COMPUTERIZED THERMAL IMAGING INC
Form 10QSB
May 20, 2005

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2005

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

For the transition period from _____ to _____

Commission file number: 001-16253

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

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

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

Check whether the issuer (1) 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 for the past 90 days.
Yes [X] No [ ]

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: Common stock, par value $0.001, of which 114,561,698 shares were issued and outstanding as of April 30, 2005.

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

FORM 10-QSB

QUARTERLY REPORT

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PART I - FINANCIAL INFORMATION

PART I - FINANCIAL INFORMATION
ITEM 1. UNAUDITED FINANCIAL STATEMENTS

COMPUTERIZED THERMAL IMAGING, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 2005	June 30 2004
ASSETS	(Unaudited)	
CURRENT ASSETS:		
Cash and cash equivalents	$ 6,383	$ 168
Accounts receivable-trade, net (less allowance for doubtful accounts of $0 at March 31, 2005 and $3,199 at June 30, 2004)	26,882	53
Accounts receivable-other, net	--	1
Inventories	220,036	260

Prepaid expenses	43,809	91
Total current assets	297,110	575
PROPERTY AND EQUIPMENT, Net	143,676	169
INTANGIBLE ASSETS:		
Intellectual property rights, net (less accumulated amortization of accounts of $19,440 and 17,437 for March 31, 2005 and June 30, 2004, respectively)	13,407	15
TOTAL ASSETS	$ 454,193	$ 760
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
CURRENT LIABILITIES:		
Accounts payable	$ 539,952	$ 512
Accrued liabilities	139,033	172
Short-term Note Payable	230,600	220
Deferred revenues	1,053,490	1,083
Total current liabilities	1,963,075	1,988
LONG-TERM NOTE PAYABLE	112,934	109
TOTAL LIABILITIES	2,076,009	2,097
STOCKHOLDERS' EQUITY (DEFICIT):		
Convertible preferred stock, no par value, 3,000,000 shares authorized; issued-none		
Common stock, $.001 par value, 200,000,000 shares authorized, 114,561,698 issued and outstanding on December 31, 2004 and June 30, 2004	114,562	114
Additional paid-in capital	95,454,274	95,454
Deficit accumulated	(97,190,652)	(96,906
Total stockholders' equity (deficit)	(1,621,816)	(1,337
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)	$ 454,193	$ 760

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

COMPUTERIZED THERMAL IMAGING, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND OTHER COMPREHENSEIVE INCOME (L
(Unaudited)

FOR THE THREE MONTHS ENDED	FOR NINE MON

	MARCH 31,		MARC
	2005	2004	2005
INCOME:			
Product revenues	$ 51,483	$ 54,218	$ 168,513
Service revenues	28,325	53,015	39,802
Total Revenues	79,808	107,233	208,315
Cost of product revenues	(23,212)	(13,444)	(45,734)
Cost of service revenues	--	--	--
Total cost of revenues	(23,212)	(13,444)	(45,734)
GROSS MARGIN	56,596	93,789	162,581
OPERATING EXPENSES:			
Operating, general and administrative	23,878	251,961	278,054
Litigation settlements	--	10,000	--
Research and development	17,118	264,266	108,024
Marketing	(1,685)	45,296	23,755
Depreciation and amortization	10,584	36,000	27,683
Total operating expenses	49,895	607,523	437,516
OPERATING LOSS	6,701	(513,734)	(274,935)
OTHER INCOME (EXPENSE):			
Interest income	4	313	65
Interest expense	(4,535)	(2)	(13,756)
Other	7	200	51
Total other income (expense)	(4,524)	511	(13,640)
NET LOSS	$ 2,177	$ (513,223)	$ (288,575)
WEIGHTED AVERAGE SHARES OUTSTANDING	114,561,698	113,430,471	114,561,698
BASIC AND DILUTED LOSS PER COMMON SHARE	$ 0.00	$ (0.00)	$ (0.00)

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

COMPUTERIZED THERMAL IMAGING, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	FOR THE NINE MONTHS ENDED MARCH 31,	
	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (288,575)	$(2,456,396)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation and amortization	27,685	54,797
Amortization of bond premium (discount)	--	(15,192)
Bad debt expense	--	63,032
Accounts receivable - trade	26,446	328,352
Accounts receivable - other	1,391	--
Inventories	40,295	(27,846)
Prepaid expenses	47,665	118,268
Accounts payable	27,410	(26,985)
Accrued liabilities	(19,337)	(28,279)
Deferred revenues	(29,610)	371,871
Net cash used in operating activities	(166,630)	(1,618,378)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceed from sale of assets	--	22,177
Net cash provided by (used in) investing activities	--	22,177
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock and warrants, net of offering costs	$ --	$ 1,000,000
Net cash provided by financing activities	--	1,000,000
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(166,630)	(596,201)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	168,955	454,387
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 2,325	$ (141,814)
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid for:		
Interest expense	$ --	$ --
Income taxes	--	--
SUPPLEMENTAL SCHEDULE OF NON-CASH FINANCING AND INVESTING ACTIVITIES		
Common stock issued to reduce debenture, interest and penalty	$ --	$ 157,277

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

COMPUTERIZED THERMAL IMAGING, INC.
Notes to Condensed Consolidated Financial Statements
March 31, 2005
(UNAUDITED)

NOTE A. UNAUDITED FINANCIAL STATEMENTS AND BASIS OF PRESENTATION

The condensed consolidated financial statements of Computerized Thermal Imaging (the "Company") for the three-month and six-month periods ended March 31, 2005 and 2004 are unaudited. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the Company's results of operation for the periods presented have been included. These interim statements should be read in conjunction with the audited consolidated financial statements and footnotes thereto contained in the Company's most recent Annual Report on Form 10-KSB for the Year Ended June 30, 2004. The consolidated results of operations for the three-month and nine-month periods ended March 31, 2005 are not necessarily indicative of the results to be expected for the full year.

Certain amounts from the prior period financial statements have been reclassified to conform to current period presentation.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions, including for example, accounts receivable allowances, inventory obsolescence reserves, deferred tax valuation allowances, and reserves for pending or threatened litigation. These assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

The accompanying condensed consolidated financial statements have been prepared assuming the Company will continue as a going concern. In its Annual Report on Form 10-KSB for the Year Ended June 30, 2004, the Company reported that its recurring losses from operations, negative cash flows from operations, the Company's need for additional working capital, and the Company's continuing struggle to obtain FDA approval for its primary product raised substantial doubt about the Company's ability to continue as a going concern. The Company's independent auditors have also expressed their doubts about the Company's ability to continue as a going concern.

In order to pursue its existing plan of operations, the Company will have to secure additional financing through the sale of equity, the incurrence of debt or the sale of assets, including the Company's intellectual property. There can be no assurance that capital will be available from any source or, if available, that the terms and conditions associated with such capital will be acceptable to the Company. If the Company raises equity or debt capital, the sale of these securities could dilute existing shareholders, and borrowings from third parties could result in assets being pledged as collateral and could provide loan terms that could adversely affect the Company's operations and the

price of its common stock.

The accompanying condensed consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary if the Company is unable to continue as a going concern.

NOTE B. REVENUE RECOGNITION

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

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

The Company has adopted the practice of deferring revenue on shipments to distributors until cash payment from the distributor is received by the Company, which is generally when the product is sold by the distributor to the end customer.

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

Service revenue is derived from non-destructive testing of turbine blades and other items as well as service of medical equipment previously sold but not covered by warranty. Service revenue is recognized upon the completion of the services provided. The Company offers extended warranties on certain of its products. Warranty revenue is recognized ratably over the period of the agreement as services are provided.

NOTE C. DEFERRED REVENUE

Deferred revenues at March 31, 2005 was approximately $1,053,996, and consisted of $660,000 of deferred revenues from the NanDa licensing and manufacturing agreement, $4,056 of deferred warranty revenues and $389,940 of deferred industrial revenues and deposits relating the Turbine Blade Inspection System ("TBIS") the Company shipped to Pratt & Whitney. Deferred revenues at June 30, 2004 was approximately $1,083,100, and $660,000 of deferred revenues associated with a manufacturing/licensing agreement between the Company and NanDa Thermal Medical Technology, Inc. ("NanDa"), $7,705 of deferred warranty revenues and $415,395 of deferred industrial revenues and deposits relating primarily to the TBIS the Company shipped to Pratt & Whitney.

DEFERRED REVENUES	MARCH 31, 2005	JUNE 30, 2004
Nanda Licensing	660,000	660,000
Medical Products		3,000
Industrial Products	389,940	496,000
Warranty Revenue	4,056	13,000
Total Deferred Revenue	$ 1,053,996	$ 1,172,000

Industrial products deferred revenue consists of non-destructive testing devices shipped to Pratt & Whitney. The Company anticipates that it will recognize these sales when it has completed its obligations under the purchase agreements with Pratt & Whitney. Although the equipment has been shipped, installed, and is in use the customer awaits a final calibration and test performed on site by the Company. The $389,940 has been paid by Pratt & Whitney. The Company has deferred the full amount of the contract until the final calibration and testing can be performed on customer site. This is in accordance with the Company's revenue recognition policy.

The Company's Manufacturing License Agreement with NanDa (the "NanDa Agreement") is billed in stages. The Company has billed NanDa $660,000 to date and received payment for $660,000. The NanDa Agreement obligates the Company to provide training services for NanDa employees in the United States and in China. The Company has provided the training services for NanDa employees in the United States, but, has yet to train in China. Therefore, according to the Company's revenue recognition policy, the Company will not recognize any revenue from the NanDa Agreement until all its obligations are performed or the NanDa Agreement is deemed to be complete.

NOTE D. INVENTORIES

Inventories are stated at the lower-of-cost or market with cost determined using the first-in first-out method of accounting. As of the dates set forth below, the Company's inventories consisted of the following:

	MARCH 31, 2005	JUNE 30, 2004
Raw materials	$ 577,230	$ 616,508
Inventory reserve	(629,967)	(629,967)
Work-in process	29,379	18,629
Finished goods	243,394	255,161
Total	$ 220,036	$ 260,331

Finished goods inventory at March 31, 2005 consisted of approximately $243,394 of finished goods ready for sale, $29,379 in the manufacturing process and $577,230 of raw materials. In their report on the Company's condensed consolidated financial statements for the year ended June 30, 2004, the Company's independent auditors expressed concern regarding the Company's ability to continue its operations as a going concern. As a result of that concern, coupled with the decision of the U.S. Food and Drug Administration (the "FDA") to deny pre-market approval of the Company's breast imaging system, (the "BCS 2100"), the Company has treated its inventories as impaired assets on its condensed consolidated financial statements for the quarter ended March 31, 2005. The impairment is held in a reserve account and represents about 74% of all inventories.

The Company has in the past reserved for excess and obsolete inventory by comparing inventory on hand to estimated consumption during the next twelve months. Consumption is estimated by annualizing trailing three or six -month sales volumes, adjusting those volumes for known activities and trends, then comparing forecast consumption to quantity on hand. However, the Company evaluates all inventories to determine if the total impaired book value could be recovered if liquidation becomes necessary. The Company felt no need to impair additional inventory in the quarter ended March 31, 2005

NOTE E. INCOME TAXES

The Company accounts for income taxes using the liability method. Under this method, the Company records deferred income taxes to reflect future year tax consequences of temporary differences between the tax basis of assets and liabilities and their financial statement amounts. The Company has reviewed its net deferred tax assets, together with net operating loss carry-forwards, and has provided a valuation allowance to reduce its net deferred tax assets to their net realizable value. Due to the going concern status of the Company there are no deferred tax assets.

NOTE F. CONTINGENCIES

SEC INVESTIGATION

In December 2002, we were requested to provide certain documents to the SEC and the U.S. Department of Justice in connection with an investigation regarding possible violations of the insider trading prohibitions found in the federal securities laws. We have responded to the Commission's requests for copies of documentation, and members of CTI management have provided testimony to the Commission. To date, we have incurred approximately $650,000 in legal costs in complying with these requests. CTI also may be required to indemnify its officers and directors in connection with fees incurred in connection with these investigations. Our efforts to respond to the Commission's requests have required, and in the future may require, significant additional legal expenses, may make fund raising more difficult if not impossible, and will distract management from our day-to-day operations.

INDEMNIFICATION

Under our bylaws and contractual agreements, CTI may be required to indemnify its current and former officers and directors who are parties to litigation or other proceedings by providing legal defense through the CTI attorneys (or reimbursing the parties for their own attorneys) and covering all damages the parties may suffer if the plaintiffs are successful.

OTHER LEGAL PROCEEDINGS

We are involved in certain other litigation matters in the normal course of business which management currently believes are not likely to result in any material adverse effects on our financial position, results of operations, or net cash flows.

NOTE G. RECENT DEVELOPMENTS

On June 30, 2004 the Company filed a "Citizen Petition" with the FDA contending that consideration of the Company's application for pre-market approval was severely and improperly prejudiced because of pervasive bias against the Company by the FDA staff reviewers who improperly undermined the review of the Company's application and ultimately caused the FDA to reject that application. The Company is seeking internal documents within the FDA to determine the basis for the FDA staff's behavior. The full text of the full Citizen Petition and 23 exhibits thereto are available at http://www.fda.gov/ohrms/dockets/dailys/04/july04/070104/04p-0276-cp00001 -toc.htm.

On January 11, 2005 Computerized Thermal Imaging, Inc. entered into a "PREFERRED STOCK ISSUANCE AGREEMENT" with Strategica Management, LLC. (See form 8-K filed with the SEC on January 18, 2005.)

Strategica Management, LLC is a Merchant banking and Financial services company that provides advisory and financial services to its client business. Strategica provides or arranges debt and/ or equity capital and value, and venture partners for clients and provides financial and business advisory services utilizing its relationships and financial expertise for emerging companies. Through their combined experience, Strategica executives have been involved with a variety of debt, equity, mergers, acquisitions and financings in multi-millions of dollars. Strategica is diversified as to industry and geography and is proficient in providing management support, creative financial strategies and sophisticated debt restructurings. (www.strategica.net)

As of date of filing of this statement Strategica Management, LLC has been unable to provide any added value to the Company in either cash or sales contracts.

NOTE H - OTHER REGULATORY MATTERS

The Company has received a Medical Device License from Health Canada to market the BCS 2100 in Canada. In late August 2004, the Company shipped the first BCS 2100 to Ville Marie in Montreal, Canada for a one-to-three month evaluation that may result in a lease of the device at the end of evaluation. Due to the limited resources the Company has been unable to support Ville Marie in their efforts to incorporate the BCS 2100 into their operations. As of filing of this statement Ville Marie continues to possess the BCS 2100.

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

FORWARD-LOOKING STATEMENTS CONCERNING OUR BUSINESS

The following discussion should be read in conjunction with the Condensed Consolidated Financial Statements, the notes thereto and the other

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

OVERVIEW

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

Our current products are the BCS 2100, Photonic Stimulator, Thermal Image Processor ("TIP") and our TBIS. We have historically marketed our products with an internal sales force and through independent distributors. At present, however, due to our troubled financial condition, we are not actively marketing our products with the exception of our web page (www.cti-net.com). To date, our revenues have been generated principally from the sale of our Photonic Stimulator, TIP, TBIS and services provided in connection with our TBIS.

Given our inability to market our principal product unless we secure FDA pre-market approval, our need to raise capital to fund our operations, our history of losses ($97 million since inception), and the risk of pending or future litigation, our independent auditor's opinion dated September 24, 2004 contains a "going concern qualification," meaning that our independent auditors have indicated that there is substantial doubt as to our ability to continue as a going concern. Our efforts to raise additional funds to date have been only marginally successful. Since the FDA's rejection of our application for pre-market approval of the BCS 2100 in December 2002, we have raised $500 thousand in advances under an equity line of credit with Beach Boulevard, $1.32 million through a private issuance of restricted stock, $660 thousand from the NanDa Agreement and $220 thousand from short-term notes. We have pursued additional financing transactions, but, as of the date of this Report, we have been unsuccessful in our efforts to raise additional capital. On January 11, 2005 we entered into a "PREFERRED STOCK ISSUANCE AGREEMENT" with Strategica Management, LLC to assist us in our efforts to raise funds through equity, debt and revenue producing contracts. Strategica's efforts have resulted in no additional cash nor producing contracts. Regardless of the FDA's ultimate decision regarding our application for pre-market approval of the BCS2100, we will require additional capital to execute our operating plan, which may include more clinical trials, research and development, marketing into Canada and marketing and manufacturing expenses.

The following discussion and analysis of our consolidated financial condition and results of operations should be read in conjunction with our audited condensed consolidated financial statements and notes thereto contained in our Annual Report on Form 10-KSB for the fiscal year ended June 30, 2004.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements requires us to estimate the effect of various matters that are inherently uncertain as of the date of the financial statements. Each of these required estimates varies in regard to the level of judgment involved and its potential impact on our reported financial results. Estimates are deemed critical when a different estimate could have reasonably been used or where changes in the estimate are reasonably likely to occur from period to period, and would materially impact our financial condition or results of operations. Our significant accounting policies are discussed in Note 1 of the Notes to Condensed Consolidated Financial Statements. Critical estimates inherent in these accounting policies are discussed in the following paragraphs. Our management has discussed the development and selection of these critical accounting policies with the Audit Committee of our Board of Directors.

CASH AND CASH EQUIVALENTS -- Cash and cash equivalents include cash in checking accounts and short-term highly liquid investments with an original maturity of one year or less.

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

Our standard domestic terms for our medical products to end-user customers are "net 30 days," and our standard international terms for our medical products require payment in cash or placement of a letter of credit before shipment. On occasion, we offer extended payment terms beyond our normal business practices, usually in connection with providing an initial order of demonstration equipment to a new domestic distributor. We consider fees on these extended terms agreements not fixed and collectibility less than probable and defer the revenue until receipt of payment. Our sales prices have declined over time and we credit price decreases to any balance due from a distributor. We sell separate extended warranty contracts for our TIP and Photonic Stimulator and recognize revenue from those arrangements ratably over the contract life. We do not offer rights or return privileges in sales agreements.

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

RESEARCH AND DEVELOPMENT EXPENSES -- We expense as incurred the direct, indirect and purchased research and development costs associated with our products. We believe this method is conservative given the product and market acceptance risk inherent to our products and reduces administrative burden and cost.

IMPAIRMENT OF LONG-LIVED ASSETS -- We follow the provisions of Financial Accounting Standards Board ("FASB") SFAS No. 141, ACCOUNTING FOR THE IMPAIRMENT OF LONG-LIVED ASSETS AND FOR LONG-LIVED ASSETS TO BE DISPOSED OF, which requires that if the sum of the future cash flows expected to result from

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

INVENTORY RESERVES -- We have in the past reserved for excess and obsolete inventory by comparing inventory on hand to estimated consumption during the next twelve months. Consumption is estimated by annualizing trailing three or six-month sales volumes, adjusting those volumes for known activities and trends, then comparing forecast consumption to quantity on hand. However, we evaluate all inventories to determine if the total impaired book value could be recovered if liquidation is necessary. We felt no need to impair additional inventory during the quarter ended March 31, 2005.

TRENDS/UNCERTAINTIES AFFECTING CONTINUING OPERATIONS

We are exposed to the opportunities and risks usually associated with marketing and manufacturing novel products, including staff retention and recruiting, market acceptance of our products, product warranty, bad debts and inventory obsolescence. We expect to earn revenues from the sale of our products, but there is no guarantee that these revenues will recover all the costs of marketing, selling and manufacturing our products.

We have only internet marketing efforts at present due to our current lack of resources. If we are able to acquire additional capital, of which there can be no assurance, we hope to be able to resume marketing efforts by building relationships with manufacturers, medical equipment dealers, physicians and clinical investigators; communicating with our target markets by attending trade shows and conferences, making direct sales calls, and sponsoring clinics in which we could introduce and demonstrate our products. We believe marketing medical products through trade shows, conference presentations, direct mail and inside sales, augmented with dealers, provides a low-cost, high-leverage approach to diagnostic imaging and pain management practitioners.

If resources permit, we hope to be able to organize clinical studies with institutions and practitioners to obtain user feedback and to secure technical papers for training and marketing purposes. These strategies represent a significant investment of time and resources and in the past have provided useful information; however, there can be no guarantee that these strategies will lead to market acceptance of our products.

To date, we have had limited operating revenues from the sale of our products and services ($4 million in total revenues since inception). We cannot provide any assurance that we will achieve profitability in the future. Our immediate priority is to produce revenue by utilizing existing TIP and Photonic Stimulator inventory, then, to expand our market in Canada where we have obtained the necessary licenses for our current product offerings to pursue the U.S. market for our TIP and Photonic Stimulator; and to reconcile issues presented to the FDA in our Citizens Petition. At this time, we are unsure how much time and additional financing we will require to resolve issues with the FDA. We are also unsure about our ability to raise additional financing that will be required to continue our business operations. These uncertainties, among

others, raise doubts about our ability to continue as a going concern.

FACTORS THAT MAY AFFECT FUTURE RESULTS

Our operating results and financial condition are subject to substantial risks and uncertainties. These risks and uncertainties include, but are not limited to, the following:

- Our failure to secure customer contracts for multiple TIP and Photonic Stimulator installations could jeopardize our agreement with our primary ally, Strategica, limiting our ability to fund the minimal sales efforts.

- Our failure to obtain FDA approval of our BCS 2100 would continue to have a material adverse impact on our results of operation and financial condition, and may result in cessation of our operations entirely.

- We have limited revenues from operations and may never have substantial revenue from operations.

- Failure to obtain insurance reimbursement codes for our BCS 2100 may make the BCS 2100 unmarketable, thereby threatening the continued operation of our company and adversely affecting shareholder value.

- We expect to continue to incur losses, deficits, and deficiencies in liquidity for the foreseeable future. Unless we are able to reverse those trends, we will likely be unable to continue our operations.

- We may sell assets or reduce activities to fund operations, which could adversely affect shareholder value.

- The recent volatility in the market price of our common stock could continue and adversely affect shareholder value.

- We could issue preferred stock or sell other securities or other financing instruments, including convertible debt, which could result in significant dilution to existing shareholders.

- We rely on third parties in the development and manufacture of key components for our products. If they fail to perform, product development and/or production could be substantially delayed.

- If we are unsuccessful in preventing others from using our intellectual property, we could lose a competitive advantage. If our intellectual property infringes the rights of other parties, we could incur damages or be forced to cease using marketing or selling those products.

- We do not have product liability insurance; if we are made subject to a products liability claim, whether or not the claim is meritorious, our results of operation and financial condition may be adversely affected.

OTHER FACTORS THAT MAY AFFECT FUTURE RESULTS.

The foregoing factors should be read in conjunction with our audited condensed consolidated financial statements, notes thereto and risk factors set forth in our Annual Report on Form 10-KSB for the fiscal year ended June 30, 2004 (the "Form 10-KSB"). Many of the risks identified above are discussed in greater detail in the Form 10-KSB.

RESULTS OF OPERATIONS

QUARTER ENDED MARCH 31, 2005, COMPARED TO QUARTER ENDED MARCH 31, 2004

REVENUES

Revenues for the three and nine months ended March 31, 2005 decreased $27 and $55 thousand, or 26% and 21%, respectively, from the same period last year of the $107 thousand and $263 thousand to $80 and $208 thousand respectively; $51 thousand (three months) and $169 thousand (nine months) of our revenues resulted from product sales and rental revenue; $24 thousand (three months) and $28 thousand (nine months) from services and repairs of equipment previously sold not under warranty; $4 thousand (three months) and $12 thousand (nine months) was recognition of warranty revenue. The decrease in revenue was primarily attributed to the reduction in sales force and other resources.

There were no unfilled orders as of March 31, 2005 as compared to one unfulfilled order for a TIP camera for $47 thousand as of March 31, 2004.

We recognized $26 thousand (three months) and $61 thousand (nine months), or 33% (three month) and 29% (six month) of total revenue, in foreign sales, consisting primarily of fees generated from the rental of a TIP camera to a Canadian customer in 2004 and repair of an industrial camera in England.

COSTS AND EXPENSES

Gross margins for the three and nine months ended March 31, 2005 were $57 thousand (three months) and $163 thousand (nine months), compared to gross margins of $94 thousand (three months) and $187 thousand (nine months) for the same periods of the prior year or a 40% decrease (three months) and a 13% decrease (nine months). Total cost of goods sold for the three and nine months ended March 31, 2005 was $23 thousand (three months) and $46 thousand (nine months), compared to $13 thousand (three months) and $76 thousand (nine months) for the same periods last year. Gross margin as a percentage of revenue has decreased from 78% to 71% (three months) however, increased from 71% to 87% (nine months).

The increase in gross margin resulted primarily from the significant reduction in our cost of goods sold. Our cost of goods declined for several principal reasons. First, we have dramatically reduced our operations, which has resulted in significantly lower revenues, but has also reduced our cost of goods. Second, in part as a result of our reduced level of operations, we have experienced lower costs of servicing equipment. Third, a change in mix of revenue from product sales to service most recently, service revenue tending to bring higher margins.

We are currently in the process of developing a revised business structure that we believe will enhance revenue through leasing our products and providing services to our customers rather than direct sales.

General and administrative expenses for the three and nine months ended March 31, 2005 were $24 thousand (three months) and $252 thousand (nine months), compared to $278 thousand (three months) and $1,287 thousand (nine months) for the same period last year, a decrease of $228 thousand (three months) and $1,177 thousand (nine months), or 82% (three months) and 91% (nine months). The decrease reflects the reduction in sales as well as the Company's inability to raise capital. The decrease consisted of declines in salary expense ($139 thousand for three months; $298 thousand for nine months), office expense ($16 thousand for three months; $38 thousand for nine months), and professional services and legal expense ($66 thousand for three months; $443 thousand for nine months), insurance expense ($4 thousand for three months; $57 thousand for nine months), travel expenses ($2 thousand for three months; $43 thousand for nine months), rent expenses ($24 thousand decrease for three months; $12 thousand decrease for nine months) and outside labor ($2 thousand for three months; $29 thousand for nine months)

Research and development expenses for the three and nine months ended March 31, 2005 were $17 thousand (three months) and $264 thousand (nine months), compared to $108 thousand (three months) and $927 thousand (nine months) for the same periods last year, a decrease of $91 thousand (three months) and $633 thousand (nine months), or 84% (three months) and 68% (nine months). The reduction in research and development is due to the lack of sales and the company's inability to attract capital funds.

Marketing expenses for the three and nine months ended March 31, 2005 were negative $2 thousand (three months) and $45 thousand (nine months), compared to $23 thousand (three months) and $296 thousand (nine months) for the same periods last year, a decrease of $47 thousand (three months) and $273 thousand (nine months), or 104% (three months) and 92% (nine months), from the same periods last year. Again due to the lack of sales and other resources any marketing efforts have been terminated with the exception of the Company's web site www.cti-net.com.

We continue to seek cash to fund on going operations as well as efforts to pursue FDA approval of our BCS 2100. However, our efforts in the near future will concentrate on leasing and service contracts with strategic customers, which, we believe, will eventually provide us with the cash needed to continue product development and FDA approval. Securing a favorable recommendation from the FDA is critical to obtaining additional capital funding. Due, however, to the delay in FDA response, we have been forced to conserve cash by reducing expenses throughout the Company. We feel it is not wise to continue development of a product that has not yet been approved by the FDA.

Depreciation and amortization expense for the three and six month periods ended March 31, 2005 decreased $25 thousand (three month) and $104 thousand (six month) from $28 thousand (three month) and $132 thousand (six month) to $11 thousand (three month) and $36 thousand (six month), or 71% (three month) and 79% (six month) decrease, compared to the same periods of the prior year. During fiscal 2003, we impaired all assets to reflect possible recovery values due to the concern expressed by our auditors that we may not be able to continue as a going concern. There was no additional impairment in the three and six-month periods ended March 31, 2005.

OPERATING INCOME / LOSS

We recorded an operating income of $7 thousand (three months) and a

operating loss of $514 thousand (nine months) ended March 31, 2005, compared to an operating loss of $275 (three months) and $2.4 million (nine months) ended March 31, 2004. The operating loss improvement of approximately $520 thousand (three months) and $2.2 million (nine months) was due principally to our receipt of revenues resulting from an existing customer's need for repairs and service on previously purchased products, sale of our Photonic Stimulator and reduction of costs due to our current lack of sales and capital funding.

OTHER INCOME

Net interest and other expense for the three and nine month periods ended March 31, 2005 decreased $5 thousand (three months) and $13 thousand (nine months) from the same periods of 2004, from $14 thousand expense (three months) and $1 thousand expense (nine months) to a net expense of $5 thousand (three months) and $1 thousand income (nine months). Interest expense is primarily an accrual of imputed interest on three loans of $100 thousand, $200 thousand and $20 thousand, all to related parties. There was virtually no interest income due to the lack of cash.

NET INCOME/(LOSS)

We recognized no extraordinary gains or losses, therefore, net income and operating income were identical. We also recorded no income taxes or income tax benefit due to the going concern opinion issued by our auditors. Because our future as an on going business is in question our ability to take advantage of a booked tax benefit is also in question. Therefore, no benefit has been recognized. However, we do hope to be able to, in the future, obtain a profitable operational status at which time we could then take advantage of a net operating loss carry-forward for tax purposes.

The net income and loss for the three and nine month periods ended March 31, 2005 resulted in a per share income of less than $0.001 (three months) and loss of less than $0.005 (nine months), compared to a per share loss of less than $0.003 (three months) and $0.02 (nine months) ended March 31, 2004.

LIQUIDITY AND CAPITAL RESOURCES

SOURCES AND USES OF LIQUIDITY

Our sources of funds used for operations have historically come from selling common stock, as well as the issuance and exercise of options and warrants, revenues generated from operations, sales of marketable securities, interest earned from marketable securities available for sale and debt assumption.

For the three and nine month periods ended March 31, 2005 our sole source of cash was from sales and collection of prior sales. We did not generate cash from the sale of equity or issuance of debt during the period. Comparably, during the same periods ended March 31, 2004 we generated $0 (three months) and $1 million (nine months) in cash from the sale of equity (a July 2003 private placement).

Our cash requirements include, but are not limited to, general corporate expenses including employee salaries and benefits, lease payments on office space, legal and accounting fees for litigation and public company reporting requirements, costs of clinical trials and studies and technical support, FDA consulting expenses, procurement of inventory and supply expenses

associated with our efforts to develop, manufacture and market our medical and industrial applications. We have reduced many of these costs in an effort to preserve cash; however, a most of these costs are attributable to activities that are necessary to continue our operations.

Net cash used in operating activities for the nine months ended March 31, 2005 was $167 thousand, compared to $1.6 million use of cash for the nine months ended March 31, 2004. The decrease in cash used in operating activities was primarily a result of our efforts to decrease our expenses and cash outlays and is affected by fluctuations in accounts receivable, accounts payable and accrued expense balances.

As of May 1, 2005, our current monthly expense rate is under $20 thousand; our monthly expense rate at our former full operational level was approximately $1.1 million.

We have no contractual obligations nor commitments as of March 31, 2005. All rentals and leases are on a month-to-month basis.

CAPITAL REQUIREMENTS/PLAN OF OPERATION

Our capital requirements have varied significantly from our estimates and will likely continue to vary from those estimates. Our capital requirements depend upon numerous factors including, but not limited to: a) FDA approval process; b) results of pre-clinical and clinical testing; c) costs of technology; d) time and costs involved in obtaining other regulatory approvals; e) costs of filing, defending and enforcing any patent claims and other intellectual property rights; f) the economic impact of developments in competing technology and our markets; g) competing technological and market developments; h) the terms of any new collaborative, licensing and other arrangements that we may establish; i) litigation costs; and j) costs we incur in responding to inquiries and investigations conducted by the SEC and other governmental entities.

Since inception, we have generated significant losses from operations ($97 million) and, although we have generated some revenues ($3.9 million), we are still a development stage enterprise. We have taken actions to reduce our expenses and cash consumption; however, we expect to incur additional operating losses for the indefinite future. Our working capital requirements in the foreseeable future will depend on a variety of factors and assumptions. In particular, we will need to obtain additional financing through additional equity and/or debt financings or through the sale of assets (including our intellectual property) during fiscal year 2005. If we raise additional funds through the issuance of equity securities or other financing instruments, which are convertible for equity securities, our shareholders may experience significant dilution that would aversely affect the price of our common stock. Furthermore, there can be no assurance that additional financing will be available when needed or at all, or that if available, such financing will be on terms favorable to us or our shareholders. If financing is not available when required or is not available on acceptable terms, we may be required to curtail our operating plan and will likely not be able to continue operations as a going concern.

We do not have sufficient capital to cover: 1) the expected costs of additional clinical studies currently required by the FDA; or 2) the anticipated expense of funding our business plan over the next year. We will not be able to continue our business operations unless we obtain additional capital

immediately. This capital, if obtained, could be generated through issuance of securities, assumption of loans, sale of assets (including our intellectual property); however, we have only limited commitments for any capital infusion, and can give no assurance that we will be able to raise any such capital. Furthermore, our troubled financial condition, as well as the lack of FDA pre-market approval of the BCS2100 have made it difficult if not impossible to raise capital needed to continue our operations. If we are not successful in quickly raising additional capital, we will have to scale back our business plan or discontinue operations.

As of March 31, 2005, we believed that we had sufficient liquidity to sustain current operations for next two months. Our monthly expense rate at that time averaged $20 thousand, we had cash, marketable securities, accounts receivable and pre-paid expenses of approximately $2 thousand and current liabilities (excluding the debenture and deferred revenue) of approximately $912 thousand. On a short-term basis, we believed we would be able to fund our operations with cash on hand and the proceeds of our receivables and current sales activities; however, to fund our operations over the long term (more than 2 months) we believed we would need to raise additional capital or curtail our operation.

ITEM 3. CONTROLS AND PROCEDURES

(a) Based on the evaluation of our "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)) required by paragraph (b) of Rules 13a-15 or 15d-15, our president and our chief financial officer have concluded that, as of June 30, 2004, our disclosure controls and procedures were effective.

(b) We are not presently required to conduct quarterly evaluations of our internal control over financial reporting pursuant to paragraph (d) of Rules 13a-15 or 15d-15 promulgated under the Exchange Act. We are, however, in the process of designing, evaluating and implementing internal controls in anticipation of the date when we will become subject to such evaluation requirements.

PART II -- OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

SEC INVESTIGATION

In December 2002, we were requested to provide certain documents to the SEC and the U.S. Department of Justice in connection with an investigation regarding possible violations of the insider trading prohibitions found in the federal securities laws. We have responded to the Commission's requests for copies of documentation, and members of CTI management have provided testimony to the Commission. To date, we have incurred approximately $650,000 in legal costs in complying with these requests. CTI also may be required to indemnify its officers and directors in connection with fees incurred in connection with these investigations. Our efforts to respond to the Commission's requests have required, and in the future may require, significant additional legal expenses, may make fund raising more difficult if not impossible, and will distract management from our day-to-day operations.

INDEMNIFICATION

Under our bylaws and contractual agreements, CTI may be required to indemnify its current and former officers and directors who are parties to litigation or other proceedings by providing legal defense through the CTI attorneys (or reimbursing the parties for their own attorneys) and covering all damages the parties may suffer if the plaintiffs are successful.

OTHER LEGAL PROCEEDINGS

We are involved in certain other litigation matters in the normal course of business which management currently believes are not likely to result in any material adverse effects on our financial position, results of operations, or net cash flows.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) EXHIBITS

31.1	Certification of Chief Executive Officer
31.2	Certification of Chief Financial Officer
32.1	Certification of Chief Executive Officer
32.2	Certification of Chief Financial Officer

(b) REPORTS ON FORM 8-K (NONE)

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

COMPUTERIZED THERMAL IMAGING, INC.
(Registrant)

/s/Richard V. Secord

Richard V. Secord
Chairman & Chief Executive Officer

May 20, 2005