VASOMEDICAL INC
Form 10-Q
April 16, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the quarterly period ended February 28, 2007

[ ] 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: 0-18105

VASOMEDICAL, INC.

(Exact name of registrant as specified in its charter)

Delaware	11-2871434
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)

180 Linden Ave., Westbury, New York 11590

(Address of principal executive offices)

Registrant's Telephone Number (516) 997-4600

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large Accelerated Filer [ ] Accelerated Filer [ ] Non-Accelerated Filer [X]

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

Number of Shares Outstanding of Common Stock, $.001 Par Value, at April 16, 2007 65,198,592

Page 1

Vasomedical, Inc. and Subsidiaries

INDEX

PART I - FINANCIAL INFORMATION

Item 1 - Financial Statements (unaudited)

Consolidated Condensed Balance Sheets as of February 28, 2007 and May 31, 2006

Consolidated Condensed Statements of Operations for the Nine and Three Months Ended February 28, 2007 and 2006

Consolidated Condensed Statement of Changes in Stockholders' Equity for the Period from June 1, 2006 to February 28, 2007

Consolidated Condensed Statements of Cash Flows for the Nine Months Ended February 28, 2007 and 2006

Notes to Consolidated Condensed Financial Statements

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations

Item 3 - Quantitative and Qualitative Disclosures About Market Risk

Item 4 - Controls and Procedures

PART II - OTHER INFORMATION

Page 2

ITEM 1. FINANCIAL STATEMENTS

Vasomedical, Inc. and Subsidiaries
CONSOLIDATED CONDENSED BALANCE SHEETS

ASSETS	February 2007 (Unaudite
CURRENT ASSETS	
Cash and cash equivalents	$1,041,
Accounts receivable, net of an allowance for doubtful accounts of $364,809 at February 28, 2007, and $410,691 at May 31, 2006	563,
Inventories, net	2,229,
Other current assets	170,
Total current assets	4,005,
PROPERTY AND EQUIPMENT, net of accumulated depreciation of $2,780,024 at February 28, 2007, and $2,613,180 at May 31, 2006	1,349,

OTHER ASSETS	271,
	$5,626,

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES	
Accounts payable and accrued expenses	$751,
Current maturities of long-term debt and notes payable	104,
Sales tax payable	135,
Deferred revenue	1,329,
Accrued director and executive compensation	79,
Accrued warranty and customer support expenses	20,
Accrued professional fees	85,
Accrued commissions	65,
Total current liabilities	2,571,
LONG-TERM DEBT	802,
ACCRUED WARRANTY COSTS	
DEFERRED REVENUE	495,
COMMITMENTS AND CONTINGENCIES	
STOCKHOLDERS' EQUITY	
Common stock, $.001 par value; 110,000,000 shares authorized; 65,198,592 shares at February 28, 2007, and May 31, 2006, issued and outstanding	65,
Additional paid-in capital	46,158,
Accumulated deficit	(44,466,
Total stockholders' equity	1,757,
	$5,626,

The accompanying notes are an integral part of these consolidated condensed financial statements.

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

	Nine Months Ended February 28,		
	2007	2006	200
Revenues			
Equipment sales	$2,080,272	$5,998,943	$43
Equipment rentals and services	2,906,308	3,059,433	94
Total revenues	4,986,580	9,058,376	1,38

Cost of Sales and Services			
Cost of sales, equipment	1,184,307	2,755,419	27
Cost of equipment rentals and services	1,097,766	993,613	32
Total cost of sales and services	2,282,073	3,749,032	60
Gross Profit	2,704,507	5,309,344	78
Operating Expenses			
Selling, general and administrative	3,381,852	6,769,946	1,02
Research and development	722,631	1,528,699	25
Provision for doubtful accounts	(1,340)	89,559	
Total operating expenses	4,103,143	8,388,204	1,28
LOSS FROM OPERATIONS	(1,398,636)	(3,078,860)	(50
Other Income (Expense)			
Interest and financing costs	(54,281)	(64,299)	(1
Interest and other income, net	48,269	59,041	1
Total other income (expense)	(6,012)	(5,258)	(
LOSS BEFORE INCOME TAXES	(1,404,648)	(3,084,118)	(50
Income tax expense, net	(14,000)	(7,112,826)	(
NET LOSS	(1,418,648)	(10,196,944)	(51
Preferred Stock Dividend	--	(877,870)	
NET LOSS ATTRIBUTABLE TO COMMON STOCKHOLDERS	$(1,418,648)	$(11,074,814)	$(51
Net loss per common share			
- basic	$(0.02)	$(0.18)	$
- diluted	$(0.02)	$(0.18)	$
Weighted average common shares outstanding			
- basic	65,198,592	60,063,566	65,19
- diluted	65,198,592	60,063,566	65,19

The accompanying notes are an integral part of these consolidated condensed financial statements.

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED CONDENSED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(Unaudited)

	Common Stock		Additional Paid-in	A
	Shares	Amount	Capital	
Balance at June 1, 2006	65,198,592	$65,198	$46,148,493	$(
Stock options granted for services			10,326	

Net loss				
Balance at February 28, 2007	65,198,592	$65,198	$46,158,819	$(

The accompanying notes are an integral part of these consolidated condensed financial statements.

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

	N
	2007
Cash flows from operating activities	
Net loss	$(1,418,6
Adjustments to reconcile net loss to net cash used in operating activities	
Depreciation and amortization	230,1
Provision for doubtful accounts	(1,3
Reserve for excess and obsolete inventory	
Deferred income taxes	
Common stock issued for services	
Stock options granted for services	10,3
Changes in operating assets and liabilities	
Accounts receivable	280,9
Inventories	495,0
Other current assets	129,8
Other assets	(1,0
Accounts payable, accrued expenses and other current liabilities	(604,8
Other liabilities	(228,0
	311,1
Net cash used in operating activities	(1,107,4
Cash flows provided by investing activities	
Redemptions of certificates of deposit	
Net cash provided by investing activities	
Cash flows provided by (used in) financing activities	
Payments on long term debt and notes payable	(236,3
Payments of preferred stock dividends	
Payments of preferred stock issue costs	
Proceeds from sale of convertible preferred stock	
Net cash provided by (used in) financing activities	(236,3

NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,343,8
Cash and cash equivalents - beginning of period	2,385,7
Cash and cash equivalents - end of period	$1,041,8

Non-cash investing and financing activities were as follows:	
Inventories transferred to (from) property and equipment, attributable to operating leases, net	$24,5
Issue of note for purchase of insurance policy	$192,1
Preferred stock dividends	$
Preferred stock issue costs	$
Supplemental Disclosures	
Interest paid	$54,2
Income taxes paid	$6,5

The accompanying notes are an integral part of these consolidated condensed financial statements.

Vasomedical, Inc. and Subsidiaries

ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

NOTE A - ORGANIZATION AND PLAN OF OPERATIONS

The Company was incorporated in Delaware in July 1987. During fiscal 1996, the Company commenced the commercialization of its EECP(R) external counterpulsation system ("EECP(R)"), a microprocessor-based medical device for the noninvasive, outpatient treatment of patients with cardiovascular disease. EECP(R) is marketed worldwide to hospitals and physician private practices. To date, the Company's revenues have been generated primarily from customers in the United States.

The Company has incurred large declines in revenue and has sustained significant operating losses during the last four fiscal years and its ability to continue operating as a going concern is dependent upon achieving profitability, a strategic alliance within the sales and marketing areas, or through additional debt or equity financing. Achieving profitability is largely dependent on sufficiently reducing operating costs and halting the current trend of declining revenue. The Company's ability to halt the declines in revenue and restore its revenue base is largely dependent upon increasing the demand in the refractory angina market and operating in a more efficient manner. To date the Company has not been able to restore its revenue base and reduce operating costs significantly enough to generate an adequate cash inflow, or raise additional capital, so we may not be able to continue as a going concern.

In order to reduce the Company's cash usage and attempt to bring its cost structure more into alignment with current revenue, the Company engaged in a restructuring in January 2006 and March 2007 to substantially reduce personnel and spending on sales, marketing and development projects. Additional cost reductions are continuing. However, revenue has continued to materially decline and the Company has not been able to achieve its goal of profitability.

The Company believes that cash flow from operations together with current cash reserves will be sufficient to fund projected capital requirements through May 2007, assuming the current revenue rate.

The Company is seeking to raise capital through public or private equity or debt financings or by other means. If the Company is unable to raise additional funds or obtain funds through arrangements with collaborative partners or others, it may be required to license or relinquish its rights to technologies and/or products. Future capital funding, if available, may result in dilution to current shareholders, and new investors could have rights superior to existing stockholders.

The accompanying financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

Reclassifications

Certain reclassifications have been made to the prior years' amounts to conform with the current year's presentation.

NOTE B - STOCK-BASED COMPENSATION

In December 2004, the FASB issued Statement of Financial Standards No. 123 (revised 2004), Share-Based Payment ("SFAS No. 123 (R)"), which is a revision of SFAS No. 123. SFAS No. 123 (R) supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and amends FASB Statement No. 95, Statement of Cash Flows. Generally, the approach to accounting for share-based payments in SFAS No. 123(R) is similar to the approach described in SFAS No. 123. However, SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. Pro forma disclosure of the fair value of share-based payments is no longer an alternative to financial statement recognition.

Prior to first quarter of fiscal 2007 the Company accounted for stock-based compensation using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related Interpretations ("APB No. 25") and adopted the disclosure provisions of Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of FASB Statement No. 123." Under APB No. 25, when the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized. Accordingly, no compensation expense has been recognized in the consolidated financial statements in connection with employee stock option grants prior to fiscal 2007.

The following table illustrates the proforma effect on net loss and loss per share had the Company applied the fair value recognition provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation, for the nine and three months ended February 28, 2006.

	Nine Months Ended February 28, 2006	Three Months Ended February 28, 2006
Net loss attributable to common		

stockholders, as reported	$(11,074,814)	$(694,781)
Deduct: Total stock-based employee compensation expense determined under fair value-based method for all awards	(618,715)	(184,973)
Pro forma net loss	$(11,693,529)	$(879,754)
Loss per share:		
Basic and diluted - as reported	$(0.18)	$(0.01)
Basic and diluted - pro forma	$(0.19)	$(0.01)

During the nine-month period ended February 28, 2007, the Board of Directors granted non-qualified stock options under the 1997 Stock Option/Stock Issuance Plan to one director to purchase an aggregate of 150,000 shares of common stock, at an exercise price of $.09 per share, and granted non-qualified stock options under the 1999 Stock Option/Stock Issuance Plan to three directors to purchase an aggregate of 450,000 shares of common stock, at an exercise price of $.09 per share, and granted non-qualified stock options under the 2004 Stock Option/Stock Issuance Plan to one officer to purchase an aggregate of 200,000 shares of common stock, at an exercise price of $.11 per share, which represented the fair market value of the underlying common stock at the time of the respective grants. These options vest over a two-year period, and expire ten years from the date of grant.

Stock-based compensation expense recognized under SFAS 123 (R) for the nine months ended February 28, 2007 was $10,326, which comprised the fair value of the stock options discussed above.

For purposes of estimating the fair value of each option on the date of grant, the Company utilized the Black-Scholes option-pricing model. The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's

opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The fair value of the Company's stock-based awards was estimated assuming no expected dividends and the following weighted-average assumptions for the nine months ended February 28, 2007:

Expected life (years)	5
Expected volatility	106.17%
Risk-free interest rate	4.5%
Expected dividend yield	0.00%

Equity instruments issued to non-employees in exchange for goods, fees and services are accounted for under the fair value-based method of SFAS No. 123(R).

During the nine-month period ended February 28, 2007, options and warrants to purchase 2,270,925 shares of common stock at an exercise price of $.20 - $5.00 were cancelled.

NOTE C -LOSS PER COMMON SHARE

Basic loss per share is based on the weighted average number of common shares outstanding without consideration of potential common shares. Diluted loss per share is based on the weighted number of common and potential common shares outstanding. The calculation takes into account the shares that may be issued upon the exercise of stock options and warrants, reduced by the shares that may be repurchased with the funds received from the exercise, based on the average price during the period, plus conversion of convertible preferred stock into common shares based upon the most advantageous conversion rate during the period.

The following table sets forth the computation of basic and diluted loss per common share:

	Nine Months Ended February 28,		Thr
	2007	2006	2007
Numerator:			
Net loss	$(1,418,648)	$(10,196,944)	$(510,
Deemed dividend related to beneficial conversion feature on Series D preferred stock	--	(786,247)	
Series D preferred stock dividends	--	(91,623)	
Net loss attributable to common stockholders - basic and diluted	$(1,418,648)	$(11,074,814)	$(510,
Denominator:			
Basic - weighted average common shares	65,198,592	60,063,566	65,198,
Stock options	--	--	
Warrants	--	--	
Convertible preferred stock	--	--	
Diluted - weighted average common shares	65,198,592	60,063,566	65,198,
Basic and diluted loss per common share	$(0.02)	$(0.18)	$(0

Vasomedical, Inc. and Subsidiaries

ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

Options, warrants, and convertible preferred stock, presented in with the

following table, were excluded from the computation of diluted loss per share for the nine and three months ended February 28, 2007 and 2006, respectively, because the effect of their inclusion would be antidilutive.

	Nine and three mont ended February 28	
	2007	
Options to purchase common stock	$6,741,150	$7,6
Warrants to purchase common stock	2,254,538	2,4
	$8,995,688	$10,0

NOTE D - INVENTORIES, NET

Inventories, net consist of the following:

	February 28, 2007	May 2
Raw materials	$848,349	$8
Work in process	982,800	1,2
Finished goods	398,022	5
	$2,229,171	$2,6

At February 28, 2007 and May 31, 2006, finished goods inventory is presented net of reserves for excess and obsolete inventory of $677,166.

NOTE E - PROPERTY AND EQUIPMENT

Property and equipment is summarized as follows:

	February 28, 2007	May 3 2006
Land	$200,000	$200,
Building and improvements	1,383,976	1,383,
Office, laboratory and other equipment	1,436,362	1,444,
EECP(R) systems under operating leases or under loan for clinical trials	829,453	874,
Furniture and fixtures	162,068	162,
Leasehold improvements	117,803	117,
	4,129,662	4,182,
Less: accumulated depreciation and amortization	(2,780,024)	(2,613,
	$1,349,638	$1,569,

NOTE F - NOTES PAYABLE

The Company financed the purchase of Director's and Officer's Liability

Insurance through the issuance of a note with a principal value of $192,120. The

note, which bears interest at 8.15%, is payable in ten monthly installments consisting of principal and interest, and expires in April 2007. The balance outstanding at February 28, 2007 of $39,471 is presented in the consolidated condensed balance sheet in current maturities of long-term debt and notes payable.

NOTE G - LONG-TERM DEBT

The following table sets forth the computation of long-term debt:

	February 28, 2007	May 31, 2006
Facility loans (a)	$866,753	$914,528
Term loans (b)	--	35,970
	866,753	950,498
Less: current portion	(64,631)	(97,309)
	$802,122	$853,189

(a) The Company purchased its headquarters and warehouse facility and secured notes of $641,667 and $500,000, respectively, under two programs sponsored by New York State. These notes, which bear interest at 7.8% and 6%, respectively, are payable in monthly installments consisting of principal and interest payments over fifteen-year terms, expiring in September 2016 and January 2017, respectively, and are secured by the building.

(b) In fiscal years 2003 and 2004, the Company financed the cost and implementation of a management information system and secured several notes, aggregating approximately $305,219. The notes, which bear interest at rates ranging from 7.5% through 12.5%, were payable in monthly installments consisting of principal and interest payments over four-year terms, and expired at various times between August and October 2006.

NOTE H - DEFERRED REVENUES

The changes in the Company's deferred revenues are as follows:

	Nine Months Ended February 28,		Th
	2007	2006	2007
Deferred Revenue at the beginning of the period	$2,322,588	$2,551,532	$2,051
ADDITIONS			
Deferred extended service contracts	1,483,702	1,713,937	434

Deferred in-service and training	35,000	115,000	10
Deferred service arrangements	105,000	355,000	30
RECOGNIZED AS REVENUE			
Deferred extended service contracts	(1,882,386)	(1,770,002)	(640
Deferred in-service and training	(35,000)	(107,500)	(10
Deferred service arrangements	(204,375)	(412,083)	(50
Deferred revenue at end of period	1,824,529	2,445,884	1,824
Less: current portion	(1,329,333)	(1,629,143)	(1,329
Long-term deferred revenue at end of period	$495,196	$816,741	$495

ITEM 1. NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

NOTE I - WARRANTY COSTS

The changes in the Company's product warranty liability are as follows:

	Nine Months Ended February 28,		Thr
	2007	2006	2007
Warranty liability at the beginning of the period	$32,000	$118,333	$26,
Expense for new warranties issued	36,000	24,000	6,
Warranty amortization	(47,500)	(97,333)	(12,
Warranty liability at end of period	20,500	45,000	20,
Less: current portion	(20,500)	(42,750)	(20,
Long-term warranty liability at end of period	$--	$2,250	

NOTE J - INCOME TAXES

During the nine-months ended February 28, 2007 and 2006, we recorded a provision for income taxes of $14,000 and $7,112,826, respectively. The fiscal 2006 tax expense consists mainly of $7,093,000 in additional valuation allowance against the deferred tax asset arising in the second fiscal quarter of 2006. The income tax expense for the first nine months of fiscal 2006 does not include $7,489,000 added to the deferred tax valuation allowance for tax benefits associated with prior years' exercises of stock options and warrants, which was charged directly to additional paid-in capital.

As of February 28, 2007 the recorded deferred tax assets were $20,038,976, reflecting an increase of $479,518 during the nine months ended February 28, 2007, which was offset by the valuation allowance of the same amount. The deferred tax assets primarily relate to NOL's of approximately $48.6 million. The potential tax benefits of the NOL's expire at various dates through 2027.

Ultimate realization of any or all of the deferred tax assets is not assured, due to significant uncertainties and material assumptions associated with estimates of future taxable income during the carryforward period. In February 2006, we concluded that, based upon the weight of available evidence,

it was "more likely than not" that the net deferred tax asset would not be realized and increased the valuation allowance to bring the net deferred tax asset carrying value to zero.

NOTE K - COMMITMENTS AND CONTINGENCIES

Employment Agreements

The approximate aggregate minimum compensation obligation under active employment agreements at February 28, 2007 is summarized as follows:

Twelve months ended February 28,	Amount
2008	$ 260,000
2009	80,167
Total	$ 340,167

Litigation

The Company is currently, and has in the past been, a party to various routine legal proceedings incident to the ordinary course of business. The Company believes that the outcome of all such pending legal proceedings in the aggregate is unlikely to have a material adverse effect on the business or consolidated financial condition of the Company.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Except for historical information contained in this report, the matters discussed are forward-looking statements that involve risks and uncertainties. When used in this report, words such as "anticipated", "believes", "could", "estimates", "expects", "may", "plans", "potential" and "intends" and similar expressions, as they relate to the Company or its management, identify forward-looking statements. Such forward-looking statements are based on the beliefs of the Company's management, as well as assumptions made by and information currently available to the Company's management. Among the factors that could cause actual results to differ materially are the following: the effect of business and economic conditions; the effect of the dramatic changes taking place in the healthcare environment; the impact of competitive procedures and products and their pricing; medical insurance reimbursement policies; unexpected manufacturing or supplier problems; unforeseen difficulties and delays in the conduct of clinical trials and other product development programs; the actions of regulatory authorities and third-party payers in the United States and overseas; uncertainties about the acceptance of a novel therapeutic modality by the medical community; and the risk factors reported from time to time in the Company's SEC reports , including the ability of the Company to continue as a going concern. The Company undertakes no obligation to update forward-looking statements as a result of future events or developments.

General Overview

Vasomedical, Inc. incorporated in Delaware in July 1987, develops, manufactures and markets EECP(R) therapy systems to deliver its proprietary form of enhanced external counterpulsation therapy. EECP(R) therapy is a noninvasive, outpatient therapy used in the treatment of ischemic cardiovascular diseases, currently used to manage chronic stable angina and heart failure. The therapy increases blood flow and oxygen supply to the heart muscle and other organs and decreases the heart's workload and need for oxygen, while also improving function of the endothelium, the inner lining of blood vessels throughout the body, lessening resistance to blood flow. We provide hospitals and physician private practices with EECP(R) equipment, treatment guidance, and a staff training and equipment maintenance program designed to provide optimal patient outcomes. EECP(R) is a registered trademark for Vasomedical's enhanced external counterpulsation systems. For more information visit www.vasomedical.com.

We have Food and Drug Administration (FDA) clearance to market our EECP(R) therapy for use in the treatment of stable and unstable angina, congestive heart failure, acute myocardial infarction, and cardiogenic shock, however our current marketing efforts are limited to the treatment of chronic stable angina and congestive heart failure. Medicare and other third-party payers currently reimburse for the treatment of angina symptoms in patients with moderate to severe symptoms who are refractory to medications and not candidates for invasive procedures, including patients with serious comorbidities, such as heart failure, diabetes, peripheral vascular disease, etc. Patients with primary diagnoses of heart failure, diabetes, peripheral vascular disease, etc. are also reimbursed under the same criteria, provided the primary indication for treatment with EECP(R) therapy is angina symptoms.

We recently sponsored a pivotal, randomized clinical trial to demonstrate the efficacy of EECP(R) therapy in the most prevalent types of heart failure patients. This trial, known as PEECH(TM) (Prospective Evaluation of EECP(R) in Congestive Heart Failure), was intended to provide additional evidence of the safety and efficacy of EECP(R) therapy in the treatment of mild-to-moderate heart failure and to support our application for expansion of the Medicare national reimbursement coverage policy to include mild-to-moderate heart failure as a primary indication. Results of the trial were initially published on line by the Journal of the American College of Cardiology (JACC) on August 25, 2006, and in print in its September 19, 2006 issue. JACC is the official journal of the American College of Cardiology. The PEECH trial was a positive clinical trial, having met the statistical requirement of meeting at least one of its co-primary endpoints, a significant difference in the proportion of patients satisfying a prespecified threshold of improvement in exercise duration. The trial also demonstrated significant improvements in favor of EECP(R) therapy on several important secondary endpoints, including exercise duration and improvement in symptom status and quality of life. Measures of change in peak

oxygen consumption were not statistically significant in the overall study population, though a trend favoring EECP(R) therapy was present in early follow-up. Patients in the trial who had an ischemic etiology, i.e. pre-existing coronary artery disease, demonstrated a greater response to EECP(R) therapy than those who had an idiopathic (non-ischemic) etiology.

Very recently, a second report of results from the PEECH(TM) trial was published in the November-December 2006 issue of the journal Congestive Heart

Failure, focusing on the results of a prespecified subgroup analysis in trial patients age 65 and over. This analysis demonstrated a statistically positive response on both co-primary endpoints of the trial in patients receiving EECP(R) therapy versus those who did not, i.e. a significantly larger proportion of patients undergoing EECP(R) therapy met or exceeded prespecified thresholds of improvement in exercise duration and peak oxygen consumption. Moreover, the patients age 65 and older who received EECP(R) therapy demonstrated the greatest differences in exercise duration, peak oxygen consumption and functional class (symptom status) compared with those who did not receive EECP(R) therapy.

The preliminary results of the PEECH(TM) trial were presented at the American College of Cardiology scientific sessions in March 2005. On June 20, 2005, the Centers for Medicare and Medicaid Services (CMS) accepted our application for expansion of reimbursement coverage of EECP(R) therapy to include patients with New York Heart Association (NYHA) Class II/III stable heart failure symptoms with an ejection fraction of less than or equal to 35%, i.e. chronic, stable, mild-to-moderate systolic heart failure as a primary indication, as well as patients with Canadian Cardiovascular Society Classification (CCSC) II, i.e. chronic, stable mild angina.

On June 23, 2005, CMS also received a request from a competing manufacturer of external counterpulsation therapy equipment, to reconsider the reimbursement coverage policy. They requested expansion of coverage to include 1) treatment of congestive heart failure, to include NYHA Class II, III with a left ventricular ejection fraction (LVEF) less than or equal to 40%, and acute heart failure; 2) treatment of stable angina to include CCSC II angina; 3) treatment of acute myocardial infarction; 4) treatment of cardiogenic shock. On September 15, 2005, they amended their request to include NYHA Class IV heart failure.

On March 20, 2006, the Centers for Medicare and Medicaid Services (CMS) issued their Decision Memorandum regarding this reconsideration with the opinion "that the evidence is not adequate to conclude that external counterpulsation therapy is reasonable and necessary for the treatment of:

- Canadian Cardiovascular Society Classification (CCSC) II angina
- Heart Failure
  - New York Heart Association Class II/III stable heart failure symptoms with an ejection fraction of less than or equal to 35%
  - New York Heart Association Class II/III stable heart failure symptoms with an ejection fraction of less than or equal to 40%
  - New York Heart Association Class IV heart failure
  - Acute heart failure
- Cardiogenic shock
- Acute myocardial infarction."

They commented in their decision memorandum that they were not able to apply full weight to the evidence generated by the PEECH trial, as it had not yet been published in a peer-reviewed medical journal by the time they were required to issue a final decision on this application. Moreover, they did not opine on whether they would consider the results of the trial when published to be sufficient evidence to conclude that external counterpulsation therapy is reasonable and necessary for the treatment of New York Heart Association Class II/III stable heart failure symptoms with an ejection fraction of less than or equal to 35%. They did, however, reiterate in the decision memorandum that "Current coverage as described in Section 20.20 of the Medicare National Coverage Determination (NCD) manual will remain in effect."

CONDITION AND RESULTS OF OPERATIONS

We will continue to educate the marketplace that EECP(R) therapy is a therapy for ischemic cardiovascular disease and that patients with a primary diagnosis of heart failure, diabetes, peripheral vascular disease, etc. are also eligible for reimbursement under the current coverage policy, provided the primary indication for treatment with EECP(R) therapy is angina or angina equivalent symptoms and the patient satisfies other listed criteria. Additionally, we will continue to pursue expansion of coverage for EECP(R)therapy with Medicare and other third-party payers as evidence of its clinical utility develops.

Critical Accounting Policies

Financial Reporting Release No. 60, which was released by the Securities and Exchange Commission, or SEC, in December 2001, requires all companies to include a discussion of critical accounting policies or methods used in the preparation of financial statements. Note A of the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended May 31, 2006, includes a summary of our significant accounting policies and methods used in the preparation of our financial statements. In preparing these financial statements, we have made our best estimates and judgments of certain amounts included in the financial statements, giving due consideration to materiality. The application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates. Our critical accounting policies are as follows:

Revenue Recognition

We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred or service has been rendered, the price is fixed or determinable and collectibility is reasonably assured. In the United States, we recognize revenue from the sale of our EECP(R) systems in the period in which we deliver the system to the customer. Revenue from the sale of our EECP(R) systems to international markets is recognized upon shipment, during the period in which we deliver the product to a common carrier, as are supplies, accessories and spare parts delivered to both domestic and international customers. Returns are accepted prior to the in-service and training subject to a 10% restocking charge or for normal warranty matters, and we are not obligated for post-sale upgrades to these systems. In addition, we use the installment method to record revenue based on cash receipts in situations where the account receivable is collected over an extended period of time and in our judgment the degree of collectibility is uncertain.

In most cases, revenue from domestic EECP(R) system sales is generated from multiple-element arrangements that require judgment in the areas of customer acceptance, collectibility, the separability of units of accounting, and the fair value of individual elements. Effective September 1, 2003, we adopted the provisions of Emerging Issues Task Force, or EITF, Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables", ("EITF 00-21"), on a prospective basis. The principles and guidance outlined in EITF 00-21 provide a framework to determine (a) how the arrangement consideration should be measured (b) whether the arrangement should be divided into separate units of accounting, and (c) how the arrangement consideration should be allocated among the separate units of accounting. We determined that the domestic sale of our EECP(R) systems includes a combination of three elements that qualify as separate units of accounting:

i. EECP(R) equipment sale,
ii. provision of in-service and training support consisting of equipment

set-up and training provided at the customer's facilities, and

iii. a service arrangement (usually one year), consisting of: service by factory-trained service representatives, material and labor costs, emergency and remedial service visits, software upgrades, technical phone support and preferred response times.

Each of these elements represent individual units of accounting as the delivered item has value to a customer on a stand-alone basis, objective and reliable evidence of fair value exists for undelivered items, and arrangements normally do not contain a general right of return relative to the delivered item. We determine fair value based on the price of the deliverable when it is sold separately or based on third-party evidence. In accordance with the guidance in EITF 00-21, we use the residual method to allocate the arrangement consideration when it does not have fair value of the EECP(R) system sale. Under the residual method, the amount of consideration allocated to the delivered item equals the total arrangement consideration less the aggregate fair value of the

undelivered items. Assuming all other criteria for revenue recognition have been met, we recognize revenue for:

i. EECP(R) equipment sales, when delivery and acceptance occurs based on delivery and acceptance documentation received from independent shipping companies or customers,

ii. in-service and training, following documented completion of the training, and

iii. the service arrangement, ratably over the service period, which is generally one year.

In-service and training generally occurs within three weeks of shipment and our return policy states that no returns will be accepted after in-service and training has been completed. The amount related to in-service and training is recognized as revenue at the time the in-service and training is completed and the amount related to service arrangements is recognized as service revenue ratably over the related service period, which is generally one year. Costs associated with the provision of in-service and training and the service arrangement, including salaries, benefits, travel, spare parts and equipment, are recognized in cost of sales as incurred.

We also recognize revenue generated from servicing EECP(R) systems that are no longer covered by the service arrangement, or by providing sites with additional training, in the period that these services are provided. Revenue related to future commitments under separately priced extended service agreements on our EECP(R) system are deferred and recognized ratably over the service period, generally ranging from one year to four years. Costs associated with the provision of service and maintenance, including salaries, benefits, travel, spare parts and equipment, are recognized in cost of sales as incurred. Amounts billed in excess of revenue recognized are included as deferred revenue in the consolidated balance sheets.

Revenues from the sale of EECP(R) systems through our international distributor network are generally covered by a one-year warranty period. For these customers we accrue a warranty reserve for estimated costs to provide warranty parts when the equipment sale is recognized.

We have also entered into lease agreements for our EECP(R) systems, generally for terms of one year or less, that are classified as operating leases. Revenues from operating leases are generally recognized, in accordance with the terms of the lease agreements, on a straight-line basis over the life of the respective leases. For certain operating leases in which payment terms are determined on a "fee-per-use" basis, revenues are recognized as incurred (i.e., as actual usage occurs). The cost of the EECP(R) system utilized under operating leases is recorded as a component of property and equipment and is amortized to cost of sales over the estimated useful life of the equipment, not to exceed five years. There were no significant minimum rental commitments on these operating leases at February 28, 2007.

Accounts Receivable, net

The Company's accounts receivable - trade are due from customers engaged in the provision of medical services. Credit is extended based on evaluation of a customer's financial condition and, generally, collateral is not required. Accounts receivable are generally due 30 to 90 days from shipment and are stated at amounts due from customers net of allowances for doubtful accounts, returns, term discounts and other allowances. Accounts that remain outstanding longer than the contractual payment terms are considered past due. Estimates are used in determining the allowance for doubtful accounts based on the Company's historical collections experience, current trends, credit policy and a percentage of our accounts receivable by aging category. In determining these percentages, we look at historical write-offs of our receivables. The Company also looks at the credit quality of its customer base as well as changes in its credit policies. The Company continuously monitors collections and payments from its customers. While credit losses have historically been within expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same credit loss rates that it has in the past.

Inventories, net

The Company values inventory at the lower of cost or estimated market, cost being determined on a first-in, first-out basis. The Company often places EECP(R) systems at various field locations for demonstration, training, evaluation, and other similar purposes at no charge. The cost of these EECP(R) systems is transferred to property and equipment and is amortized over the next two to five years. The Company records the cost of refurbished components of EECP(R) systems and critical components at cost plus the cost of refurbishment. The Company regularly reviews inventory quantities on hand, particularly raw materials and components, and records a provision for excess and obsolete inventory based primarily on existing and anticipated design and engineering changes to our products as well as forecasts of future product demand.

Effective June 1, 2005, we adopted the provisions of Statement of Financial Accounting Standards No. 151, "Inventory Costs", on a prospective basis. The statement clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. As a result of adopting SFAS No. 151, we absorbed approximately $81,000 less in fixed

production overhead into inventory.

Deferred Revenues

We record revenue on extended service contracts ratably over the term of the related warranty contracts. Effective September 1, 2003, we prospectively adopted the provisions of EITF 00-21. Upon adoption of the provisions of EITF 00-21 we began to defer revenue related to EECP(R) system sales for the fair value of installation and in-service training to the period when the services are rendered and for warranty obligations ratably over the service period, which is generally one year.

Warranty Costs

Equipment sold is generally covered by a warranty period of one year. Effective September 1, 2003, we adopted the provisions of EITF 00-21 on a prospective basis. Under EITF 00-21, for certain arrangements, a portion of the overall system price attributable to the first year service arrangement is deferred and recognized as revenue over the service period. As such, we no longer accrue warranty costs upon delivery but rather recognize warranty and related service costs as incurred. Prior to September 1, 2003, we accrued a warranty reserve for estimated costs to provide warranty services when the equipment sale was recognized.

Equipment sold to international customers through our distributor network is generally covered by a one-year warranty period. For these customers we accrue a warranty reserve for estimated costs of providing a parts only warranty when the equipment sale is recognized.

The factors affecting our warranty liability included the number of units sold and historical and anticipated rates of claims and costs per claim.

Net Loss per Common Share

Basic losses per share are based on the weighted average number of common shares outstanding without consideration of potential common stock. Diluted losses per share are based on the weighted number of common and potential dilutive common shares outstanding. The calculation takes into account the shares that may be issued upon the exercise of stock options and warrants, reduced by the shares that may be repurchased with the funds received from the exercise, based on the average price during the period.

Income Taxes

Deferred income taxes are recognized for temporary differences between financial statement and income tax bases of assets and liabilities and loss carryforwards for which income tax benefits are expected to be realized in future years. A valuation allowance is established, when necessary, to reduce

deferred tax assets to the amount expected to be realized. In estimating future tax consequences, we generally consider all expected future events other than an enactment of changes in the tax laws or rates. The deferred tax asset is continually evaluated for realizability. To the extent our judgment regarding

the realization of the deferred tax assets change, an adjustment to the allowance is recorded, with an offsetting increase or decrease, as appropriate, in income tax expense. Such adjustments are recorded in the period in which our estimate as to the realizability of the asset changed that it is "more likely than not" that all of the deferred tax assets will be realized. The "more likely than not" standard is subjective, and is based upon our estimate of a greater than 50% probability that our long range business plan can be realized.

Deferred tax liabilities and assets are classified as current or non-current based on the classification of the related asset or liability for financial reporting. A deferred tax liability or asset that is not related to an asset or liability for financial reporting, including deferred tax assets related to carryforwards, are classified according to the expected reversal date of the temporary difference. The deferred tax asset we recorded relates primarily to the realization of net operating loss carryforwards, of which the allocation of the current portion, if any, reflects the expected utilization of such net operating losses in next twelve months. Such allocation is based on our internal financial forecast and may be subject to revision based upon actual results.

Stock-based Employee Compensation

In December 2004, the FASB issued Statement of Financial Standards No. 123 (revised 2004), Share-Based Payment ("SFAS No. 123 (R)"), which is a revision of SFAS No. 123. SFAS No. 123 (R) supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees, and amends FASB Statement No. 95, Statement of Cash Flows. Generally, the approach to accounting for share-based payments in SFAS No. 123(R) is similar to the approach described in SFAS No. 123. However, SFAS No. 123(R) requires all share-based payments to employees including grants of employee stock options, to be recognized in the financial statements based on their fair values. Pro forma disclosure of the fair value of share-based payments is no longer an alternative to financial statement recognition. The Company has five stock-based employee compensation plans.

Prior to second quarter of fiscal 2007 the Company accounts for stock-based compensation using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related Interpretations ("APB No. 25") and has adopted the disclosure provisions of Statement of Financial Accounting Standards No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of FASB Statement No. 123." Under APB No. 25, when the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized. Accordingly, no compensation expense has been recognized in the consolidated financial statements in connection with employee stock option grants prior to fiscal 2007.

In May 2006, the compensation committee of the board of directors accelerated the vesting provision of all outstanding stock options and warrants so that they were fully vested at May 31, 2006, and as a result the Company expects that the adoption of SFAS No. 123(R) will not have an immediate material effect on its financial statements, however as new stock options are issued the Company has adopted SFAS No 123(R) and this will have a material effect on its quarterly and annual financial statements, in the form of additional compensation expense. It is not possible to precisely determine the expense impact of adoption since a portion of the ultimate expense that is recorded will likely relate to awards that have not yet been granted. The expense associated with these future awards can only be determined based on factors such as the price for the Company's common stock, volatility of the Company's stock price and risk free interest rates as measured at the grant date. However, the pro forma disclosures related to SFAS No. 123 included in the Company's historic financial statements are relevant data points for gauging the potential level of expense that might be recorded in future periods.

For purposes of estimating the fair value of each option on the date of grant, the Company utilized the Black-Scholes option-pricing model.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

Equity instruments issued to non-employees in exchange for goods, fees and services are accounted for under the fair value-based method of SFAS No. 123 (R).

Recently Issued Accounting Standards

Statement of Financial Accounting Standards No. 152, "Accounting for Real Estate Time-Sharing Transactions", an amendment of FASB Statements No. 66 and 67 (SFAS 152) was issued in December 2004 and becomes effective for financial statements for fiscal years beginning after June 15, 2005. The Company does not expect that SFAS 152 will have an effect on future financial statements.

In December 2004, the FASB issued FASB Statement No. 153 ("SFAS No. 153"), "Exchanges of Non-monetary Assets - an amendment of APB Opinion No. 29". SFAS No. 153 amends Opinion 29 to eliminate the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. A non-monetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS No. 153 is effective for fiscal periods after June 15, 2005. The Company does not expect the adoption of SFAS No. 153 to have a material impact on the Company's consolidated financial statements.

In May 2005, the FASB issued Statement of Financial Accounting Standards No. 154 ("SFAS No. 154"), "Accounting Changes and Error Corrections." SFAS No. 154 replaces APB Opinion No. 20, Accounting Changes, and FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements, and changes the requirements for the accounting for and reporting of a change in accounting principle. The Statement applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. When a pronouncement includes specific transition provisions, those provisions should be followed. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

Statement of Financial Accounting Standards No. 155, Accounting for Certain Hybrid Financial Instruments--an amendment of FASB Statements No. 133 and 140, was issued in February 2006 and is effective for all financial instruments

acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. Certain parts of this Statement may be applied prior to the adoption of this Statement. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided the entity has not yet issued financial statements, including financial statements for any interim period for that fiscal year. Provisions of this Statement may be applied to instruments that an entity holds at the date of adoption on an instrument-by-instrument basis. The Company does not expect that SFAS 155 will have any significant effect on future financial statements.

Statement of Financial Accounting Standards No. 156, Accounting for Servicing of Financial Assets--an amendment of FASB Statement No. 140, pertains to the servicing of financial assets and was issued in March 2006 and should be adopted as of the beginning of its first fiscal year that begins after September 15, 2006. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided the entity has not yet issued financial statements, including interim financial statements, for any period of that fiscal year. The Company does not expect that SFAS 156 will have any significant effect on future financial statements.

In March 2005, FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations--an interpretation of FASB Statement No. 143 (FIN 47). FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005 (December 31, 2005, for calendar-year enterprises). Retrospective application for interim financial information is permitted but is not required. Early adoption of this Interpretation is encouraged. The Company does not expect that FIN 47 will have any significant effect on future financial statements.

In December 2004, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants (AcSEC) issued Statement of Position 04-2, Accounting for Real Estate Time-Sharing Transactions (SOP 04-2). SOP 04-2 is effective for financial statements issued for fiscal years beginning after June 15, 2005, with earlier application encouraged. The Company does not expect that SOP 04-2 will have any effect on future financial statements.

In September 2005, AcSEC issued Statement of Position 05-1: Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts (SOP 05-1). SOP 05-1 is effective for fiscal years beginning after December 15, 2006, with earlier adoption encouraged. The Company does not expect that SOP 05-1 will have any effect on future financial statements.

FASB Staff Position (FSP) FAS 13-1--Accounting for Rental Costs Incurred during a Construction Period, was issued on October 6, 2005, and becomes effective for new transactions or arrangements entered into after the beginning of the first fiscal quarter following the date that the final FSP is posted by the FASB. The Company does not expect that FSP 13-1 will have any significant effect on future financial statements.

On June 29, 2005, the FASB ratified the consensus reached for Emerging Issues Task Force (EITF) Issue No. 05-5, Accounting for Early Retirement or Postemployment Programs with Specific Features (Such As Terms Specified in

Altersteilzeit Early Retirement Arrangements). The consensus in this Issue should be applied to fiscal years beginning after December 15, 2005, and reported as a change in accounting estimate effected by a change in accounting principle as described in paragraph 19 of FASB Statement 154. The Company does not expect that EITF 05-5 will have any significant effect on future financial statements.

On September 28, 2005, the FASB ratified the consensus reached for EITF Issue No. 05-7, Accounting for Modifications to Conversion Options Embedded in Debt Instruments and Related Issues. The provisions of this Issue should be applied to future modifications of debt instruments beginning in the first interim or annual reporting period beginning after December 15, 2005. The Company expects that the application of EITF 05-7 could have an effect on interest and debt valuations in future financial statements. It is not possible to determine the impact, if any, from the application since the Company does not presently have any convertible debt.

On July 13, 2006, the FASB issued Interpretation No. 48 for Uncertainty in Income Taxes and Interpretation of FASB Statement 109. Interpretation 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with Statement No. 109 and prescribes a recognition threshold and measurement attribute for financial statements disclosure of tax position taken or expected to be taken on a tax return. Additionally, Interpretation No. 48 provides guidance on depreciation, classification, interest and penalties accounting in interim periods, disclosure and transition. Interpretation No. 48 is effective for fiscal years beginning after December 15, 2006, with early adoption permitted. The Company is currently evaluating whether the adoption of Interpretation No. 48 will have a material effect on our consolidated financial position, results of operations and cash flows.

In July 2006, the FASB issued Staff Position ("FSB") on FAS 13, FSP FAS 13-2, Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction. FSP FAS 13-2 addresses how a change or projected change in the timing of cash flows relating to income taxes generated by a leveraged lease transaction affects the accounting by a lessor for that lease and amends FAS 13 Accounting for Leases.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FSP FAS 13-2 is effective for fiscal years beginning December 15, 2006, with earlier application permitted. The Company does not expect that FSP FAS 13-2 will have any significant effect on future financial statements.

Statement of Financial Accounting Standards No. 157, Fair Value Measurements. This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the Board having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. However, for some entities, the application of this Statement will change current practice. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Earlier application is encouraged, provided that the

reporting entity has not yet issued financial statements for that fiscal year, including financial statements for an interim period within that fiscal year. The Company does not expect that this pronouncement will have any significant effect on future financial statements.

FASB Staff Position (FSP) No. FIN 46(R)-6, Determining the Variability to Be Considered in Applying FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities. Posted on April 13, 2006. An enterprise shall apply the guidance in this FSP prospectively to all entities (including newly created entities) with which that enterprise first becomes involved and to all entities previously required to be analyzed under Interpretation 46(R) when a reconsideration event has occurred pursuant to paragraph 7 of Interpretation 46(R) beginning the first day of the first reporting period beginning after June 15, 2006. Early application is permitted for periods for which financial statements have not yet been issued. Retrospective application to the date of the initial application of Interpretation 46(R) is permitted but not required. Retrospective application, if elected, must be completed no later than the end of the first annual reporting period ending after July 15, 2006. The Company does not expect that this pronouncement will have any significant effect on future financial statements.

FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations--an interpretation of FASB Statement No. 143 (FIN 47) was issued in March 2005. FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005 (December 31, 2005, for calendar-year enterprises). Retrospective application for interim financial information is permitted but is not required. Early adoption of this Interpretation is encouraged. The Company does not expect that FIN 47 will have any significant effect on future financial statements.

FASB Staff Position (FSP) No. FTB 85-4-1, Accounting for Life Settlement Contracts by Third-Party Investors, was posted in March 27, 2006 and is effective for fiscal years beginning after June 15, 2006. It provides initial and subsequent measurement guidance and financial statement presentation and disclosure guidance for investments by third-party investors in life settlement contracts. This FSP also amends certain provisions of FASB Technical Bulletin No. 85-4, Accounting for Purchases of Life Insurance, and FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities. The Company does not expect that (FSP) No. FTB 85-4-1 will have any effect on future financial statements.

Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans--an amendment of FASB Statements No. 87, 88, 106, and 132(R). This Statement requires employers to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income of a business entity or changes in unrestricted net assets of a not-for-profit organization. This Statement also requires employers to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions.

An employer with publicly traded equity securities is required to initially recognize the funded status of a defined benefit postretirement plan and to provide the required disclosures as of the end of the fiscal year ending after December 15, 2006.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

An employer without publicly traded equity securities is required to recognize the funded status of a defined benefit postretirement plan and to provide the required disclosures as of the end of the fiscal year ending after June 15, 2007. The Company does not expect that SFAS 158 will have any significant effect on future financial statements.

Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment to FASB Statement No. 115. This Statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with the Board's long-term measurement objectives for accounting for financial instruments. This Statement is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007, and interim periods within those fiscal years. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of FASB Statement No. 157, Fair Value Measurements. The Company does not expect that SFAS 158 will have any significant effect on future financial statements.

FASB Staff Position (FSP) No. AUG AIR-1, Accounting for Planned Major Maintenance Activities, was posted on September 8, 2006 and is effective for the first fiscal year beginning after December 15, 2006. This FSP addresses the accounting for planned major maintenance activities and amends certain provisions in the AICPA Industry Audit Guide, Audits of Airlines (Airline Guide), and APB Opinion No. 28, Interim Financial Reporting. The Airline Guide permits four alternative methods of accounting for planned major maintenance activities: direct expense, built-in overhaul, deferral, and accrual (accrue-in-advance). Those methods are widely used by other industries. The FSP prohibits the use of the accrue-in-advance method. The Company does not expect that this pronouncement will have any significant effect on future financial statements.

FASB Staff Position No. FAS 126-1, Applicability of Certain Disclosure and Interim Reporting Requirements for Obligors for Conduit Debt Securities, was posted on October 25, 2006. This FASB Staff Position (FSP) clarifies the definition of a public entity in certain accounting standards to include entities that are conduit bond obligors for conduit debt securities that are traded in a public market. The guidance in this FSP is to be applied prospectively in fiscal periods beginning after December 15, 2006. The Company does not expect that this pronouncement will have any significant effect on future financial statements.

FASB Staff Position (FSP) No. EITF 00-19-2, Accounting for Registration Payment Arrangements. Posted on December 21, 2006. This FASB Staff Position (FSP) addresses an issuer's accounting for registration payment arrangements. This FSP specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with FASB Statement No. 5, Accounting for Contingencies. Effective immediately. The Company does not expect that this pronouncement will have any significant effect on future financial statements.

EITF Issue 06-8, Applicability of the Assessment of a Buyer's Continuing Investment under FASB Statement No. 66 for Sales of Condominiums. In assessing the collectibility of the sales price pursuant to paragraph 37(d) of Statement 66, an entity should evaluate the adequacy of the buyer's initial and continuing investment to conclude that the sales price is collectible. This Issue is effective for the first annual reporting period beginning after March 15, 2007. Earlier application is permitted as of the beginning of an entity's fiscal year provided that the entity has not yet issued financial statements for that fiscal year. The Company does not expect that this pronouncement will have any significant effect on future financial statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

Three Months Ended February 28, 2007 and 2006

Net revenue from sales, leases and service of our EECP(R) systems for the three-month periods ended February 28, 2007 and 2006, was $1,381,501 and $2,841,821, respectively, which represented a decline of $1,460,320 or 51%. We reported a net loss of $510,256 compared to $671,447 for the three-month periods ended February 28, 2007 and 2006, respectively. We reported a net loss attributable to common stockholders of $510,256 and $694,781 for the third quarter of fiscal 2007 and 2006, respectively. Our net loss per common share was $0.01 for the three-month period ended February 28, 2007 compared to a net loss of $0.01 per share for the three-month period ended February 28, 2006.

Revenues

Revenue from equipment sales declined approximately 76% to $432,124 for the three-month period ended February 28, 2007 as compared to $1,807,625 for the same period for the prior year. The decline in equipment sales is due primarily to a 70% decline in the number of equipment shipments and a 28% decrease in average sales prices. The overall decrease in average sales prices is primarily due to the decline of equipment sales in both the domestic and international markets, from the prior fiscal period.

We believe the decline in domestic units shipped reflects weakened demand in the refractory angina market as existing capacity is more fully utilized, coupled with increased direct and indirect competition. We anticipate that demand for EECP(R) systems will remain soft unless there is greater clinical acceptance for the use of EECP(R) therapy in treating patients with angina or angina equivalent symptoms who meet the current reimbursement guidelines or an expansion of the current CMS national reimbursement policy to include some or all Class II & III heart failure patients. Patients with angina or angina equivalent symptoms eligible for reimbursement under current policies include many with serious comorbidities, such as heart failure, diabetes, peripheral vascular disease and/or others. Despite this, many cardiology clinicians appear to be waiting for approval of reimbursement coverage for heart failure as a primary indication before they will move forward with the treatment of ischemic heart failure patients with angina equivalent symptoms. Reluctance to bill for ischemic heart failure patients under the current coverage guidelines, and failure to get or maintain adequate reimbursement coverage for angina and heart failure would adversely affect our business prospects. We anticipate that a

prevailing trend of declining prices will continue in the immediate future as our competition attempts to capture greater market share through pricing discounts. The average price of new systems sales declined slightly, in the third quarter of fiscal 2007, compared to the same period in the prior year, but was offset by an 81% decline in the average sales price of used systems. There was a higher mix of used units sold domestically during the three-month period ended February 28, 2007 for which there are higher average sales prices than those sold internationally. During the three-month period ended February 28, 2006 used system sales consisted of mostly used units sold internationally, which generate lower average sales prices. Lastly, we continue to reorganize certain territory responsibilities in our sales department due to vacant and/or unproductive territories. Our revenue from the sale of EECP(R) systems to international distributors in the third quarter of fiscal 2007 decreased approximately 56% to $137,333 compared to $310,199 in same period of the prior year reflecting decreased sales volume.

The above decline in revenue was also a result of an 8% decrease in revenue from equipment rental and services for the three-month period ended February 28, 2007, from the same three-month period in the prior year. Revenue from equipment rental and services represented 69% of total revenue in the third quarter of fiscal 2007 compared to 36% in the third quarter of fiscal 2006. The decrease in the absolute amounts and the decrease in the percentage of total revenue resulted primarily from a 7% decline in service related revenue, and a 66% decline in rental revenue. The decline was due to a decrease in the rental install base from the prior period ended February 28, 2006.

Gross Profit

Gross profit declined to $780,646 or 57% of revenues for the three-month period ended February 28, 2007, compared to $1,613,802 or 57% of revenues for the three-month period ended February 28, 2006. Gross profit margin as a percentage of revenue for the three-month period ended February 28, 2007, decreased compared to the same period of the prior fiscal year mainly due to the higher fixed production unit costs associated with reduced production due to decreasing sales in the last three fiscal quarters. In addition, the adoption of SFAS No. 151 lowered the amount of fixed overhead costs absorbed into inventory in the third quarter of fiscal 2007. The decline in gross profit when compared to the prior year in absolute dollars is principally due to the lower sales volume.

Gross profits are dependent on a number of factors, particularly the mix of EECP(R) models sold domestically and internationally and their respective average selling prices, the mix of EECP(R) units sold, rented or placed during the period, the ongoing costs of servicing such units, and certain fixed period costs, including facilities, payroll and insurance. Gross profit margins are generally less on non-domestic business due to the use of distributors resulting in lower selling prices. Consequently, the gross profit realized during the current period may not be indicative of future margins.

Selling, General and Administrative

Selling, general and administrative ("SG&A") expenses for the three-months ended February 28, 2007 and 2006, were $1,024,688 or 74% of revenues and $1,852,173 or 65% of revenues, respectively reflecting a decrease of $827,485 or

approximately 45%. The decrease in SG&A expenditures in the third quarter of fiscal 2007 compared to fiscal 2006 resulted primarily from decreased sales and marketing expenditures reflecting lower sales and marketing personnel and travel, plus reduced market research and advertising costs.

Research and Development

Research and development ("R&D") expenses of $253,346 or 18% of revenues for the three months ended February 28, 2007, decreased by $159,651 or 39%, from $412,997 or 15% of revenues for the three months ended February 28, 2006. The decrease is primarily attributable to lower new product development spending and reduced spending on clinical trials.

Provision for Doubtful Accounts

During the three-month periods ended February 28, 2007 and 2006, the Company recorded a provision for doubtful accounts of $2,661 and $0, respectively. The minimal change in the provision is a direct result of the third quarter of fiscal 2007 decrease in accounts receivable and sales.

Interest Expense and Financing Costs

Interest expense and financing costs decreased to $16,952 in the three-month period ended February 28, 2007, from $19,346 for the same period in the prior year. Interest expense primarily reflects interest on loans secured to refinance the November 2000 purchase of the Company's headquarters and warehouse facility.

Interest and Other Income, Net

Interest and other income for the three months ended February 28, 2007 and 2006, were $12,445 and $18,251 respectively. Interest income primarily reflects interest earned on the Company's cash balances. As cash balances decline, the direct impact is a decrease in interest income.

Income Tax Expense, Net

During the three-months ended February 28, 2007 and 2006, we recorded a provision for state income taxes of $5,700 and $0, respectively.

As of February 28, 2007, the recorded deferred tax assets were $20,038,976, reflecting an increase of $173,487 during the three months ended February 28, 2007, which was offset by the valuation allowance of the same amount.

Ultimate realization of any or all of the deferred tax assets is not assured, due to significant uncertainties and material assumptions associated with estimates of future taxable income during the carryforward period. In February 2006, we concluded that, based upon the weight of available evidence, it was "more likely than not" that the net deferred tax asset would not be realized and increased the valuation allowance to bring the net deferred tax asset carrying value to zero.

Nine Months Ended February 28, 2007 and 2006

Net revenue from sales, leases and service of our EECP(R) systems for the nine-month periods ended February 28, 2007 and 2006, was $4,986,580 and $9,058,376, respectively, which represented a decline of $4,071,796 or 45%. We reported a net loss of $1,418,648 compared to $10,196,944 for the nine-month periods ended February 28, 2007 and 2006, respectively. We reported a net loss attributable to common stockholders of $1,418,648 and $11,074,814 for the third quarter of fiscal 2007 and 2006, respectively. Our net loss per common share was $0.02 for the nine-month period ended February 28, 2007 compared to a net loss of $0.18 per share for the nine-month period ended February 28, 2006. The decrease in the net loss per share is due primarily to a $7,112,826 income tax valuation reserve established in November 2005 for the remaining value of the deferred tax asset.

Revenues

Revenue from equipment sales declined approximately 65% to $2,080,272 for the nine-month period ended February 28, 2007 as compared to $5,998,943 for the same period for the prior year. The decline in equipment sales is due primarily to a 57% decline in the number of equipment shipments, and a 25% decrease in average sales prices. A higher mix of used equipment sold versus both newer model equipment and new equipment was partially the cause of the decrease in average sales prices, as well as the overall decline in equipment sales in the domestic market.

We believe the decline in domestic units shipped reflects weakened demand in the refractory angina market as existing capacity is more fully utilized, coupled with increased direct and indirect competition. We anticipate that demand for EECP(R) systems will remain soft unless there is greater clinical acceptance for the use of EECP(R) therapy in treating patients with angina or angina equivalent symptoms who meet the current reimbursement guidelines or an expansion of the current CMS national reimbursement policy to include some or all Class II & III heart failure patients. Patients with angina or angina equivalent symptoms eligible for reimbursement under current policies include many with serious comorbidities, such as heart failure, diabetes, peripheral vascular disease and/or others. Despite this, many cardiology clinicians appear to be waiting for approval of reimbursement coverage for heart failure as a primary indication before they will move forward with the treatment of ischemic heart failure patients with angina equivalent symptoms. Reluctance to bill for ischemic heart failure patients under the current coverage guidelines, failure to get or maintain adequate reimbursement coverage for angina and heart failure would adversely affect our business prospects. We anticipate that a prevailing trend of declining prices will continue in the immediate future as our competition attempts to capture greater market share through pricing discounts. The average price of new systems sales decreased slightly, in the first three quarters of fiscal 2007 compared to the same period in the prior year but was offset by an 39% decline in the average sales price of used systems. There was a higher mix of used units sold domestically for the nine-month period ended February 28, 2007 for which there are higher average sales prices than for those sold internationally. During the nine-month period ended February 28, 2006 used system sales consisted of mostly used units sold internationally, which generate lower average sales prices. Lastly, we continue to reorganize certain territory responsibilities in our sales department due to vacant and/or unproductive territories. Our revenue from the sale of EECP(R) systems to international distributors during the first nine months ended February 28, 2007 increased approximately 12% to $829,288 compared $741,915 in same period of the prior year reflecting increased sales volume.

The above decline in revenue was also partially due to a 5% decrease in revenue from equipment rental and services for the nine-month period ended February 28, 2007, from the same nine-month period in the prior year. Revenue

from equipment rental and services represented 58% of total revenue for the

first nine months ended February 28, 2007 compared to 34% for the same period the prior year. The decrease in the absolute amounts and the increase in the percentage of total revenue resulted primarily from a less than a 2% change in service related revenue, and a 69% decline in rental revenue. The decline was due to a decrease in the rental installed base from the prior period ended February 28, 2006.

Gross Profit

Gross profit declined to $2,704,507 or 54% of revenues for the nine-month period ended February 28, 2007, compared to $5,309,344 or 59% of revenues for the nine-month period ended February 28, 2006. Gross profit margin as a percentage of revenue for the nine-month period ended February 28, 2007, decreased compared to the same period of the prior fiscal year mainly due to the higher fixed production unit costs associated with reduced production, due to decreased sales in the last three fiscal quarters. In addition, the adoption of SFAS No. 151 lowered the amount of fixed overhead costs absorbed into inventory for the nine months ended February 28, 2007. The decline in gross profit when compared to the prior year in absolute dollars is a direct result of the lower sales volume.

Gross profits are dependent on a number of factors, particularly the mix of EECP(R) models sold domestically and internationally and their respective average selling prices, the mix of EECP(R) units sold, rented or placed during the period, the ongoing costs of servicing such units, and certain fixed period costs, including facilities, payroll and insurance. Gross profit margins are generally less on non-domestic business due to the use of distributors resulting in lower selling prices. Consequently, the gross profit realized during the current period may not be indicative of future margins.

Selling, General and Administrative

Selling, general and administrative ("SG&A") expenses for the nine-months ended February 28, 2007 and 2006 were $3,381,852 or 68% of revenues and $6,769,946 or 75% of revenues, respectively reflecting a decrease of $3,388,094 or approximately 50%. The decrease in SG&A expenditures in the first three quarters of fiscal 2007 compared to fiscal 2006 resulted primarily from decreased sales and marketing expenditures reflecting fewer sales and marketing personnel and reduced travel, plus lower market research, and advertising costs.

Research and Development

Research and development ("R&D") expenses of $722,631 or 14% of revenues for the nine months ended February 28, 2007, decreased by $806,068 or 53%, from the nine months ended February 28, 2006, of $1,528,699 or 17% of revenues. The decrease is primarily attributable to lower new product development spending and reduced spending on clinical trials.

Provision for Doubtful Accounts

During the nine-month period ended February 28, 2007, the Company reversed

$1,340 from its provision for doubtful accounts as compared to recording $89,559 during the nine-month period ended February 28, 2006. The decrease in the provision is a direct result of the first three quarters of fiscal 2007 decrease in accounts receivable and sales from the corresponding quarter ended February 28, 2006.

Interest Expense and Financing Costs

Interest expense and financing costs decreased to $54,281 in the nine-month period ended February 28, 2007, from $64,299 for the same period in the prior year. Interest expense primarily reflects interest on loans secured to refinance the November 2000 purchase of the Company's headquarters and warehouse facility.

Interest and Other Income, Net

Interest and other income for the first three quarters of fiscal 2007 and fiscal 2006, were $48,269 and $59,041, respectively. Interest income primarily reflects interest earned on the Company's cash balances. As cash balances decline, the direct impact is a decrease in interest income.

Income Tax Expense, Net

During the nine-months ended February 28, 2007 and 2006, we recorded a provision for state income taxes of $14,000 and $7,112,826, respectively. The fiscal 2006 tax expense consists mainly of $7,093,000 in additional valuation allowance provided for the deferred tax asset in the second fiscal quarter of 2006. The income tax expense for the first nine months of fiscal 2006 does not include $7,489,000 added to the deferred tax valuation allowance for tax benefits associated with prior years' exercises of stock options and warrants, which was charged directly to additional paid-in capital.

As of February 28, 2007, the recorded deferred tax assets were $20,038,976, reflecting an increase of $479,518 during the nine months ended February 28, 2007, which was offset by the valuation allowance of the same amount.

Ultimate realization of any or all of the deferred tax assets is not assured, due to significant uncertainties and material assumptions associated with estimates of future taxable income during the carryforward period. In February 2006, we concluded that, based upon the weight of available evidence, it was "more likely than not" that the net deferred tax asset would not be realized and increased the valuation allowance to bring the net deferred tax asset carrying value to zero.

Liquidity and Capital Resources

We have financed our operations in fiscal 2007 and fiscal 2006 from working capital mainly provided by the issuance of preferred stock. At February 28, 2007, we had cash, and cash equivalents of $1,041,890 and working capital of $1,433,547 as compared to cash, cash equivalents, and certificates of deposit totaling $2,385,778 and working capital of $2,867,288 at May 31, 2006. Our cash, cash equivalents, and certificates of deposit balances decreased $1,343,888 in fiscal year 2007 primarily due to cash used in operating activities of $1,107,494 and cash used in financing activities of $236,394.

The decrease in cash used in operating activities during the first three quarters of fiscal year 2007 resulted primarily from the net loss of $1,418,648 plus adjustments to reconcile net loss to net cash used in operating activities of $311,154. Changes in our operating assets and liabilities were $71,976. The changes in the asset components primarily reflect a decrease in accounts receivable of $280,959, lower inventory of $495,036 and other current assets of $129,865. The changes in our operating liability components reflect a decrease in accounts payable and accrued liabilities of $604,806 and a decrease in other liabilities of $228,005. Non-cash adjustments amounted to $239,178, which partially offset the above. Net accounts receivable were 11% of revenues for the nine-month period ended February 28, 2007, compared to 28% at the end of the nine-month period ended February 28, 2006, and accounts receivable turnover was 6.4 times as of February 28, 2007, and was 6.2 times as of February 28, 2006.

Standard payment terms on our domestic equipment sales are generally net 30 to 90 days from shipment and do not contain "right of return" provisions. We have historically offered a variety of extended payment terms, including sales-type leases, in certain situations and to certain customers in order to expand the market for our EECP(R) products in the US and internationally. Such extended payment terms were offered in lieu of price concessions, in competitive situations, when opening new markets or geographies and for repeat customers. Extended payment terms cover a variety of negotiated terms, including payment in full - net 120, net 180 days or some fixed or variable monthly payment amount for a six to twelve month period followed by a balloon payment, if applicable. During the first three quarters of fiscal 2007 and 2006, less than 1% of revenues were generated from sales in which initial payment terms were greater than 90 days and we offered no sales-type leases during either period. In general, reserves are calculated on a formula basis considering factors such as the aging of the receivables, time past due, and the customer's credit history and their current financial status. In most instances where reserves are required, or accounts are ultimately written-off, customers have been unable to successfully implement their EECP(R) program. As we are creating a new market for the EECP(R) therapy and recognizing the challenges that some customers may encounter, we have opted, at times, on a customer-by-customer basis, to recover

our equipment instead of pursuing other legal remedies, which has resulted in our recording of a reserve or a write-off.

There were no investing activities during the nine-month period ended February 28, 2007.

Our financing activities used cash of $236,394 during the nine-month period ended February 28, 2007, reflecting payments on our outstanding notes and loans.

We have incurred large declines in revenue and sustained significant operating losses during the last four fiscal years and our ability to continue operating as a going concern is dependent upon achieving profitability, a strategic alliance within the sales and marketing areas, or through additional debt or equity financing. Achieving profitability is largely dependent on sufficiently reducing operating costs and halting the current trend of declining revenue. Our ability to halt the declines in revenue and restore our revenue base is largely dependent upon increasing the demand in the refractory angina

market and operating in a more efficient manner. To date, we have not been able to restore our revenue base and reduce operating costs significantly enough to generate an adequate cash inflow, nor raise additional capital, so we may not be able to continue as a going concern.

We believe that our projected cash flow from operations together with our current cash reserves and working capital will be sufficient to fund our business plan and projected capital requirements through May 2007, assuming our current revenue rate.

The following table presents the Company's expected cash requirements for contractual obligations outstanding as of February 28, 2007.

	Total	Due as of 2/29/08	Due as of 2/28/09 and 2/28/10	Due as of 2/28/11 and 2/29/12
Long-Term Debt				
Notes Payable	$866,753	$64,631	$144,524	$165,656
Employment Agreements	340,167	260,000	80,167	--
Total Contractual Cash Obligations	$1,206,920	$324,631	$224,691	$165,656

Effects of Inflation

We believe that inflation and changing prices over the past three years have not had a significant impact on our revenue or on our results of operations.

ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to certain financial market risks, including changes in interest rates. All of our revenue, expenses and capital spending are transacted in US dollars. Our exposure to market risk for changes in interest rates relates primarily to our cash and cash equivalent balances. The majority of our investments are in short-term instruments and subject to fluctuations in US interest rates. Due to the nature of our short-term investments, we believe that there is no material risk exposure.

ITEM 4 - CONTROLS AND PROCEDURES

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of February 28, 2007, our disclosure controls and procedures are effective to provide reasonable assurances that such disclosure controls and procedures satisfy their objectives and that the information required to be disclosed by us in the reports we file under the Exchange Act is recorded, processed, summarized and reported within the required time periods. There were

no changes during the fiscal quarter ended February 28, 2007 in our internal controls or in other factors that could have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 6 - EXHIBITS

Exhibits

31 Certifications pursuant to Rules 13a-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32 Certifications pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

In accordance with the requirements of the Exchange Act, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

VASOMEDICAL, INC.

By: /s/ Thomas Glover

Thomas Glover
Chief Executive Officer and Director
(Principal Executive Officer)

/s/ Tricia Efstathiou

Tricia Efstathiou
Chief Financial Officer
(Principal Financial and Accounting Officer)

Date: April 16, 2007