial use until it receives FDA approval. The BCS 2100 is currently approved for use in Canada. .

Further, management believes that success with regulatory activities, if achieved, and the development of the Canadian market, if accomplished, would facilitate funding and insurance reimbursement efforts.

The Company hopes to secure additional cash from operations through continuing efforts to market its pain management products in the United States, Canada and other international markets, to the extent it currently has, or the future obtains, necessary regulatory approvals.

PRINCIPLES OF CONSOLIDATION--The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Computerized Thermal Imaging Company ("CTICO"), formerly known as Thermal Medical Imaging, Inc, which was dissolved during June 2001, and Bales Scientific, Inc. All intercompany transactions and accounts have been eliminated.

USE OF ESTIMATES IN PREPARING FINANCIAL STATEMENTS--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 reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS--Cash and cash equivalents include cash in checking

accounts and short-term highly liquid investments with an original maturity of three months or less.

CONCENTRATION OF CREDIT RISK--Financial instruments that potentially subject the Company to credit risk consist primarily of cash in bank. The Company maintains its cash in bank deposit accounts insured by the Federal Deposit Insurance Corporation (FDIC) up to $100,000. The Company's accounts at times may exceed federally insured limits.

INVESTMENTS AVAILABLE FOR SALE--The Company invests cash reserves in U.S. government securities, corporate bonds and certificates of deposit. All investments are classified as available for sale and are reported at fair market value with net unrealized gains or losses (net of taxes) reported as a separate component of stockholders' equity. The Company has no investments available for sale mature during the year ending June 30, 2005. For computing the realized gain or loss on sales of investments available for sale, the cost of a security sold or the amount reclassified out of accumulated other comprehensive income into earnings was determined by specific identification.

INVENTORIES--Inventories consist of finished goods, work-in-process, and raw materials. Inventories are stated at the lower of cost or market, with cost determined using the first-in first-out method.

PROPERTY AND EQUIPMENT--Property and equipment are stated at cost and depreciated using the straight-line method over their estimated useful lives:

Leasehold improvements	3 years
Office furniture and fixtures	5-7 years
Machinery and equipment (including demonstration equipment)	2-7 years

INTANGIBLE ASSETS--Intangible assets are stated at cost and amortized using the straight-line method over their estimated useful lives:

Intellectual property rights	10 years

REVENUE RECOGNITION-- The Company generates revenues from sales of its products and from services provided to its customers. The Company sells its products to independent distributors and to end customers. With the exception of sales transactions in which a customer may return defective product, the Company does not provide its customers with other rights to return products.

The Company recognizes revenue from its product sales to end customers upon shipment of products when persuasive evidence of an agreement exists, delivery of the product has occurred, no significant Company obligations remain, the fee is fixed or determinable, and collectibility is probable. If these conditions are not met, revenue is deferred until such obligations and conditions are fulfilled. If the Company retains an ongoing obligation under a sales arrangement, revenue is deferred until all of the Company's obligations are fulfilled.

Beginning July 1, 2001, revenue on shipments to distributors has been deferred until cash payment from the distributor has been received by the Company, which is generally when the product is sold by the distributor to the end customer. Prior to that date, revenue on shipments to distributors, which was not significant, was recognized upon shipment to the distributor if all of the criteria for revenue recognition have been satisfied. The Company believes that

deferral of revenue on shipments to distributors until cash payment is received is a more meaningful measurement of results of operations.

Certain of the Company's products contain software that is not considered incidental to the product. Sales of those products are subject to the provisions of AICPA Statement of Position No. 97-2, SOFTWARE REVENUE RECOGNITION, as amended, which requires the deferral of revenue from certain multiple-element arrangements. The Company defers revenue from multiple-element arrangements until all elements have been delivered.

Deferred revenues at June 30, 2005 was approximately $669 thousand and consisted of $660 thousand of deferred revenues from the NanDa licensing and manufacturing agreement, and $9 thousand of deferred warranty. Deferred revenues on June 30, 2004 were approximately $1.83million and consisted of $3 thousand of deferred medical revenues, $13 thousand of deferred warranty revenues, $496 thousand of deferred industrial revenues and deposits and $660 thousand from the NanDa contract.

Service revenue is derived from the non-destructive testing of turbine blades, repair of non-warranty medical products, and other items. Service revenue is recognized upon completion of the services. The Company offers extended warranties on certain of its products. Warranty revenue, which is not significant, is recognized ratably over the period of the agreement as services are provided.

INCOME TAXES--Deferred taxes are provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carry-forwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases.

Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

RESEARCH AND DEVELOPMENT EXPENSES--The Company expenses as incurred the direct, indirect, and purchased research and development costs associated with its products. Research and development expenses for the years ended June 30, 2005 and 2004 were approximately $181 thousand and $996 thousand respectively.

IMPAIRMENT OF LONG-LIVED ASSETS--The Company evaluates its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets or intangibles may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. The Company impaired one TBIS machine located at Pratt & Whitney in fiscal 2005 and no impairments in 2004.

STOCK-BASED COMPENSATION--The Company has elected to follow the accounting provisions of Accounting Principles Board (APB) Opinion No. 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES FOR STOCK-BASED COMPENSATION, for stock options

granted to employees and directors and to furnish the pro forma disclosure required under Statement of Financial Accounting Standards ("SFAS") No. 123, ACCOUNTING FOR STOCK-BASED COMPENSATION, as amended. Transactions in which the Company receives goods or services in exchange for equity instruments of the Company are accounted for based on the fair value of the equity instrument issued.

ACCRUED LIABILITIES AND NOTES PAYABLE-- During the year ended June 30, 2005, the Company received $100 thousand in the form of a short-term loan to assist in continuing operations. The Company borrowed $20 thousand from Harry Aderholt, a director of the Company, on May 11, 2004 and $200 thousand from Mr. Nabeel Al Mulla, a shareholder of the Company, on June 14, 2004. The Company also carries a long-term note due in 2010 acquired from the settlement with the former Company president for $100 thousand. Interest has been accrued for each of these outstanding notes although no formal documents exist. The details of these notes are yet to be determined. The Company is now accruing a 6% interest rate for accounting purposes. Due to the reduction in legal costs the accrued legal and professional services has decreased and general expense accruals. Accrued liabilities consisted of the following at June 30, 2005 and 2004:

	2005	2004
Accrued Bonuses	$ -	$ -
Accrued Vacation	17,992	26,088
Other Accrued Employee Costs	180,850	3,347
Accrued Legal and Professional Services	63,060	93,110
Other Accrued Liabilities	293,360	49,491
Total Accrued Liabilities	555,262	172,036
Imputed Interest Payable	13,891	690
Short-term Notes Payable	320,000	220,000
Total Short-term Notes Payable	333,891	220,690
Imputed Interest Payable	14,181	9,178
Long-term Notes Payable	100,000	100,000
Total Long-term Notes Payable	$ 114,181	$ 109,178

NET LOSS PER SHARE--Net loss per share is based on the net loss and the weighted average number of common shares outstanding during each period. Common equivalent shares from common stock options and warrants are excluded from the computation of diluted earnings per share, as their effect would be antidilutive to the loss per share for all periods presented. Options to purchase 3.7 million and 3.6 million shares of common stock and warrants to purchase 74 million and 65 million shares were outstanding at June 30, 2005 and 2004, respectively, but were not included in the computation of diluted earnings per share because the

effect would be antidilutive.

RECENTLY ISSUED FINANCIAL ACCOUNTING STANDARDS-- During the years ending June 30, 2004 and 2005, the Company did not adopt any new accounting pronouncements.

RECLASSIFICATION--Certain prior period amounts have been reclassified to conform to the current year presentation.

3. INVENTORIES

Inventories consisted of the following at June 30, 2005 and 2004:

	JUNE 30, 2005	JUNE 30, 2004
Raw materials	$ 536,053	$ 616,508
Inventory reserve	(639,664)	(629,967)
Work-in process	-	18,629
Finished goods	190,887	255,161
Total	$ 87,276	$ 260,331

Finished goods inventories include approximately $174 thousand in TIP cameras and $16 thousand in assemblies and Photonic Stimulators at June 30, 2005. Due to cutbacks, no work was in progress at fiscal year end 2005. Raw materials inventory was approximately $536 thousand and $616 thousand for the years ending June 30, 2005 and 2004 respectively. The inventory reserve represents the impairment and obsolescence adjustments to inventory.

Inventory and commitments are based upon future demand forecasts. During fiscal 2004, the Company impaired the inventory no further. For fiscal year 2005, inventory levels were impaired 10%. The Company reserves for excess and obsolete inventory by comparing inventory on hand to estimated consumption during the next twelve months. Consumption is estimated by annualizing trailing three or six month sales volumes, adjusting those volumes for known activities and trends and then comparing forecast consumption to quantity on hand. Any difference between inventory on hand and estimated consumption is recorded to cost of revenues and an excess and obsolete reserve which is included as an element of net inventory reported on the Company's balance sheet. Amounts charged into the inventory reserves are not reversed to income until the reserved inventory is sold or otherwise disposed.

4. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at June 30, 2005 and 2004:

	2005	2004
Leasehold Improvements	-	-
Office Furniture & Fixtures	38,421	38,421
Machinery & Equipment	409,618	557,281
	448,039	595,702
Less Accumulated Depreciation	(440,514)	(426,344)

Property & Equipment, Net	7,525	169,358

Depreciation expense for the years ended June 30, 2005 and 2004 was approximately $14 thousand and $139 thousand, respectively.

As of June 30, 2005, machinery and equipment included approximately $240 thousand of demonstration equipment. Demonstration equipment is used in clinical studies, tradeshows, research and development, and customer demonstrations is recorded at cost and amortized over two years.

For the year ended June 30, 2003, the FDA's decision to not approve the BCS pre-market application raised substantial uncertainty in the Company's ability to eventually market and sell the BCS. This factor, coupled with the other conditions listed in Note 1, has raised substantial doubt about the Company's ability to continue as a going concern. Accordingly, the Company evaluated the carrying value of all operating assets and, based on the Company's estimated undiscounted net cash flows, determined that its assets were impaired. The Company recorded an impairment charge of approximately $694,000 relating to its medical and industrial operating assets. These assets include computers, equipment, furniture, leasehold improvements, software and other operating assets for the year ended June 30, 2003. There was no additional impairment in the year ended June 30, 2004. For fiscal year 2005, inventory levels were impaired 10 %.

5. INTANGIBLE ASSETS

Intangible assets consisted of the following at June 30, 2005 and 2004:

	2005	2004
Intellectual Property Rights	$ 32,847	$ 32,847
Less Accumulated Amortization	(20,107)	(17,437)
Net Intangible Assets	$ 12,740	$ 15,410

For the year ended June 30, 2003, the FDA's decision to not approve the BCS pre-market application raised substantial uncertainty in the Company's ability to eventually market and sell the BCS. This factor, coupled with other conditions listed in Note 1, has raised substantial doubt about the Company's ability to continue as a going concern. Accordingly, the Company evaluated the carrying value of its intangible asset based on estimated undiscounted net cash flows and determined that its intangible asset was impaired and recorded an impairment write-down of approximately $17,000 as of June 30, 2004. No additional impairment was recognized for the fiscal year ended June 30, 2005.

6. INCOME TAXES

Deferred taxes are provided on the liability method, whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carry-forwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the

reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Net deferred tax assets consist of the following components as of June 30,2005 and 2004:

	2005	2004
Deferred Tax Assets		
NOL Carryover	$ 29,784,812	$ 29,412,300
Research Credit	2,193,864	2,193,864
Accrued Compensation	70,532	243,273
Deferred Revenue	298,204	267,327
Other	--	675,487
Depreciation	--	54,765
Deferred Tax Liabilities	--	--
Valuation Allowance	$(32,347,412)	$ 32,847,016)
Net Deferred Tax Asset	$ 0	$ 0

The income tax provision differs from the amount of income tax determined by applying the U.S. federal and state income tax rates of 39% to pretax income from continuing operations for the years ended June 30, 2005 and 2004 due to the following.

	2005	2004
Book Income	$ (276,585)	$ (964,254)
Other	-	4,443
Accrued Compensation	-	23,239
Deferred Revenue	-	222,862
NOL Expiration	-	222,955
True up Prior Year	-	(18,104)
Non-deductible Meals & Entertainment	215	
Penalties	577	
Officer Life Insurance Premiums	2,287	
Valuation Allowance	$ 273,506	$ 508,859
	$ 0	$ 0

At June 30, 2004, the Company had net operating loss carry-forwards of approximately $75,000,000 that may be offset against future taxable income from the year 2005 through 2024. No tax benefit has been reported in the June 30,2005 financial statements since the potential tax benefit is offset by a valuation allowance of the same amount.

Due to the change in ownership provisions of the Tax Reform Act of 1986, net operating loss carry forwards for Federal income tax reporting purposes are subject to annual limitations. Should a change in ownership occur, net operating loss carry-forwards may be limited as to use in future years.

7. COMMITMENTS AND CONTINGENCIES

Two separate lawsuits were settled during the year ended June 30, 2005.

1) On April 11, 2003, St. Paul Properties, Inc. (the "Landlord") filed suit against the Company in the Circuit Court for Clackamas County. The Landlord alleged that the Company breached its prior corporate office lease by failing to pay the rent specified under the lease. The Landlord sought damages of approximately $667,000, plus interest and attorneys and other fees. The Company filed an answer and affirmative defenses alleging that St. Paul Properties failed to use reasonable efforts to mitigate its damages. In April of 2004, the Company settled with St. Paul for the sum of $110,000 and which included a $50,000 payment with 5 monthly payments of $12,000. The final payment of $12,000 was paid on August 15, 2004.

2) An appeal of COMPUTERIZED THERMAL IMAGING, INC., SECURITIES LITIGATION (see prior SEC filings) was heard on July 16, 2004 in the United States Court of Appeals for the Ninth Circuit. The Ninth Circuit decision upheld the determination of the District Court to dismiss the plaintiff's complaint because it failed to adequately plead a case.

OPERATING LEASES--The Company leases certain office and warehouse space. Total expense recorded under operating lease agreements in the accompanying consolidated statements of operations was approximately $71 thousand and $88 thousand for the years ended June 30, 2005 and 2004, respectively.

On June 30, 2005, there an amendment to the agreement with SilverCreek Engineering effective December 2004 to June of 2006. We have two leases: 1) Ogden, Utah location which houses all offices and manufacturing and 2) a storage unit also in Ogden. Both leases are on a month-to-month basis with 30 day notice for termination. Monthly lease payments are $5,783 for the Ogden office and $80 for the storage unit.

OTHER CONTINGENCIES--The Company has funded its operations in part by means of various offerings which the Company's management believes were exempt from the registration requirements of the Securities Act and applicable state securities laws. In the event that any of the exemptions upon which the Company relied were not, in fact, available, the Company could face claims from federal and state regulators and from purchasers of their securities. Management and legal counsel, although not aware of any alleged specific violations, cannot predict the likelihood of claims or the range of potential liability that could arise from this issue.

Prior to February 4, 1998, most of the Company's stockholders held preemptive rights to acquire shares of the Company's common stock under certain circumstances. In certain instances, the Company failed to properly offer stockholders these preemptive rights. No shareholder has asserted any preemptive rights to date. Should any stockholder do so, the Company plans to issue shares of common stock at the price to which the stockholder was originally entitled.

8. STOCKHOLDERS' EQUITY

PREFERRED STOCK--The Company has authorized 3,000,000 shares of $5.00 par value

preferred stock that is convertible into shares of common stock. The Board of Directors has the authority, without further stockholder action, to issue up to 3,000,000 shares of preferred stock in one or more series and to fix the rights, preferences, privileges, and restrictions thereof.

The Company had no preferred stock outstanding as of June 30, 2005 and 2004.

9. STOCK WARRANTS AND OPTIONS

WARRANTS--A summary of warrant activity for the period from July 1, 2004, through June 30, 2005 is as follows:

	# SHARES	EXERCISE PRICE
Balance at June 30, 2003	6,459,096	$1.56 - $5.0
Exercised	-	
Balance at June 30, 2004	6,459,096	$1.56 - $5.0
Exercised	-	
Forfeited	(5,718,070)	$5.0
Balance at June 30, 2005	741,026	$0.10 - $2.27

During the year ended June 30, 2003, the Company reduced the exercise price of the warrants that were issued to the Investor from $2.028 to $0.087733 per share. These warrants were exercised to pay $21,000 of the debenture principal and $2,000 of accrued interest. The fair value of the warrant modification was estimated at the date of modification using the Black-Scholes option pricing model.

OPTIONS--Periodically, the Company has issued incentive stock options to employees and officers and non-qualified options to directors and outside consultants to promote the success of the Company and enhance its ability to attract and retain the services of qualified persons.

The Company has 3,592,023 options outstanding and issued under the 1997 Stock Option and Restricted Stock Plans (the "Plan") since its adoption, and could issue an additional aggregate of 6,357,977 options and shares. The Plan permits restricted stock grants to employees, officers, directors and consultants at prices that may be less than 100% of the fair market value of the Company's common stock on the date of issuance. The Company also has outstanding 75,000 non-statutory stock options issued outside the Plan. Options issued under the Plan will have variable terms based on the services provided and will generally vest on the date of grant.

EMPLOYEE STOCK OPTIONS--The Company has granted the following fixed price stock options during the period July 1, 2004, THROUGH June 30, 2005:

	2005	2004
	Weighted Average	

	Shares	Exercise Price	Shares
Outstanding at beginning of year	3,592,023	1.27	4,367,719
Granted	2,560,000	0.10	510,000
Exercised	--	--	--
Forfeited	(2,468,091)	1.06	1,360,695
Outstanding at end of year	3,683,932	1.13	3,592,023
Options exercisable at year end	3,643,932		3,367,023
Weighted average fair value of options granted during the year	.0.13		0.29

	OPTIONS OUTSTANDING			OPTIO
RANGE OF EXERCISE PRICE	NUMBER OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE	NUMBE EXERCIS
$.10 - .64	750,000	4.47	$.15	750,0
$1.25 - 1.25	2,000,000	4.5	1.25	2,000,0
$1.50 - $1.95	840,000	5.32	1.53	840,0
$2.27 - $2.44	13,932	5..68	2.27	13,9
$3.50 - 3.50	80,000	5.98	3.50	80,0
$.22 - $3.50	3, 683,932	2.28	$1.13	3, 683,9

Modifications to the terms of previously fixed stock options or awards granted to employees are accounted for in accordance with APB Opinion No. 25 and Interpretation No. 44, ACCOUNTING FOR CERTAIN TRANSACTIONS INVOLVING STOCK COMPENSATION--AN INTERPRETATION OF ACCOUNTING PRINCIPLES BOARD (APB) OPINION NO. 25 ("FIN 44"). During the year ended June 30, 2004 the Company did not re-price any options. As a result of the Company's significant reduction in personnel during the year ended June 30, 2004, nearly all those employees holding options that had been re-priced in prior years are no longer employed by the Company and their rights to exercise their options have lapsed. During 2005 $8,200 intrinsic expense was claimed for revaluation of options granted to employees.

If compensation cost for options or awards granted to employees had been determined based on SFAS No. 123, the Company's net loss and basic and diluted loss per common share would have changed to the pro forma amounts indicated below:

	2005	2004
Net loss:		
As reported	$ (709,193)	$ (2,472,347)
Pro forma	(769,460)	(2,688,459)
Basic and diluted loss per common share:		
As reported	$ (0.01)	$ (0.02)
Pro forma	(0.01)	(0.02)

The fair value of the options and awards was estimated at the date of grant using the Black-Scholes option pricing model with the following assumptions for 2005 and 2004:

1) risk-free interest rate between 4.18 percent
2) no dividend yield;
3) no discount for lack of marketability;
4) expected life of from 1 to 10 years; and
5) a volatility factor of the expected market price of the Company's common stock from 259.14% to 263.29% for the years ended June 30, 1997 through 2005

NON-EMPLOYEE STOCK OPTIONS--Changes in stock options issued to non-employees are as follows for the year ended June 30, 2005.

	2005	
	SHARES	WEIGHTED AVERAGE EXERCISE PRICE
Outstanding at beginning of year.....	75,000	$1.88
Granted.....	75,000	$0.10
Exercised	--	--
Forfeited.....		
Outstanding at end of year.....	150,000	$0.99
Options exercisable at year end.....	150,000	
Weighted average fair value of options granted during the year.....	--	

10. RELATED PARTY TRANSACTIONS

The Company has been dependent upon certain individuals, officers, stockholders and other related parties to provide capital, management services, assistance in finding new sources for debt and equity financing, and guidance in the development of the Company's business. The related parties have generally provided services and incurred expenses on behalf of the Company in exchange for shares of the Company's common stock.

11. SEGMENTS

Beginning July 1, 2001, the Company changed the structure of its internal organization such that management at that time started to evaluate the Company based on two distinct operating segments: medical and industrial products and services. Due to the dramatic changes and cost cuts beginning in January 2003 and continuing through fiscal 2005, the allocation models used to separate costs into these segments became misleading. Each time a new model was developed changes in the cost structure would render the model inaccurate. The Company continues to accurately separate revenue but believes any attempt to assign

costs to the segments would be inconsistent from year to year. The revenue segment information follows:

	2005			2004	
	Medical	Industrial	Total	Medical	Industrial
Product Revenue	$ 72	$ 29	$ 101	$ 269	$ 5
Service Revenue	$ 64	$ 71	$ 135	$ -	$ 83
Total Revenue	$ 136	$ 100	$ 236	$ 269	$ 88

MEDICAL	Percentage			Dollars		
Fiscal Year	USA	Canada	China	USA	Canada	China
2005	74%	26%	0%	$ 100	$ 36	$ -
2004	35%	14%	1%	$ 187	$ 78	$ 4

INDUSTRIAL	Percentage		Dollars		
Fiscal Year	USA	UK	USA	UK	To
2005	0%	100%	$ -	$ 100	$ 1
2004	100%	0%	$ 88	$ -	$ 8

	2005 Sales	Percentage of Sales
Alstom / Siemens	$ 79,273	34%
Boothroyd	$ 34,200	14%

Deferred revenues as of June 30, 2005 and 2004 contained the following balances from significant customers

	YEARS ENDED JUNE 30,	
	2005	2004
Pratt & Whitney	0	$ 106,000
NanDa	660,000	925,000
	$ 660,000	$ 1,031,000

13. SUBSEQUENT EVENTS

We have received $300 thousand of debt proceeds since June 30, 2005 and we continue to engage in discussions with other prospective sources of equity

capital. To restore operations to former levels, we must secure additional funding.

14. FOURTH QUARTER LOSS RECOGNITION

Pursuant to APB 28, "Interim Financial Reporting", the following is a reconciliation of the net loss as reported in the Company's March 31, 2005 consolidated financial statements to the net loss as recorded at June 30, 2005.

Net loss reported March 31, 2005	$(288,146)
4th quarter accrual of payroll	(178,456)
4th quarter accrual of additional legal fees	(53,473)
Other 4th quarter adjustments and general loss from operations in the 4th quarter	(189,118)
Net loss reported June 30, 2005	$(709,193)

ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

ITEM 8A. CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including our principal executive officer and acting financial officer, we conducted an evaluation of our disclosure controls and procedures; as such term is defined under Rule 13a-15(e) promulgated under the Exchange Act, as of June 30, 2005. Based on this evaluation, our principal executive officer and acting financial officer concluded that our disclosure controls and procedures are effective in alerting them on a timely basis to material information relating to our company required to be included in our reports filed or submitted under the Exchange Act. There have been no significant changes (including corrective actions with regard to significant deficiencies or material weaknesses) in our internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation referenced above.

PART III

ITEM 9. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

DIRECTORS	AGE	POSITION	DIRECTOR
Richard V. Secord	73	Chairman of the Board, Chief Executive Officer	1996
Brent M. Pratley, M.D.	69	Director	1995
Milton R. Geilmann	72	Director	1998
Harry C. Aderholt	84	Director	1998

RICHARD V. SECORD (Major General, United States Air Force, retired) has served as our Chairman and Chief Executive Officer since September 22, 2000. General

Secord served as our Vice Chairman from July 1997 through September 2000, as our Secretary from July 1997 to June 2000, as our President from February 1996 to April 1997 and as our Chief Operating Officer from June 1995 to December 1999. General Secord served in numerous positions while performing military service from July 1951 until June 1984. General Secord received a Bachelor of Science degree from the United States Military Academy. General Secord is also a graduate of the United States Air Force Command and Staff College and the United States Naval War College. General Secord holds a Masters degree in International Affairs from George Washington University.

BRENT M. PRATLEY, M.D., has been a director since June 1995 and is a member of our Audit Committee. Dr. Pratley served as our Secretary from June 1994 to September 1997. Dr. Pratley is currently licensed to practice medicine in Utah and California. Since 1978, Dr. Pratley has been in private practice in General Orthopedics and Sports Medicine at Utah Valley Regional Medical Center located in Provo, Utah, as well as in Los Angeles, California. Dr. Pratley holds a Doctor of Medicine degree in Orthopedic Surgery from the College of Medicine at University of California, Irvine and a Bachelors of Science degree from Brigham Young University.

MILTON R. GEILMANN has been a director since January 1998 and serves as a member of our Audit Committee. From 1965 until his retirement in 1992, Mr. Geilmann worked at E. R. Squibb & Sons where he held many positions, including Nuclear Consultant for Diagnostic Medicine. Mr. Geilmann holds an Associates degree in dental science from State University of New York.

HARRY C. ADERHOLT (Brigadier General, United States Air Force, retired) has been a director since January 1998 and serves as Chairman of our Audit Committee. >From 1942 until his retirement in 1976, General Aderholt served in the U.S. Air Force. Since his retirement from military service, General Aderholt has engaged in various private business ventures, including serving as Vice President of Air Siam in Bangkok, Thailand. General Aderholt owns and operates Far East Designs, a furniture importer and retailer in Florida, and is President of the McCroskie Threshold Foundation, a humanitarian organization that donates medical supplies, food and clothing to needy people in the U.S. and around the world.

ITEM 10. EXECUTIVE COMPENSATION

SUMMARY COMPENSATION TABLE

						Long
		Annual Compensation				Awards
Name and principal Position	Fiscal Year	Salary	Bonus	Other Annual compensation (2)	Restricted Stock Award	Se Underl
Richard V. Secord	2005	31,544	-	10,200	-	
Chairman, Chief Executive	2004	90,000	-	32,400	-	
Officer (1)	2003	201,000	-	35,309	-	
	2002	210,000	-	32,400	-	
	2001	210,000	-	13,400	-	

(1) Under his employment agreement with the Company, which expired in September 2003 but is being extended on a month-to-month basis, Richard V. Secord, our chairman and Chief Executive Officer, is entitled to receive a base salary of $210,000 per year. During June 2003, Mr. Secord voluntarily began to accept a reduced salary of $105,000 per year and again on March 5, 2004 to $52,000 per year. Effective January 10, 2005, Mr. Secord requested he not receive any compensation until such time as he determines to demand the full $210,000 per year salary authorized by the Board. The salary Mr. Secord should have received has been accrued under employee accruals..

(2) Other Annual Compensation includes car allowance. For our Chief Executive Officer, Other Annual Compensation for 2004 and 2003 also includes the premiums of $24,000 per year on a $500,000 personal life insurance policy. During 2005 only one quarter of personal life insurance premium was paid - $6,000 and only 6 months of car allowance.

DIRECTOR COMPENSATION

We currently do not pay each non-employee director for attending quarterly board meetings, special meetings of the board and its committees as needed

ANNUAL MEETINGS, BOARD MEETINGS AND COMMITTEES

We request that all of the members of our Board of Directors attend each annual meeting of shareholders. During the years ending June 30, 2004 and 2005, our Board of Directors held board meetings and met informally on numerous occasions and approved relevant matters by written consent. All incumbent directors attended at least 75% of all board meetings and applicable committee meetings.

Our Board of Directors has a standing Audit Committee. The members of our Audit Committee are Harry C. Aderholt (Chairman), Brent M. Pratley and Milton R. Geilmann. All members of our Audit Committee are independent according to NASDAQ's listing standards, however, our Board of Directors has not determined that the Audit Committee has a member qualifying as an audit committee financial expert, as defined in Item 401(h) of Regulation S-K. The Company is seeking a possible member of the Board of Directors and audit committee as the financial expert.

Our Board of Directors adopted a written Audit Committee Charter in 2001. The Audit Committee oversees our accounting and financial reporting processes and related audits. This involves, among other tasks, the selection of our external auditors for ratification by our shareholders, pre-approving engagements of our auditors with respect to audit and non-audit services, reviewing our accounting practices and controls and administering our Code of Ethics for Officers and Finance Department Employees and whistleblower policy.

CODE OF ETHICS

We have adopted the FC-01 Business Ethics Policy Code of Ethics included in each employee packet for Officers and Finance Department Employees, which constitutes a code of ethics that applies to the principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, as defined in Item 406 of Regulation S-K under the Securities Exchange Act of 1934, as amended.

OPTION GRANTS IN LAST FISCAL YEAR

The following table sets forth individual grants of options to acquire shares of common stock we made to our Chief Executive Officer during the fiscal year ended June 30, 2005. No other grants were made to executive officers.

NAME	NUMBER OF SECURITIES UNDERLYING OPTIONS GRANTED	PERCENT OF TOTAL OPT GRANTED TO EMPLOYEES IN F
Richard V. Secord, Chairman and Chief Executive Officer (1)	2,000,000	83%

(1) Such options were fully vested when granted on June 12, 2005.

AGGREGATE OPTION EXERCISES AND FISCAL YEAR-END OPTION VALUES

The following table provides information regarding options held by our Chief Executive Officer as of June 30, 2005. No options were exercised by our Chief Executive Officer or any other executive officers during the year ended June 30, 2005.

NAME AND POSITION	SECURITIES ACQUIRED ON EXERCISE (#)	AGGREGATE VALUE REALIZED ($)	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS AT JUNE 30, 2005 EXERCISABLE (#)	UNEXERCISABLE (#)	IN EX
Richard V. Secord, Chairman and Chief Executive Officer	0	0	2,775,000	0	

(1) On June 30, 2005, the closing sale price for a share of our common stock on the OTC Bulletin Board was $0.11.

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following table sets forth, as of June 30, 2005, the number of common shares beneficially owned by (i) the persons known to the Company to be owners of more than 5% of the common stock, (ii) each director of the Company, (iii) each named executive officers as a group. Shares not outstanding but deemed beneficially owned by virtue of the right of any individual to acquire shares within 60 days are treated as outstanding only when determining the amount of and percentage of common stock owned by such individual.

Title of	Name and Address of	Amount & Nature of	Percentage of

Class	Beneficial owner	Beneficial owner	Class
Common	Richard V. Secord Chairman of the Board and Chief Executive Officer	3,165,286	2.8%
Common	Brent M. Pratley Director	30,600	*
Common	Milton R. Geilmann Director	25,000	*
Common	Harry C. Aderholt Director	172,500	*
5% SHAREHOLDERS OTHER THAN OFFICERS AND DIRECTORS			
Common	Thermal Imaging, Inc. 141 North State Street, Ste 150 Lake Oswego, Oregon 97034	9,229,855	8.1%
All executive officers and directors as a group (5 persons)		3,393,386	2.9%

* Less than 1%

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The Company indemnifies all board members and officers. During the fiscal year 2005, the Company did not incur any additional costs for indemnifications.

In May 2004 we entered into a loan transaction with Harry Aderholt, one of our directors. Mr. Aderholt loaned us $20,000, which we used for general corporate purposes. The loan is payable, with interest, at the rate of 6%. The loan is unsecured and does not stipulate maturity date.

ITEM 13. EXHIBITS

(a) EXHIBITS

NUMBER	DESCRIPTION
3.1.5**	Amendment to Articles of Incorporation filed February 17, 1998 (incorporated by reference to the Registrant's Registration Statement SB-2 filed March 3, 1998, as subsequently amended).
3.1.6**	Amendment to Articles of Incorporation filed July 5, 2000 (incorporated by reference to the Registrant's Registration Statement SB-2 filed March 3, 1998, as subsequently amended).
3.2**	Bylaws of Computerized Thermal Imaging, Inc., as amended January 15, 1998 (incorporated by reference to the Registrant's Registration Statement SB-2 filed March 3, 1998, as subsequently amended). Debenture (incorporated by reference to Form 8-K filed on January 14, 2002).
4.4**	Registration Rights Agreement (Debenture) (incorporated by reference to Form 8-K filed on January 14, 2002).
4.5**	Registration Rights Agreement (Equity Line) (incorporated by reference to Form 8-K filed on January 14, 2002).
10.1**	Computerized Thermal Imaging, Inc. 401(k) Retirement Plan Restatement 2001 (the "Plan") (incorporated by reference to

	Form S-8 filed on July, 15, 2002).
10.2**	Computerized Thermal Imaging, Inc. 401(k) Retirement Plan Restatement 2001 Amendment (incorporated by reference to Form S-8 filed on July, 15, 2002).
10.3**	Computerized Thermal Imaging, Inc. 401(k) Retirement Plan Restatement 2001 Second Amendment (incorporated by reference to Form S-8 filed on July, 15, 2002).
10.5**	Employment Agreement dated September 18, 2000 between Computerized Thermal Imaging, Inc. and Richard V. Secord (incorporated by reference to Form 10-K filed on September 30, 2002).
10.11**	Lease agreement dated June 13, 2001, between Computerized Thermal Imaging, Inc. and Silver Creek Engineering (incorporated by reference to Form 10-K/A filed on October, 2, 2001).
10.16**	Manufacturing license agreement with NanDa Thermal Medical Technology, Inc., (incorporated by reference to Form 8-K filed on June 24, 2003).

10.17**	Products supply and purchase agreement with NanDa Thermal Medical Technology, Inc., (incorporated by reference to Form 8-K filed on June 24, 2003).
10.18**	Sales agreement for Product "Kits" with NanDa Thermal Medical Technology, Inc., (incorporated by reference to Form 8-K filed on June 24, 2003).
21**	Subsidiaries of registrant (incorporated by reference to Form 10-K filed on September 30, 2002).
23.1*	Consent of HJ and Associates.
31.1*	Certification of Chief Executive Officer.
31.2*	Certification of Principal Accounting Officer

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

AUDIT FEES

The aggregate fees billed by HJ and Associates, our independent public accountants, for professional services rendered for the audit of our financial statements and the reviews of our interim financial statements included in our Quarterly Reports on Forms 10-Q were approximately $26,367 the fiscal year ended June 30, 2005 and approximately $45,513 for the fiscal year ended June 30, 2004.

AUDIT-RELATED FEES

The aggregate fees billed by HJ and Associates for assurance and related services performed by HJ and Associates that were reasonably related to the performance of the audit of our financial statements and are not reported in the preceding paragraph were approximately $1,156 for the fiscal year ended June 30, 2004 and nothing for the fiscal year ended June 30, 2005. Audit-related fees relate primarily to audits of employee benefit plans and miscellaneous accounting and internal control related consultations.

ALL OTHER FEES

There were no fees billed for other non-audit services during fiscal years 2005 and 2004..

PRE-APPROVAL POLICIES AND PROCEDURES

The Audit Committee of our Board of Directors ensures that we engage our public accountants to provide only audit and non-audit services that are compatible with maintaining the independence of our public accountants. Our Audit Committee approves or pre-approves all services provided by our public accountants. Permitted services include audit and audit-related services, tax and other non-audit related services. Certain services are identified as restricted. Restricted services are those services that may not be provided by our external public accountants, whether identified in statute or determined in the opinion of our Audit Committee to be incompatible with the role of an independent auditor. Our Audit Committee approved all fees identified in the preceding four paragraphs. During the fiscal year ended June 30, 2005, our Audit Committee reviewed all non-audit services provided by our external public accountants, and concluded that the provision of such non-audit services was compatible with maintaining the independence of the external public accountants.

SIGNATURES

In accordance with Sections 13 or 15(d) of the Exchange Act, the registrant caused this Annual Report on Form 10-KSB to be signed on its behalf by the undersigned, thereunto duly authorized.

COMPUTERIZED THERMAL IMAGING, INC.

Date: October 27, 2005

/s/ RICHARD V. SECORD

Richard V. Secord
Director, Chairman of the Board and
Chief Executive Officer

In accordance with the Exchange Act, this Annual Repot on Form 10-KSB has been signed by the following persons on behalf of the issuer and in the capacities and on the dates indicated.

/s/ Richard V. Secord — October 27, 2005

RICHARD V. SECORD
Director, Chairman of the Board and
Chief Executive Officer (Principal Executive Officer)

/s/ Richard V. Secord — October 27, 2005

RICHARD V. SECORD
Acting Chief Financial Officer (Principal Financial Officer)

/s/ Brent M. Pratley, M.D. October 27, 2005

BRENT M. PRATLEY, M.D.
Director

/s/ Milton R. Geilmann October 27, 2005

MILTON R. GEILMANN
Director

/s/ Harry C. Aderholt October 27, 2005

HARRY C. ADERHOLT
Director