COMPUMED INC
Form 10QSB
February 11, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-QSB

(MARK ONE)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED DECEMBER 31, 2004

[ ] 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 0-14210

COMPUMED, INC.
(exact name of small business issuer as specified in its charter)

DELAWARE	95-2860434
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

5777 WEST CENTURY BLVD., SUITE 1285, LOS ANGELES, CA 90045
(Address of principal executive offices)

(310) 258-5000
(issuer's telephone number)

Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 in for the past 90 days. Yes X No

As of January 31, 2005, we had 20,287,226 shares of Common Stock outstanding.

Transitional Small Business Disclosure Format (check one): Yes No X

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PART I FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS

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COMPUMED, INC. AND SUBSIDIARIES

FINANCIAL INFORMATION
BALANCE SHEETS
COMPUMED, INC.

	December 31, 2004 (UNAUDITED)
ASSETS	
CURRENT ASSETS	
Cash and cash equivalents	$ 105,000
Marketable securities, at fair market value	167,000
Accounts receivable, less allowance of $25,000 (December 2004) and $21,000 (September 2004).	296,000
Inventory.	35,000
Prepaid expenses and other current assets.	31,000
TOTAL CURRENT ASSETS	634,000
PROPERTY AND EQUIPMENT	
Machinery and equipment.	1,231,000
Furniture, fixtures and leasehold improvements	78,000

Equipment under capital leases	50,000
	1,359,000
Accumulated depreciation and amortization.	(1,230,000)
TOTAL PROPERTY AND EQUIPMENT	129,000
OTHER ASSETS	
Patents, net of accumulated amortization of $4,000 (December 2004) and $4,000 (September 2004).	70,000
Other assets	13,000
TOTAL OTHER ASSETS.	83,000
TOTAL ASSETS	$846,000
LIABILITIES AND STOCKHOLDERS' EQUITY CURRENT LIABILITIES	
Accounts payable	$ 184,000
Accrued liabilities.	113,000
Current portion of capital lease obligations	8,000
TOTAL CURRENT LIABILITIES.	305,000
Capital lease obligations, less current portion	37,000
STOCKHOLDERS' EQUITY	
Preferred Stock, $.10 par value - authorized 1,000,000 shares	
Preferred Stock- Class A $3.50 cumulative convertible voting - issued and outstanding - 8,400 shares.	1,000
Preferred Stock- Class B $3.50 cumulative convertible voting - issued and outstanding - 300 shares.	-
Common Stock, $.01 par value-authorized 50,000,000 shares, issued and outstanding - 20,247,238 shares (December 2004) issued and outstanding - 19,599,812 shares (September 2004)	203,000
Additional paid in capital	32,603,000
Accumulated deficit.	(32,346,000)
Accumulated other comprehensive income	51,000
Deferred stock compensation.	(8,000)
TOTAL STOCKHOLDERS' EQUITY	504,000
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$846,000

See notes to condensed financial statements.

STATEMENT OF OPERATIONS (UNAUDITED)
COMPUMED, INC.

	Three Months Ending Dec	
	2004	
REVENUES		
ECG services.	399,000	38
ECG product and supplies sales.	270,000	1
OsteoGram (R) sales and services.	8,000	5
TOTAL REVENUES.	677,000	46
COSTS AND EXPENSES		
Cost of ECG services.	138,000	11
Cost of goods sold-ECG.	221,000	1
Cost of goods sold-OsteoGram (R).	1,000	
Selling expenses.	68,000	4
Research & development.	62,000	5
General & administrative expenses	274,000	24
Depreciation & amortization	18,000	5
TOTAL EXPENSES.	782,000	52
OPERATING LOSS.	(105,000)	(6
Interest income and dividends	6,000	
Other miscellaneous income.	8,000	
Realized gains on marketable securities	-	
Interest expense.	(2,000)	
NET LOSS.	(93,000)	(6
NET LOSS PER SHARE (BASIC AND DILUTED).	(0.00)	
Weighted average number of common shares outstanding.	19,691,544	17,95

STATEMENT OF CASH FLOWS (UNAUDITED)
COMPUMED, INC.

	Thre
OPERATING ACTIVITIES:	
Net loss	
Net adjustments to reconcile net loss to net cash used in operating activities:	
Realized gain/loss on marketable securities.	
Amortization of deferred stock compensation.	
Depreciation and amortization.	
Decrease in accounts receivable.	
Decrease (Increase) in inventory and prepaid expenses.	
Decrease (Increase) in accounts payable and other liabilities.	
NET CASH USED IN OPERATING ACTIVITIES.	

CASH FLOW FROM INVESTING ACTIVITIES:
Proceeds from selling of marketable securities . . . .
Investments in purchase of marketable securities. . . . .
Purchase of other asset. . . . .
Purchase of property, plant and equipment. . . . .

NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES. . . . .

CASH FLOW FROM FINANCING ACTIVITIES:
Proceeds from exercise of stock option . . . .
Net offering of the investment agreement with Dutchess Private Equities Fund . .
Payments on capital lease obligations. . . . .

NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES. . . . .

NET [INCREASE] DECREASE IN CASH. . . . .

CASH BEGINNING OF PERIOD . . . .

CASH AT END OF PERIOD. . . . .

SUPPLEMENTAL DISCLOSURES:
Interest paid. . . . .
Disposal of fixed assets . . . .

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)
COMPUMED, INC.

NOTE A-BASIS OF PRESENTATION AND ACCOUNTING POLICIES

The accompanying interim unaudited condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month period ended December 31, 2004 are not necessarily indicative of the results that may be expected for the year ending September 30, 2005. For further information, refer to the financial statements for the year ended September 30, 2004 and the notes thereto included in the Company's Annual Report on Form 10-KSB.

The balance sheet at September 30, 2004 has been derived from the Company's year-end audited financial statements but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

The Company has historically used existing cash and readily available marketable securities balances to fund operating losses and capital expenditures. The Company raised these funds in 1997 through 2000 through the sale of Preferred Stock issuances and proceeds from the exercise of certain stock options and warrants.

The Company has incurred recurring losses and had net losses aggregating $154,000 for the three months ended December 31, 2004 and 2003.

STOCK-BASED COMPENSATION

The Company accounts for employee stock option grants in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees and related interpretations (APB 25), and has adopted the "disclosure only" alternative described in Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, amended by SFAS No. 148 Accounting for Stock-Based Compensation-Transition and Disclosure.

SFAS No. 123, Accounting for Stock-Based Compensation, requires pro forma information regarding net income (loss) using compensation that would have been incurred if the Company had accounted for its employee stock options under the fair value method of that statement.

In fiscal 2005, during the three months ended December 31, 2004, the Company granted 35,000 shares to a consultant and 235,000 shares to employees. 35,000 shares were valued at $8,000 of which $200 was expensed in this quarter and 235,000 shares were valued at $54,000 and recorded at $0 using the intrinsic method.

In fiscal 2004, during the three months ended December 31, 2003, the Company granted 26,087 shares to a consultant and 235,000 shares to employees. 26,087 shares were valued at $8,000 of which $8,000 was expensed in fiscal 2004 and 235,000 shares were valued at $59,000 and recorded at $0 using the intrinsic method.

The options were valued in accordance with SFAS 123 and the fair values were estimated using Black-Scholes option pricing method with the following assumptions:

	For The Three Months Ended December 31, 2004	December 31, 2003
Risk free interest rate	4.23%	4.05%
Stock volatility factor	33%	55% to 65%
Weighted average expected option life . .	10 years	10 years
Expected dividend yield	None	None

The pro forma net loss and loss per share had the Company accounted for the options using FAS 123 would have been as follows:

	Three Months Ended December 31, 2004	2003
Net loss as reported	(93,000)	(61,000)
Basic and diluted loss per share as reported .	(0.00)	(0.00)
Add: stock-based employee compensation cost included in determination of net loss reported	--	8,000
Deduct: stock-based employee compensation cost that would have been included in the determination of net loss if the fair value based method had been applied to all awards. .	(16,000)	(8,000)

Pro forma net loss if the fair value based method had been applied to all awards.	(109,000)	(61,000)
Basic and diluted pro forma loss per share if the fair value based method had been applied to all awards.	(0.01)	(0.00)

A summary of the stock options activity, and related information for the nine months ended December 31 follows:

	2004		
	Shares	Weighted Average Exercise Price	Shares
Options outstanding, beginning of period	6,437,217	0.22	5,027,025
Options exercised	(525,869)	0.09	-
Options granted	270,000	0.32	261,087
Options forfeited/canceled	(10,879)	0.71	(1,104)
Options outstanding, end of period	6,170,469	0.24	5,287,008
Options exercisable, end of period	4,093,809	0.25	4,495,347

The following summarizes information concerning stock options outstanding at December 31, 2004:

Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
$0.0000 - $0.4250	5,306,234	8.5	0.17
$0.4251 - $0.8500.	832,985	4.5	0.67
$0.8501 - $1.2750.	31,250	2.9	1.15
	6,170,469	7.9	0.24

PER SHARE DATA

The Company reports its earnings (loss) per share in accordance with Statement of Financial Accounting Standards No.128, "Accounting for Earnings Per Share" ("FAS 128"). Basic loss per share is calculated using the net loss divided by the weighted average common shares outstanding. Shares from the assumed conversion of outstanding warrants, options and the effect of the conversion of the Class A Preferred Stock and Class B Preferred Stock are omitted from the computations of diluted loss per share because the effect would be antidilutive.

NOTE B-OTHER AGREEMENTS

On December 23, 2003, the Company entered into an Investment Agreement with Dutchess Private Equities Fund. That agreement provides that, following notice to Dutchess, the Company may sell to Dutchess up to $5 million in shares of our Common Stock for a purchase price equal to 95% of the average of the three lowest closing bid prices on the Over-the-Counter Bulletin Board of our Common Stock during the five day period following that notice. The number of shares that are permitted to sell pursuant to the Investment Agreement is either: (A) two hundred percent of the average daily volume of our Common Stock for the ten trading days prior to the applicable sale notice, multiplied by the average of the three daily closing best bid prices immediately preceding the day we issue the notice, or (B) $25,000; provided that in no event will the sale be more than $1,000,000 with respect to any single sale.

Dutchess' obligation to purchase the Company's Common Stock is contingent upon certain closing conditions. Such conditions relate to the Investment Agreement and include: (i) that our representations and warranties are true and correct as of the funding date, (ii) that we have performed all of our covenants, agreements and conditions required to be performed by us, (iii) that trading of our Common Stock has not been suspended, (iv) that no statute, rule, regulation, executive order, decree, ruling or injunction is in force against the transactions contemplated in the Investment Agreement, (v) that no pending or threatened litigation exists, and (vi) that the SEC has declared effective a registration statement covering the shares to be purchased by Dutchess.

The Company entered into an agreement with CEOcast, Inc. (the "Consultant") an investor relations company from June 15, 2004 to December 15, 2004. During the term of this Agreement, the Company paid the Consultant $45,000 and issued 250,000 shares of Common Stock.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

SAFE HARBOR FOR FORWARD-LOOKING STATEMENTS

This Report on Form 10-QSB contains forward-looking statements, including, without limitation, statements concerning our possible or assumed future results of operations. These statements are preceded by, followed by or include the words "believes," "could," "expects," "intends" "anticipates," or similar expressions. Our actual results could differ materially from those anticipated in the forward-looking statements for many reasons including, but not limited to, product and service demand and acceptance, changes in technology, ability to raise capital, the availability of appropriate acquisition candidates and/or business partnerships, economic conditions, the impact of competition and pricing, capacity and supply constraints or difficulties, government regulation and other risks described in this report. Although we believe the expectations reflected in the forward-looking statements are reasonable, they relate only to events as of the date on which the statements are made, and our future results, levels of activity, performance or achievements may not meet these expectations. We do not intend to update any of the forward-looking statements after the date of this document to conform these statements to actual results or to changes in our expectations, except as required by law.

OVERVIEW

Our core business is providing remote electrocardiogram (ECG) interpretation services to medical facilities that may not have access either to trained physicians that can interpret ECG results or to self-interpreting ECG equipment. Our customers are typically correctional facilities, ambulatory surgery centers, occupational health clinics and physician offices. Although self-interpreting ECG equipment is widely available, many of our customers like the optional feature of automatically sending their ECG results to one of our cardiologists for an overread when the results are abnormal. This overread feature is a key advantage that enables us to market our services in segments of the market where physicians may not be available on a routine basis. We are evaluating new opportunities for our ECG business; however, we could lose customers who choose to receive services from a competitor or who purchase a self-interpretive machine and no longer need our ECG interpretations. If we were to lose existing customers, they may be difficult to replace, and that could have a material adverse impact on our operations and financial condition.

Our other business is the development and marketing of medical imaging software tools that automatically make accurate and precise measurements to diagnose bone disease. Our target markets for these products are hospitals, imaging centers and orthopedic office practices. Our initial product, the OsteoGram(R), is an automated system for the rapid screening, diagnosis and monitoring of osteoporosis, a disease that effects more than 200 million people worldwide.

Osteoporosis is a "silent disease" that costs the U.S. healthcare system over $16 billion annually. Medicare is currently scrutinizing methods to lower the costs of fighting this largely preventable disease through point-of-care testing of "at risk" patients with fragility fractures. We believe that convenient, low-cost methods of screening and diagnosing will become increasingly desirable as hospitals comply with recent initiatives directing them to test for and treat this insidious disease.

The OsteoGram(R) was originally marketed as a film-based product that utilizes a standard hand x-ray film that is digitized on a desktop scanner. The image is then analyzed on a personal computer by means of the patented OsteoGram(R) software. This system is marketed to small hospitals, clinics and physician's offices. Last year we began marketing a DICOM, or Digital Imaging and Communications in Medicine, version of the OsteoGram software. The DICOM OsteoGram(R) was developed to take advantage of the growing market for digital (filmless) x-ray equipment. DICOM is the information standard that allows digital imaging equipment to interconnect, enabling clinicians to readily move, archive and retrieve images over networks. By residing on the workstations of these advanced digital systems, the OsteoGram(R) software can automatically capture and analyze images directly from either the x-ray equipment or the network. We license our DICOM OsteoGram software to manufacturers of digital x-ray and network equipment. In addition we enlist dedicated imaging distributors to sell our products in the after sale market.

For the quarter ended December 31, 2004 we continued to focus on the implementation of our DICOM OsteoGram(R) strategy. Our development team is now experienced in the integration of OsteoGram software into digital x-ray workstations, and as a result, future integration projects will progress more rapidly. Although our initial partnerships in this market have yielded mediocre results, we continue to believe the strategy is viable and that partnerships with the market leaders will be successful. We recently signed licensing and distribution agreements with Swissray International and SourceOne Healthcare Technologies. Swissray is the global market leader in direct digital x-ray equipment, and SourceOne is the largest imaging distributor in the United States. To assist SourceOne in their efforts, we are developing the OsteoGram CADKit and CADServer products that will enable distribution partners to readily connect the OsteoGram to the growing installed base of digital x-ray equipment. In addition to these partners, Fuji Medical Systems exhibited the DICOM OsteoGram at the 90th Scientific Assembly and Annual Meeting of the Radiological Society of North America (RSNA) in Chicago (November 29-December 3). Fuji Medical is the market leader in the computed radiography (CR) arena, and we hope to expand our relationship with this firm.

During October we completed the proof of principal phase of utilizing the OsteoGram on a digital mammography platform at a major teaching center. The global market for digital mammography is rapidly expanding, and these advanced units have a more consistent peak energy level than their analog predecessors, which produces an excellent image for OsteoGram analysis. One of the public health problems in stopping osteoporosis is to test and treat more at risk women. By combining the OsteoGram with mammography equipment, women can be conveniently tested for osteoporosis at the same time and on the same equipment as their routine mammogram. We were delighted that Fuji Medical displayed the OsteoGram in conjunction with their digital mammography image reader at the recent RSNA. We are planning a clinical trial in the second quarter of 2005 to validate the use of the OsteoGram on these new digital platforms.

Our ECG business grew significantly this quarter as we shipped a one-time order of nearly 100 new ECG terminals to the New York State Department of Correctional Services. These state-of-the-art terminals are transmitting to our new Schiller SEM@Net system, which will serve our ECG customers for years to come. The Internet capability of the SEM@Net will allow us to enter the international markets, where the cost of a telephone transmission was previously prohibitive. We believe that an overread by a U.S. based cardiologist could be a value-added service in those countries where cardiologists are not readily available.

RESULTS OF OPERATIONS FOR THE QUARTER ENDED DECEMBER 31, 2004 COMPARED TO THE QUARTER ENDED DECEMBER 31, 2003.

Revenues from ECG operations increased by 66% for the first quarter of fiscal 2005 to $669,000 from $402,000 for the same period in fiscal 2003, due to increase in ECG equipment sales. Revenues from the OsteoGram(R) sales and services for the first quarter of fiscal 2005 decreased by 86% to $8,000 from $58,000 due to continued delays in obtaining a CE Mark enabling European sales and a slower than expected ramp up of licensing partnerships.

Cost of services and goods sold consists of the costs of ECG services provided, supplies, electrocardiograph equipment sold and OsteoGram(R) systems sold. Costs of services of ECG for the first quarter of fiscal 2005 increased by 16% to $138,000 from $119,000 for the same period in fiscal 2004, mostly due to increased of overread services and some overhead expenses related to the acquisition and renewal of certain contracted ECG accounts. Cost of goods sold of ECG for the first quarter of fiscal 2005 increased by 1373% to $221,000 from $15,000, primarily due to increase of ECG equipment sales. The cost of goods sold for OsteoGram(R) for the first quarter of fiscal 2005 decreased by 75% to $1,000 from $4,000 for the same period in fiscal 2004, primarily due to lower sales.

Selling expenses for the first quarter 2005 increased by 51% to $68,000 from $45,000, mostly due to increased trade shows and marketing expenses related to the OsteoGram (R) business.

General and administrative expenses for the first quarter of fiscal 2005 increased by 14% to $274,000 from $241,000 for the same period in fiscal 2004, primarily due to cash payment to our Directors that previously were accepting stock options in lieu of cash (see Stock-Based Compensation) and increased costs of investor relations.

Research and development costs for the first quarter of fiscal 2005 increased by 17% to $62,000 from $53,000 in fiscal 2004 due to contracted services and salary adjustments.

Depreciation expenses for the first quarter of fiscal 2005 decreased by 65% to $18,000 from $51,000 compared to fiscal 2004 due to a large portion of fixed assets that was fully amortized.

Interest income and dividends for the first quarter of fiscal 2005 increased by 20% to $6,000 from $5,000 due to increase of investments in marketable securities.

Other miscellaneous income was $8,000 for the first quarter of fiscal 2005 and none for the same period in fiscal 2004, mostly due to the reversal of a reserve related to a disputed charge from a utility company.

Net loss for the first quarter of fiscal 2005 increased by 52% to $93,000 from $61,000, primarily due to lower than expected sales of highly profitable OsteoGram (R) products.

FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2004, we had approximately $272,000 in cash and marketable securities, as compared to a balance of $227,000 at September 30, 2004, a net increase of $45,000 primarily due to increased sales in ECG. Purchases of property, plant and equipment used $3,000 in the first quarter ended December 31, 2004.

We have historically used existing cash and readily available marketable securities balances to fund operating losses and capital expenditures. We also raise funds through the sale of Common and Preferred stock issuances and proceeds from the exercise of stock options and warrants.

CAPITAL COMMITMENTS

We entered into an agreement with CEOcast, Inc,.an investor relations company, from June 15, 2004 to December 15, 2004. During the term of this Agreement, we paid CEOcast $45,000 and issued 250,000 shares of Common Stock.

We lease our corporate offices at a monthly rental of $11,478 per month with 3% annual increase.

We entered into a long-term agreement with John McLaughlin effective November 2, 2002 through September 30, 2004. This agreement provides a base salary of $150,000 per year and a bonus up to $150,000 based on performance factors including revenue, profit and the accomplishment of certain key milestones. In addition, Mr. McLaughlin received standard employee options to purchase 50,000 shares of Common Stock at an exercise price of $0.20 per share upon acceptance of the agreement.

Each of our Directors receives an annual Board of Directors fee of $10,000, which is paid to each Director in equal monthly installments. The Chairman receives an additional $4,500. In addition to the Board of Directors fee, Directors receive an additional $750 per meeting when they serve as a member of the Executive, Audit or Compensation Committee. Such amount is reduced to $250 if the committee meeting is held by teleconference or on the same day as a board meeting.

FINANCING ACTIVITIES

On December 23, 2003, we entered into an Investment Agreement with Dutchess Private Equities Fund. That agreement provides that, following notice to Dutchess, we may sell to Dutchess up to $5 million in shares of our Common Stock for a purchase price equal to 95% of the average of the three lowest closing bid prices on the Over-the-Counter Bulletin Board of our Common Stock during the five day period following that notice. The number of shares that are permitted to sell pursuant to the Investment Agreement is either: (A) two hundred percent of the average daily volume of our Common Stock for the ten trading days prior to the applicable sale notice, multiplied by the average of the three daily closing best bid prices immediately preceding the day we issue the notice, or (B) $25,000; provided that in no event will the sale be more than $1,000,000 with respect to any single sale.

Dutchess' obligation to purchase our Common Stock is contingent upon certain closing conditions. Such conditions relate to the Investment Agreement and include: (i) that our representations and warranties are true and correct as of the funding date, (ii) that we have performed all of our covenants, agreements and conditions required to be performed us, (iii) that trading of our Common Stock has not been suspended, (iv) that no statute, rule, regulation, executive order, decree, ruling or injunction is in force against the transactions contemplated in the Investment Agreement, (v) that no pending or threatened litigation exists, and (vi) that the SEC has declared effective a registration statement covering the shares to be purchased by Dutchess.

During the fiscal quarter ended December 31, 2004, we sold 121,557 shares of Common Stock to Dutchess Private Equities Fund at $0.28 per share. Gross proceeds were $34,036.

PLAN OF OPERATIONS

Our business strategy includes an increase in OsteoGram(R) revenue through OEM sales to manufactures of medical digital x-ray equipment and through direct sales through domestic and international distributors. We intend to finance this business strategy by using our current working capital resources and cash flows from existing operations, including the ECG and OsteoGram(R) businesses. There can be no assurance that the ECG and OsteoGram(R) sales will be sufficient to offset related expenses. We anticipate that our cash flow from operations, available cash and marketable securities will be sufficient to meet our anticipated cash requirements for at least the next 12 months. However, in certain circumstances we may need to raise additional capital in the future, which might not be available on reasonable terms or at all. If we raise additional capital we will likely utilize our $5,000,000 available through the Investment Agreement with Dutchess Private Equities Fund. Failure to raise capital when needed could adversely impact our business, operating results and liquidity. If additional funds are raised through the issuance of equity or convertible securities, the percentage of ownership of existing stockholders will be reduced. Furthermore, some equity and convertible securities might have rights, preferences or privileges senior to our Common Stock. Our Common Stock is currently traded on the over-the-counter bulletin board, which makes it more difficult to raise funds through the issuance of equity or convertible securities because our Common Stock is thinly traded and those who wish to sell shares of our Common Stock may have difficulty locating buyers. Additional sources of financing may not be available on acceptable terms, if at all.

We intend to pursue additional research and/or sub-contractor agreements relating to our development projects. Additionally, we may seek partners and acquisition candidates of businesses that are complementary to our own. Such investments would be subject to our obtaining financing through issuance of debt or other securities. Acquisition could be dilutive to stockholders.

MATERIAL TRENDS AND UNCERTAININITIES

We are disappointed by the rate of progress in commercializing the Digital Communications and Imaging in Medicine (DICOM) OsteoGram, and we expect that our distribution partners will accelerate their efforts to incorporate our product into their sales training schedules in early fiscal 2005. The Chinese market continues to be a disappointment, mainly due to delays in a government sponsored program to bring osteoporosis testing to rural areas. We experienced a slowing of sales for our older, film-based unit; however, we laid the groundwork for the introduction of our DICOM version of the OsteoGram(R) by expanding distribution to include Siemens AG, Orex's local partner.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition and results of operations, including the discussion on liquidity and capital resources, are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we re-evaluate our estimates and judgments, particularly those related to the determination of the estimated recoverable amounts of trade accounts receivable, impairment of long-lived assets, revenue recognition and deferred tax assets. We believe the following critical accounting policies require our more significant judgment and estimates used in the preparation of the financial statements.

We maintain an allowance for doubtful accounts for estimated losses that may arise if any of our customers are unable to make required payments. Management specifically analyzes the age of customer balances, historical bad debt experience, customer credit-worthiness, and changes in customer payment terms when making estimates of the uncollectability of our trade accounts receivable balances. If we determine that the financial conditions of any of our customers deteriorated, whether due to customer specific or general economic issues, increases in the allowance may be made. Accounts receivable are written off when all collection attempts have failed.

We have a significant amount of property, equipment and intangible assets, including patents. In accordance with Statement of Financial Accounting Standards (SFAS) No. 144, Accounting for the Impairment or Disposal of Long Lived Assets, we review our long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability of long-lived and amortizable intangible assets to be held and used is measured by a comparison of the carrying amount of an asset to the undiscounted future operating cash flows expected to be generated by the asset. If these assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying value of the assets exceeds their fair value.

We follow the provisions of Staff Accounting Bulletin 101, "Revenue Recognition in Financial Statements" (SAB 101), for revenue recognition. Under SAB 101, four conditions must be met before revenue can be recognized: (i) there is persuasive evidence that an arrangement exists, (ii) delivery has occurred or service has been rendered, (iii) the price is fixed or determinable and (iv) collection is reasonably assured. In December 2003, the SEC issued Staff Accounting Bulletin (SAB) No. 104, "Revenue Recognition" (SAB No. 104), which revises and rescinds certain sections of SAB No. 101, "Revenue Recognition", in order to make this interpretive guidance consistent with current authoritative accounting and auditing guidance and SEC rules and regulations. The changes noted in SAB No. 104 did not have a material effect on our results of operations, financial position or cash flows.

ITEM 3. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

Based on management's evaluation (with the participation of our principal executive officer and principal financial officer), as of the end of the period covered by this report, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, (the "Exchange Act")) are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and regulations.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There was no change in our internal control over financial reporting during our first quarter of fiscal 2004 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

LIMITATION ON THE EFFECTIVENESS OF CONTROLS

Our management, including our chief executive officer and principal financial officer, does not expect that our disclosure controls and internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control.

The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

PART II OTHER INFORMATION

ITEM 1 LEGAL PROCEEDINGS

None.

ITEM 2 UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

During the fiscal quarter ended December 31, 2004, we issued an aggregate of 647,426 shares of Common Stock, of which 505,869 shares were exercise of stock options by directors, 20,000 shares by a consultant and 121,557 shares sold to Dutchess Private Equities Fund at $0.28.

All sales were made pursuant to Section 4(2) of the Securities Act of 1933, as amended, and Rule 506 of Regulation D promulgated hereunder. All proceeds received were added to the Company's working capital.

ITEM 3 DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None

ITEM 5 OTHER INFORMATION

None

ITEM 6. EXHIBITS

NUMBER	DESCRIPTION OF EXHIBIT

3.1 Certificate of Incorporation (filed as Exhibit 3.1 to the Registrant's Registration Statement of Form S-1 effective May 7, 1992 and incorporated herein by reference).

3.2 Certificate of Amendment of Certificate of Incorporation (filed as Exhibit 3.1a to the Registrant's Registration Statement on Form S-2/A filed on June 28, 1994 and incorporated herein by reference).

3.3 Certificate of Amendment of Certificate of Incorporation (filed as Exhibit 3.1b to the Registrant's Registration Statement on Form S-2/A filed on November 7, 1994 and incorporated herein by reference).

3.4 Certificate of Correction of Certificate of Amendment (filed as Exhibit 3.1c the Registrant's Registration Statement on Form S-2/A filed on November 7, 1995 and incorporated herein by reference).

3.5 By-Laws (filed as Exhibit 3.5 to the Registrant's Quarterly Report on Form 10-QSB filed on February 13, 2004 and incorporated herein by reference).

3.6 Amendment to By-laws (filed as Exhibit 3.6 to the Registrant's Quarterly Report on Form 10-QSB filed on February 13, 2004 and incorporated herein by reference).

4.1 Certificate of Designation of Class A Preferred Stock (filed as Exhibit 4.5 to the Registrant's Annual Report on Form 10-KSB filed on December 29, 1995 and incorporated herein by reference).

4.2 Certificate of Designation of Class B Preferred Stock (filed as Exhibit 4.6 to the Registrant's Annual Report on Form 10-KSB filed on December 29, 1995 and incorporated herein by reference).

4.3 Certificate of Designation of Class C Preferred Stock (filed as Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on January 9, 1998 and incorporated herein by reference).

4.4 Certificate of Correction for Class C Preferred Stock (filed as Exhibit 3.2 to the Registrant's Current Report on Form 8-K filed on January 9, 1998 and incorporated herein by reference).

10.1 Form of Non-Qualified Stock Option Agreement (filed as Exhibit 10 to the Registrant's Registration Statement on Form S-8 filed on October 14, 1995 and incorporated herein by reference).

10.2 Commercial Office Lease between the Registrant and L.A.T. Investment Corporation, dated August 16, 1999 (filed as Exhibit 10.24 to the Registrant's Annual Report on Form 10-KSB filed on December 29, 1999 and incorporated herein by reference).

10.3 Form of Stock Option Agreement (filed as Exhibit 10.5 to the Registrant's Quarterly Report on Form 10-QSB filed on August 14, 2002 and incorporated herein by reference).

10.4 Employment Agreement between the Registrant and John McLaughlin dated November 2, 2002 (filed as Exhibit 10.6 to the Registrant's Quarterly Report on Form 10-QSB filed on February 14, 2003 and incorporated herein by reference).

10.5 Amendment to Employment Agreement between the Registrant and John McLaughlin (filed as Exhibit 10.5 to the Registrant's Quarterly Report on Form 10-QSB filed on December 29, 2004 and incorporated herein by reference).

10.6 2003 Stock Incentive Plan (filed as Exhibit 99.2 to the Registrant's Registration Statement on Form S-8 filed on June 2, 2003 and incorporated herein by reference).

10.7 Amendment to Commercial Office Lease between the Registrant and L.A.T. Investment Corporation (filed as Exhibit 10.6 to the Registrant's Quarterly Report on
Form 10-QSB filed on December 29, 2004 and incorporated herein by reference).

10.8 Investment Agreement between the Registrant and Dutchess Private Equities Fund, LP, dated February 25, 2004 (filed as Exhibit 10.9 to the Registrant's Registration Statement on Form SB-2 filed on February 27, 2004 and incorporated herein by reference).

10.9 Registration Rights Agreement between the Registrant and Dutchess Private Equities Fund, LP, dated February 25, 2004 (filed as Exhibit 10.10 to the Registrant's Registration Statement on Form SB-2 filed on February 27, 2004 and incorporated herein by reference).

10.10 Placement Agent Agreement between the Registrant, Charleston Securities and Dutchess Private Equities Fund, LP, dated February 25, 2004 (filed as Exhibit 10.11 to the Registrant's Registration Statement on Form SB-2 filed on February 27, 2004 and incorporated herein by reference).

31.1 Certification Pursuant to 18 U.S.C. Section 7241, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification Pursuant to 18 U.S.C. Section 7241, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

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

COMPUMED, INC.

Date February 11, 2005 By: /s/ John G. McLaughlin

John G. McLaughlin
President and Chief Executive Officer
(Chief Executive Officer)

Date February 11, 2005 By: /s/ Phuong Dang

Phuong Dang
Controller (Principal Financial and Accounting Officer)